INFORMED BUDGETEER

FY 1999: AULD LANG SYNE

- As Maxwell Smart would say: "missed it by *that much*." The final figures for fiscal year 1999 won't be released until late October, but using eleven months of actual data and projected figures for September, Senate Budget Committee staff project a $121 billion unified budget surplus for 1999. The projected on-budget deficit is $3 billion - oh so close to balance!

- The $121 billion surplus is essentially what CBO forecast in their summer update – kudos to CBO for such excellent analysis! The OMB summer estimate of the surplus was lower by about $20 billion.

- Total outlays for 1999 are expected to be less than 3 percent over outlays in 1998. Net interest costs have fallen more than 6 percent relative to last year because of the growing unified surplus and lower interest rates. Net interest reached a high of 15.4 percent of total outlays in 1996; interest is project to be 13.8 percent of total outlays in 1999.

- Medicare outlays are also down more than one percent relative to last year, and social security benefit costs have risen only about 3 percent in 1999. Defense outlays are up about 2.5 percent relative to 1998.

- Revenues for 1999 are likely to be up 5.7 percent from last year. Individual income taxes have been particularly strong this year, given the buoyant job market. Corporate tax payments are actually below last year's level, due to the plunge in profits during last year's global financial crisis.

- However, on a more encouraging note, corporate payments have picked up in September in keeping with the reported improvement in profits in 1999. This corporate pick-up should ensure that we hit CBO's summer revenue forecast. It also suggests that the risks to SBC's FY99 forecasts are slightly to the upside.

FY 1999 Totals vs. FY 1998 Totals
($ in billions)

	FY 1998	FY 1999	$ Difference	% Change
Revenues	1722	1821	99	5.7
Outlays	1653	1700	47	2.8
Total Surplus	69	121	- -	- -
On-budget	-30	-3	- -	- -
Off-budget	99	125	- -	- -

NOTE: FY 1999 Numbers are SBC Staff estimates. Details may not add to totals due to rounding.

HOW WILL FLOYD WEIGH IN: THE LAST HURRICANE OF FY 1999?

- Since Hurricane Floyd terrorized most of the east coast last week, and the Congress awaits an emergency request from FEMA for the damage, the *Bulletin* thought it would be interesting to look at past hurricanes and their federal budget costs.

- The most expensive hurricane to hit since 1990 was Georges - - a category 4 hurricane - - which caused damage to 6 states (Alabama, Florida, Louisiana, Mississippi, and Virginia) and Puerto Rico. The total federal budget cost was over $2.4 billion dollars.

- Informed Budgeteers who are planning to build a vacation home will want to know where hurricanes have hit the most often. The states of Florida and North Carolina top the list with five each.

- However Puerto Rico tops the list for total amount received from 1990 -1999. FEMA has obligated over $2.7 billion there, with $2 billion for damage done by Hurricane Georges. Florida is second on the list for total funds at $1.8 billion and North Carolina is third at $652 million.

- It remains to be seen where Hurricane Floyd , a category 4, will fit on this list. At the time of the *Bulletin's* publication, flood waters still had not receded in many places. Of note so far, widespread damage in New Jersey means that state will probably receive disaster funds for the first time since before 1990.

- The Federal Government does subsidize flood insurance for some home owners. Under the emergency program, structures in identified flood- prone areas are eligible for limited amounts of coverage at subsidized rates. However, under the regular flood insurance program, studies are conducted of different flood risks in flood-prone areas to establish actuarial premium rates.

- Even with Georges, Bonnie and Earl hitting the coast in 1998 (the last year actual numbers are available), the National Flood Insurance Fund was self-supporting. Premiums paid into the Fund exceeded pay-outs in 1998 by $450 million. Estimates for 1999 and 2000 predict the same for the Fund, weather permitting of course.

Total FEMA Obligations for Past Hurricanes
(1990-1999, $ in millions)

Hurricane	Year	Category	Total Obligations
Georges	1998	4	2,436
Andrew	1992	4	1,844
Hugo	1989	4	1,334
Fran	1996	3	602
Marilyn	1995	2	496
Hortense	1996	4	292
Iniki	1992	NA	260
Opal	1995	3	197
Val	1991	NA	102
Bob	1991	2	71
Bonnie	1998	3	49
Erin	1995	1	40
Ola	1990	NA	39
Bertha	1996	2	37
Bret	1999	NA	4
Emily	1993	3	3
Earl	1998	2	2

SOURCE: FEMA; NA= Not available or less than 1.

DEBT BUY-BACKS A NICE MANAGEMENT PROBLEM TO HAVE

- The U.S. Treasury has three goals for managing the U.S. debt:

  1. to ensure a sufficient supply of cash to pay obligations;
  2. to ensure that the debt is financed at the lowest cost; and,
  3. to promote efficient capital markets.

- Treasury's debt management goals are the same whether the budget is in deficit or surplus. Balancing the goals, however, has become more of a challenge since the amount of debt held by the public is falling due to recent unified budget surpluses.

- As debt held by the public falls, balancing the goals of lowest cost financing and promoting efficient markets by offering debt instruments with a variety of maturities and yields become more difficult for Treasury.

- Treasury can choose to not issue new debt to replace the maturing debt issue, eliminate a debt instrument, reduce the number of debt instruments in a given auction, or change the auction cycle. They may also try something that hasn't been done since the 1960s - buying back outstanding non-callable debt securities before they mature.

- On August 4, 1999, Secretary Summers announced that Treasury was issuing for public comment proposed rules for carrying out Treasury repurchases of outstanding debt securities. The rules were published in the Federal Register, and Treasury is accepting public comment for a period of 60 days.

- According to Treasury's press releases, the use of buy-backs could allow Treasury to maintain larger issuance sizes, enhancing the liquidity of Treasury's benchmark securities. Over the longer term, this enhanced liquidity should reduce the government's interest expense and promote more efficient capital markets.

- Secondly, debt buy-backs could enhance Treasury's ability to exert control over the maturity structure of Treasury debt. Lastly, buy-backs could be used as a cash management tool, absorbing excess cash in periods such as late April when tax revenues greatly exceed immediate spending needs.

- Are debt buy-backs a costless transaction? Depends on how you look at it. At least some of the debt securities that Treasury would buy back were issued at interest rates higher than today's levels. That means Treasury would have to pay a premium to buy back those securities. The prevailing, yet still evolving, opinion from OMB is that this "premium" would be recorded as an interest outlay in the year the buy-back occurs, and interest savings would be recorded in succeeding years (depending on how long it would have been until the instrument matured).

- Since Treasury buy-backs would be an administrative action and not legislated, the interest costs would not be "scored" as Congressional action (and therefore would not have to be offset) nor would they appear on the pay-as-you-go scorecard. The interest costs would, however, have the effect of reducing the on-budget surplus in the year the buy-back occurred, and increasing the on-budget surplus in succeeding years.

- However, others find it odd that buy-backs of premium securities should be counted in the budget totals at all, since the present value of future interest savings roughly equals the premium. (Indeed, the discounted interest savings actually exceed the cost of the premium by a slight amount.) Thus, a credible argument can be made that the entire buyback transaction should be treated as another means of finance, just like the repayment of matured debt, and perhaps should have no outlay effect at all. This is how Canada scores its current buyback program. However, it is ultimately OMB's decision as to how to account for this transaction.

- Interested budgeteers will be paying close attention to what Treasury says following the 60-day comment period. Will Treasury in fact proceed with buying back outstanding debt? If so, how much, and when? Will the President's budget for 2001 assume Treasury debt buy-backs? How will they be accounted for in the budget? Stay tuned.

Aviation Trust Fund Off Budget? Another Attack on the Budget Process

- This week the *Bulletin* once again addresses the dangers of the House Aviation Investment and Reform Act for the 21st Century (AIR-21). In June, the House passed its FAA Reauthorization bill, a piece of legislation lacking fiscal discipline. AIR-21 would take the Aviation Trust Funds off-budget and, beginning in 2003, would align aviation authorizations with revenues. After attacks from House budget hawks, the House passed a half-measure amendment to AIR-21 that would reduce the discretionary caps by the amount of the freeze baseline for the program.

- Advocates of AIR-21 argue that the bill would protect the aviation tax revenues from being diverted to non-aviation spending, tax relief, or deficit reduction. But faithful *Bulletin* readers will remember that AIR-21 also would continue the general fund contribution to FAA programs. Budgeteers know that this proposal is fiscally irresponsible and undermines the struggle to control spending, reduce taxes, and balance the budget.

- Taking the Aviation Trust Fund off-budget would allow FAA spending to be exempt from all congressional budget control mechanisms and would provide aviation with a level of protection now provided only to Social Security. Important spending control mechanisms such as budget caps, pay-as-you-go rules, and annual congressional oversight and review would no longer apply.

- The off-budget status would reduce management and oversight of the FAA by taking trust fund spending out of the budget process. Placing the FAA and the trust fund on autopilot by locking up funding would result in fewer opportunities to review and effect needed reforms. There would be little leverage to induce the FAA to strive for higher standards of performance.

- CBO had originally estimated that the Committee-passed bill would lower projected surpluses by $43 billion between 2000 and 2004. But a last minute amendment to AIR-21 reduced the discretionary cap in 2001 and 2002 by the amount of current aviation spending in the freeze baseline. AIR-21, however, provides more than $14 billion in spending above a freeze baseline of the FAA between 2000 and 2004. The cap adjustment amendment does not solve AIR-21's problems -- there is no easy offset to pay for AIR-21.

- The *Bulletin* is vehemently opposed to taking aviation trust funds off-budget. Some say that the House is really seeking to impose a new "firewall," similar to that provided to the highway and mass transit accounts of the Highway Trust Fund under TEA-21. This is another flawed option that would result in similar problems. Neither off-budget status nor creation of a firewall are fit to fly.

- The Budget Enforcement Act (BEA) and other budget laws were created to keep runaway spending in check. The *Bulletin* opposes budgetary changes that would make it more difficult to control spending, weaken congressional oversight, create a misleading federal budget, and violate the spirit the of current law.

CALENDAR

October 1: Happy Fiscal New Year!

October 5: As part of the preparation for the 25th Anniversary Hearings, a **staff briefing will be given by Professor Allen Schick**. Dr. Shick was one of the original staff experts who assisted in drafting the Act and is the author of the 1980 classic: Congress and Money: Budgeting, Spending and Taxes. Dirksen 608, 2:30-4:00.

October 19-20: **25th Anniversary of the Congressional Budget Act, Senate Budget Committee Hearings.** In addition to the witnesses announced in the September 13 *Bulletin*, Leon Panetta will be testifying on October 19 as part of the Legislative - Executive Relations panel. Mr. Panetta is a former Chairman of the House Budget Committee, Director of the Office of Management and Budget and White House Chief of Staff.