REPUBLICAN CAUCUS

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THE HOUSE REPUBLICAN BUDGET FOR FISCAL YEAR 2008

(H.Con.Res. 109)

INTRODUCED BY

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COMMITTEE ON THE BUDGET

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This document was prepared by the Republican staff, Committee on the Budget, U.S. House of Representatives.

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INTRODUCTION

SUMMARY

The Republican budget substitute asserts that the question is not *whether* Congress should balance the budget, but *how* balance is achieved. It proceeds from the premise that America works best when Americans are, to the greatest extent possible, freed from the shackles of government; that bigger government means less freedom, smothering ingenuity and creativity; that the individual – exercising liberty coupled with personal responsibility – is the moral and economic backbone of the Nation. It follows from the principle expressed by President Reagan in his first inaugural: "We are a Nation that has a government – not the other way around."

Consequently this budget limits government and promotes a strong economy by adhering to the following guidelines:

- **Balancing the Budget Without Raising Taxes.** The budget continues the tax laws adopted in 2001 and 2003 beyond their scheduled expiration at the end of 2010. Their lowered marginal rates, increased child tax credit, relief from marriage penalties and death taxes, enhanced capital and investment incentives, and all the others, remain in place, without tax increases.

- **Ending the Raid on Social Security.** The budget reaches balance in 2012 *without using excess Social Security payroll tax receipts* – protecting the surplus cash dedicated to Social Security.

- **Reforming Entitlements.** The budget recognizes the mission of the government's entitlement programs cannot be fulfilled without reform; and that the largest entitlements are growing at a rate that is fiscally and economically unsustainable. Therefore the budget begins important reforms necessary to sustain the entitlement programs for future generations.

- **Controlling Annual Spending.** It limits annually appropriated spending by setting priorities – such as fighting terrorism, providing veterans' health care, and supporting medical research – and holding the line elsewhere.

- **Increasing Accountability.** The budget also increases accountability by tightening procedural controls and enhancing transparency with process reforms such as the line item veto, a reserve fund for domestic emergencies, earmark transparency, a pay-as-you-go [PAYGO] rule that emphasizes controlling spending rather than chasing higher spending with higher taxes.

Summary: The Republican Budget for Fiscal Year 2008
(in billions of dollars)

	2008	2009	2010	2011	2012
Total Spending (outlays)	2,894.7	2,969.7	2,974.3	3,055.8	3,082.4
Total Revenue	2,671.1	2,800.5	2,886.3	3,016.4	3,181.9
Surplus/Deficit(-)	-223.6	-169.2	-88.0	-39.5	99.5
Note: Figures may not add due to rounding.					

THE BUDGET RESOLUTION

The functional spending categories in this budget resolution are reorganized to emphasize the principle of federalism and the growing significance of entitlement spending.

- **Federalism.** It distinguishes between spending categories that are, for the most part, intrinsic to the Federal Government – such as national defense, veterans' benefits, Federal law enforcement activities, and so on – and those initiated elsewhere (State and local governments or non-government institutions) and *supported* by the Federal Government. The latter are referred to as "domestic" spending categories.

- **Entitlements.** The format emphasizes the increasingly dominant role of entitlement spending in the Federal budget by grouping together the categories reflecting domestic entitlement spending. These categories exclude the mandatory spending associated with principal Federal activities, such as defense and veterans' benefits.

Budget Resolution Totals
(in billions of dollars)

		2007	2008	2009	2010	2011	2012	2008-12
Summary								
Total Spending	BA	2,812.186	2,921.452	2,920.669	2,973.866	3,105.720	3,169.452	15,091.159
	OT	2,746.838	2,894.667	2,969.721	2,974.347	3,055.843	3,082.411	14,976.989
On-Budget	BA	2,358.834	2,452.253	2,432.323	2,464.843	2,575.993	2,613.919	12,539.331
	OT	2,295.735	2,427.922	2,484.251	2,468.400	2,529.608	2,530.737	12,440.918
Off-Budget	BA	453.352	469.199	488.346	509.023	529.727	555.533	2,551.828
	OT	451.103	466.745	485.470	505.947	526.235	551.674	2,536.071
Revenue								
Total		2,532.848	2,671.086	2,800.486	2,886.307	3,016.355	3,181.942	14,556.176
On-Budget		1,895.262	2,002.088	2,097.634	2,148.718	2,244.002	2,374.337	10,866.779
Off-Budget		637.586	668.998	702.852	737.589	772.353	807.605	3,689.397
Surplus/Deficit(-)								
Total		-213.990	-223.581	-169.235	-88.040	-39.488	99.531	
On-Budget		-400.473	-425.834	-386.617	-319.682	-285.606	-156.400	
Off-Budget		186.483	202.253	217.382	231.642	246.118	255.931	
Debt Subject to Limit (end of year)		5,048	5,285	5,468	5,571	5,624	5,538	
Debt Held by the Public (end of year)		8,933	9,476	9,980	10,419	10,820.	11,106	

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By Function								
Principal Federal Activities (functions 050, 150, 700, 750)								
National Defense	BA	619.363	648.770	584.705	550.790	564.117	579.375	2,927.757
(function 050)	OT	560.462	617.792	626.892	561.384	536.057	525.407	2,867.532
International Affairs	BA	34.790	31.989	32.387	32.199	32.268	32.336	161.179
(function 150)	OT	32.015	31.637	30.263	29.873	29.679	29.774	151.226
Veterans Benefits	BA	73.896	84.493	89.019	92.397	98.286	96.528	460.723
(function 700)	OT	72.342	84.512	89.033	90.798	96.779	94.838	455.960
Admin. of Justice	BA	45.559	45.765	45.471	45.742	45.995	46.198	229.171
(function 750)	OT	44.709	46.432	46.631	46.466	46.323	46.166	232.018
Domestic Discretionary Programs (functions 250-650 discretionary spending)								
	BA	301.811	292.800	295.564	293.278	293.002	293.302	1,467.946
	OT	366.053	369.548	363.600	358.033	351.707	347.325	1,790.213
Major Domestic Entitlements (functions 250-650 mandatory spending)								
Social Security (func-	BA	583.125	610.197	640.959	676.285	714.111	756.562	3,398.114
tion 650 mandatory)	OT	580.841	607.714	638.083	673.209	710.619	752.703	3,382.328
on-budget	BA	19.089	19.644	21.518	23.701	27.009	29.898	121.770
	OT	19.089	19.644	21.518	23.701	27.009	29.898	121.770
off-budget	BA	*564.036*	*590.553*	*619.441*	*652.584*	*687.102*	*726.664*	*3,276.344*
	OT	*561.752*	*588.070*	*616.565*	*649.508*	*683.610*	*722.805*	*3,260.558*
Medicare (function)	BA	360.364	374.888	394.116	409.473	445.312	431.401	2,055.190
570 mandatory)	OT	365.315	374.964	393.804	409.730	445.359	431.057	2,054.914
Medicaid (function	BA	215.507	223.389	235.128	249.592	264.095	279.920	1,252.124
(550 mandatory)	OT	215.912	223.837	236.849	249.840	265.040	281.389	1,256.955
Income Security (func-	BA	310.874	327.076	333.545	341.943	355.686	354.709	1,712.959
tion 600 mandatory.)	OT	308.550	325.432	329.632	338.354	352.150	351.288	1,696.856
Agriculture (function	BA	15.704	14.563	14.416	14.221	13.735	13.332	70.267
350 mandatory)	OT	13.928	13.624	13.652	13.390	13.147	12.916	66.729
Student Loans (func-	BA	12.493	8.008	10.664	11.592	10.526	10.186	50.976
tion 500 mandatory)	OT	11.874	5.251	9.120	9.761	9.897	8.590	42.619
Other Mandatory	BA	65.292	63.536	54.275	52.657	51.015	50.923	272.406
Spending	OT	1.078	-1.539	-2.571	-3.917	-5.457	-4.804	-18.288
on-budget	BA	60.592	61.736	52.175	51.657	51.215	51.223	268.006
	OT	-3.622	-3.339	-4.671	-4.917	-5.257	-4.504	-22.688
off-budget	BA	4.700	1.800	2.100	1.000	-0.200	-0.300	4.400
	OT	4.700	1.800	2.100	1.000	-0.200	-0.300	4.400
Government and Financial Management (functions 800, 900, 920, 950)								
General Government	BA	18.202	17.873	17.844	20.270	17.801	18.264	92.052
(function 800)	OT	18.583	18.353	18.013	20.262	17.649	18.230	92.507
Net Interest	BA	236.411	255.621	264.636	275.558	285.011	291.461	1,372.287
(function 920	OT	236.411	255.521	263.236	270.558	275.011	275.461	1,339.787
Allowances	BA	0.785	6.439	-11.795	-5.709	-0.150	4.167	-7.048
(function 920)	OT	0.755	5.544	-6.242	-6.972	-3.007	1.286	-9.391
Offsetting Receipts	BA	-81.990	-83.955	-80.265	-86.422	-85.090	-89.212	-424.944
(function 950)	OT	-81.990	-83.955	-80.274	-86.422	-85.110	-89.215	-424.976

[Note: Although Social Security is reflected in the table above, the program is off budget and is not reflected in the budget resolution.]

TAX POLICY

MAINTAINING PRO-GROWTH POLICIES

The revenue levels in the Republican budget retain all provisions of the 2001 and 2003 tax laws, with none of the tax increases that would otherwise result from the scheduled expiration of these laws after 31 December 2010. This represents one of the clearest distinctions between the Republican budget and the budget reported by the Democrat majority: the Democrat proposal rhetorically supports these tax provisions; but its actual revenue numbers call for the largest tax increase in American history – $392.5 billion over 5 years – and it relies on that tax hike to achieve balance.

Included among the tax provisions that would be continued in the Republican budget are the following:

- Current marginal tax rates on income.
- The 10-percent bracket for low-income individuals.
- The current $1,000-per child tax credit.
- Relief from the marriage penalty.
- Relief from the death tax.
- The existing reduced rates on capital gains and dividends, to encourage investment in the U.S. economy and higher savings for seniors.

The Republican budget also provides one-year extensions of relief from the alternative minimum tax [AMT], the State and local sales tax deduction, and the research and experimentation tax credit.

BENEFITS OF REPUBLICAN TAX POLICY

None of these provisions is protected in the revenue levels of the base Democrat resolution, despite the fact that millions of Americans have benefitted from tax relief, and these policies have supported sustained economic growth.

As a result of Republican tax policies, this year:

- One hundred thirteen million taxpayers will see their taxes decline by an average of $2,216.
- A family of four earning $40,000 will receive tax relief of $2,052.

- More than 5 million individuals and families will see their income tax liabilities completely eliminated.

- Forty-five million families with children will receive an average tax cut of $2,864.

- Fifteen million elderly individuals will receive average tax relief of $2,934.

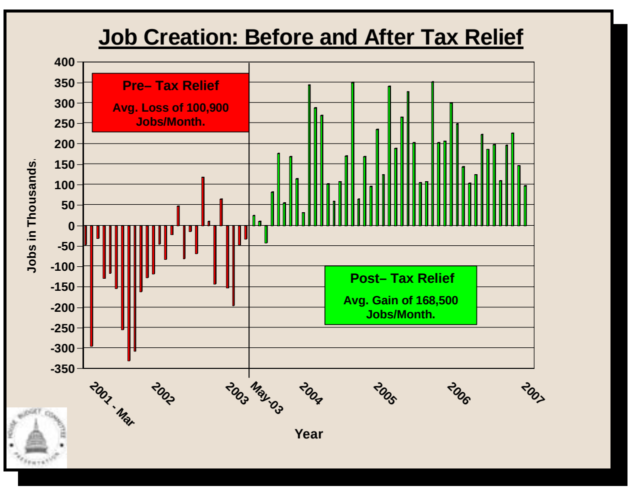
- Twenty-seven million small-business owners will save an average of $4,712.

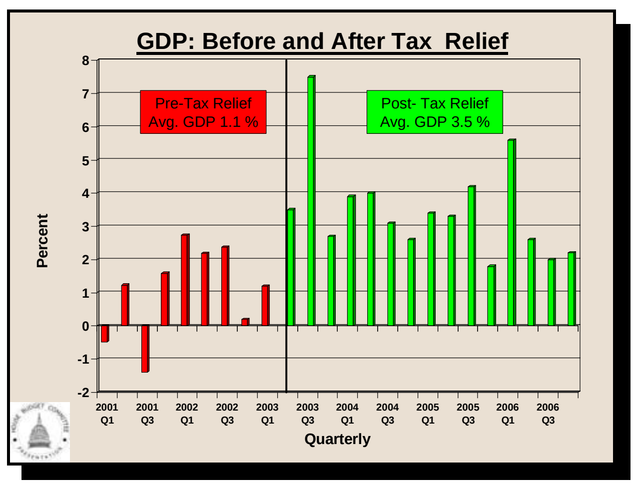
These tax policies also have laid the foundation for sustained economic growth and job creation. The benefits of retaining current tax laws are amply demonstrated by comparing economic performance before and after 2003:

- **Job Growth.** A total of 7.6 million new jobs have been created – an average of 168,500 per month. In the prior 27 months, the economy *lost* 2.7 million jobs – an average of 100,000 jobs lost per month.

- **Unemployment Declines.** The unemployment rate has fallen from 6.1 percent to 4.5 percent.

- **Economic Growth.** In the past 15 quarters, real gross domestic product [GDP] has grown an average of 3.5 percent per year. In the nine prior quarters, average GDP growth was an anemic 1.1 percent.





- **Investment Growth.** Business investment has increased for 15 straight quarters, reversing a previous nine-quarter decline.

- **Stock Market Gains.** Despite recent market corrections, the Dow Jones Industrial Average remains 43 percent above its 2003 level.

These economic gains have yielded significant fiscal benefits as well. Total Federal revenue has increased from 16.5 percent of GDP in 2003 to 18.5 percent this year – *exceeding* the average percentage of the past four decades. Revenue grew by 14.6 percent in 2005, 11.5 percent in 2006, and 9.3 percent in the first five months of fiscal year 2007. This revenue growth has the principal factor in reducing the budget deficit from $412.7 billion in 2004 to an estimated $176 billion this year, according to the Congressional Budget Office.

PRINCIPAL FEDERAL ACTIVITIES

For activities most closely associated with the Federal Government's intrinsic role, the budget provides for the spending levels described below.

NATIONAL DEFENSE
(Function 050)

National Defense includes funds to develop, maintain, and equip the military forces of the United States, and represents the most fundamental responsibility of a Nation's government. More than 95 percent of the funding in this function goes to Department of Defense [DOD] military activities; the remaining funding in the function applies to atomic energy defense activities of the Department of Energy, and other defense-related activities.

The National Defense funding level for 2008 is $645.6 billion. This figure includes both base funding for function 050 and emergency funding for ongoing contingency operations in Iraq and Afghanistan related to the Global War on Terrorism.

The level is equal to the President's request for 2008 and 2009 and assumes an increase both within and above the topline for procurement accounts in 2010 through 2012. These increases are consistent with the request made by the Committee on Armed Services in its *Views and Estimates* to the Committee on the Budget.

The level does not assume the President's increase in TRICARE fees for military retirees under the age 65. The level does, however, assume the President's mandatory savings derived from the sale of the Defense Stockpile.

INTERNATIONAL AFFAIRS
(Function 150)

The conduct of international affairs is a constitutional responsibility of the Federal Government, specifically vested in the President. This category includes international development and humanitarian assistance; international security assistance; the conduct of foreign affairs; foreign information and exchange activities; and international financial programs. The major agencies in this function include the Departments of Agriculture, State and Treasury, the United States Agency for International Development, and the Millennium Challenge Corporation.

The budget holds International Affairs discretionary spending at the 2007 level of $35.6 billion (excluding emergency funding), to fund the Department of State and other diplomatic activities. The budget assumes a small mandatory savings by recouping excessive corporate subsidies for research and development expenses.

VETERANS BENEFITS AND SERVICES
(Function 700)

Veterans' programs represent a unique set of benefits – those earned as a consequence of service in the United States Armed Forces. This category includes funding for the Department of Veterans Affairs [VA], which provides benefits to veterans who meet various eligibility rules. Benefits range from income security for veterans, principally disability compensation and pensions; veterans education, training, and rehabilitation services; hospital and medical care for veterans; and other veterans' benefits and services, such as home loan guarantees. There are approximately 24 million veterans.

The level for 2008 discretionary spending for Veterans is $42.4 billion. This substantial increase over 2007, and over the President's 2008 request, is designed to fully fund the Veterans Health Administration as it prepares to accommodate those injured while waging the Global War on Terrorism. What's more, the budget accommodates a healthy 5-year annual average growth of 7.2 percent, compared to the Democrats' increase of 5.8 percent.

The Veterans Benefits and Services mandatory accounts are funded above the President's 2008 request and reject the President's proposal to impose fees and copays.

ADMINISTRATION OF JUSTICE
(Function 750)

This category supports the majority of Federal justice and law enforcement programs and activities. This includes funding for the Department of Justice; the financial law enforcement activities of the Department of the Treasury; Federal courts and prisons; and criminal justice assistance to State and local governments. Homeland security spending in this function includes funding for the law enforcement and border protection activities of the Department of Homeland Security and the counterterrorism activities of the Departments of Justice and Treasury.

For annually appropriated spending, this budget accommodates $43.7 billion in budget authority. This represents a decrease of $599 million from the fiscal year 2007 level, but is consistent with the amount requested by the President in his budget submission.

The budget also assumes savings from the adoption of medical malpractice reform legislation, under the jurisdiction of the Committee on the Judiciary.

Medical liability and the resulting practice of defensive medicine continue to plague the medical profession in the United States, reducing access for patients, increasing the cost of medical care generally, and increasing the cost of government programs such as Medicare and Medicaid for the U.S. taxpayer. The Congressional Budget Office estimates a Federal cap on non-economic damages ($250,000 per provider and $500,000 per case) would reduce direct spending for Federal health entitlement programs by $2 billion over 5 years. Federal entitlement spending on programs such as Medicare and Medicaid, which represent a growing expenditure of more than $600 billion per year, will only continue to grow without direct action taken by Congress. As the medical liability crisis grows, a large fraction of these dollars will be spent on wasteful health care services provided solely to shield providers from a lawsuits.

Although the savings are recorded here, in function 750, effective medical liability reform contributes to the overall goal of domestic entitlement reform (discussed below), constraining the growth of vital programs such as Medicare and Medicaid and helping to ensure their long-term viability.

DOMESTIC DISCRETIONARY PROGRAMS
(Functions 250-650 Discretionary)

The substitute provides a total of $292.8 billion in annually appropriated fiscal year 2008 budget authority for domestic discretionary spending programs (functions 250-650), which provide varying degrees of Federal support for activities predominantly driven by State and local governments or nongovernment institutions. Among these activities are K-12 education (in function 500); medical research supported through the National Institutes of Health (function 550); community and regional development (function 450); and local transportation activities (in function 400). Homeland security activities also receive support from most of these functional categories here.

The overall amount in this category is part of the total discretionary allocation to the Committee on Appropriations, which will subdivide it among its subcommittees.

The Republican budget proposes a freeze at 2007 levels (excluding emergencies) for domestic discretionary spending. Within this sum, nevertheless, the resolution recommends priority funding in the following areas:

- **Homeland Security (multiple functions).** The budget accommodates the President's requested level for these activities, approximately $3.4 billion over the fiscal year 2007 enacted level. Homeland security activities are spread across a range of functional categories.

- **Medical Research (function 550).** The substitute recommends an increase of $1.3 billion above the President's request for the National Institutes of Health.

- **Community Development Block Grants [CDBGs] (function 450).** The budget provides for an increase above the President's request.

- **Science and Technology (function 250).** The resolution assumes the President's request for science and technology in fiscal year 2008, an increase of $2.4 billion over 2007.

For the past 3 years, Congress has held domestic discretionary spending growth at or below the rate of inflation while still providing funding to critical needs such as homeland security. This policy of spending restraint – coupled with the double-digit revenue increases that have resulted from sturdy economic growth – has yielded significant deficit reduction without tax increases.

This approach contrasts with the profligacy of the new Democrat majority, which has seized every opportunity to increase spending. In their initial fiscal decision of the new Congress, Democrats added $6.1 billion to the current-year (fiscal year 2007) omnibus appropriations bill. Last week, House Democrats added more than $20 billion above the President's request to an emergency supplemental bill for overseas combat operations. Their fiscal year 2008 budget proposes another increase of more than $22.5 billion in nondefense, nonemergency spending – plus a $2-billion increase in "advance appropriations," spending for years after 2008.

Domestic Entitlements

During committee hearings over the past several weeks, a series of expert witnesses testified to the unsustainable growth of entitlement programs – especially Medicare and Medicaid – and the urgent need to begin reform. Among the most significant statements were the following:

- Without "early and meaningful action" to address the rapid growth of entitlements, "the U.S. economy could be seriously weakened, with future generations bearing much of the cost." – *Federal Reserve Chairman Ben S. Bernanke, Budget Committee hearing, 28 February 2007*.

- "Health care is the number one fiscal challenge for the Federal and State governments. . . it is the number one competitiveness challenge for American business; and . . . it is a growing challenge for American families. If there is one thing that can bankrupt America, it is health care. We need dramatic and fundamental reforms."– *Comptroller General David M. Walker, Budget Committee hearing, 23 January 2007*.

- The rising costs of government entitlements are a "fiscal cancer" that threatens "catastrophic consequences for our country" and could "bankrupt America." – *Comptroller General Walker on 60 Minutes, 4 March 2007*.

The facts behind these concerns are well known. Among them are the following:

- Even if taxes were increased by $392.5 billion in the next 5 years, as proposed in the Democrat budget, Federal spending at its current rate will outpace Federal revenue by increasing amounts over the next several decades – mainly due to entitlements, which are growing at an average of 5.2 percent per year – twice as fast as inflation, and faster than the entire economy.

- The principal drivers of this problem are Medicare, currently growing at an average of 5.2 percent per year, and Medicaid, at 7.7 percent per year. Even if the budget were balanced today, these two programs *alone* would drive it right back into deficit. With the forthcoming retirement of the baby boomers, the situation will only get worse.

- The urgency of the problem is further demonstrated by the unfunded liabilities in Medicare and Medicaid, which currently total $52 trillion over the next 75 years. The Medicare share of these liabilities – the dollar amount of benefits promised over the coming decades in excess of projected financial resources – is $32 trillion, and has been growing at about 9 percent per year.

- By 2040, three entitlement programs – Social Security, Medicare, and Medicaid *alone* – will consume 20 percent of the Nation's economy. That is equivalent to the cost of the *entire Federal Government* today; and it will take twice the current rate of taxes *just to maintain the current level of entitlement benefits.*

- In less than a decade, entitlements will take up 62 percent of the entire Federal budget – and they will keep growing until they crowd out all our other spending – including education, science, the environment, agriculture, and even homeland security and defense.

But this challenge is also an *opportunity* – an opportunity to make these programs better, more efficient, more responsive, more sustainable for the future.

Ignoring all of this, however, the Democrat budget puts off any significant reform for at least 5 years – allowing the problem to worsen. Instead, it succumbs to the temptation noted by Senate Budget Committee Chairman Kent Conrad: "It's always easier to defer, to kick the can down the road to avoid making choices." (*60 Minutes, 4 March 2007*.)

The only savings in the Democrat budget are a negligible $75 million reconciled to the Education and Labor Committee (which is merely a lever to get higher education reauthorization considered under reconciliation procedures, and the savings get spent elsewhere anyway); and $410 million in receipts from selling defense commodities such as Tungsten. These are not reforms, and they do nothing to address the massive entitlement problem. In contrast, the Deficit Reduction Act of 2005 saved more than $38 billion over 5 years, and the President's budget for fiscal year 2008 proposed $96 billion in mandatory savings.

The Republican budget, in contrast, tackles the challenge of reforming the government's major entitlement programs to make them better, more responsive, and more flexible; and to improve their alignment with, and sensitivity to, national and global economics. These reforms have the additional benefit of slowing the growth of spending in these programs, making the programs more sustainable for the long term and yielding budgetary savings as well. The reforms moderate the rate of overall mandatory spending growth, to 4.3 percent when the reforms are implemented. This results in savings of $279 billion over 5 years.

The principal reforms are described below.

(Note: Although Social Security is the largest of the domestic entitlements, it is off budget and not reflected in the budget resolution.)

HEALTH ENTITLEMENTS

A major problem for the government's health entitlement spending is the rapid inflation in medical costs. Analysts often describe this effect as if Medicare and Medicaid are helpless bystanders that are simply forced to keep up with these costs. But it is well-known that third-party payment arrangements – especially when the third party is the government – tend to reduce the normal consumer disciplines that help maintain price stability and limit spending growth. Further, under standard economic theory, increased government spending in health care tends to increase demand, which tends to drive prices still higher.

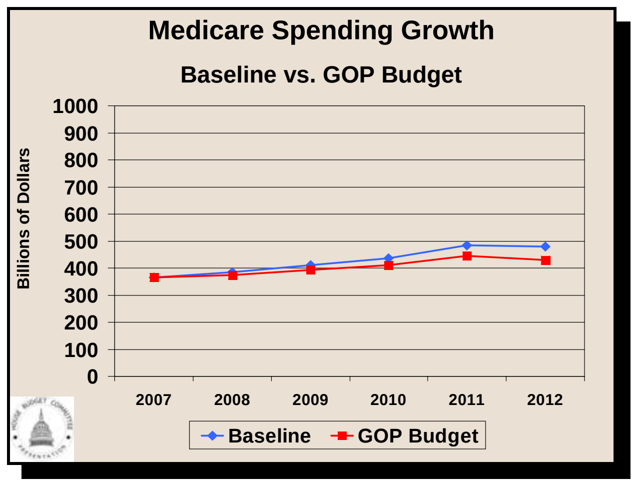
The reform concepts underlying the budget substitute are designed to enhance the efficiency of Medicare and Medicaid spending, moderating their growth rates and reducing their unfunded liabilities. The substitute finances both programs at levels sufficient to continue coverage for qualified beneficiaries, but also enhances their responsiveness to the diversity and vigor of the U.S. medical community.

MEDICARE
(Function 570 Mandatory)

Underlying Medicare's unsustainable spending growth are the rigidity of its benefit and payment structure, its lack of beneficiary control, and its intrusion on the doctor-patient relationship. Benefits and payment levels are determined by well-intentioned policy makers attempting to fit a single, nationalized quasi-insurance plan to more than 44 million enrollees.

Further, the vast reach of Medicare creates benchmarks for other, non-government, health plans, and tends of suppress market vitality throughout the medical community. Hence, enhancing the responsiveness and flexibility of Medicare will not only improve Medicare, but also benefit every other consumer who seeks medical services.

The budget recommends $375.0 billion in outlays for Medicare benefits (function 570 mandatory spending) in fiscal year 2008, and $2.055 trillion in 2008-12. Coupled with these spending levels is a reform strategy that will advance the transformation of Medicare into a vital and flexible program that can meet its mission without imposing unmanageable burdens on the Nation's medical community, and its economy.



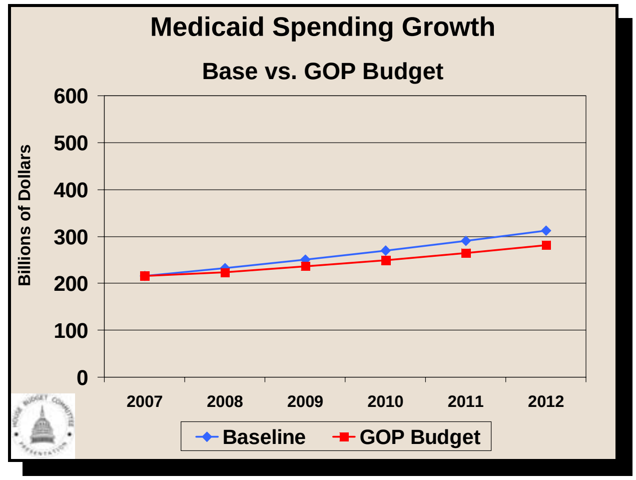
The program structure envisioned in this budget expands protections against catastrophic medical costs; simplifies beneficiary contributions; and increases flexibility for hospitals serving unusually high numbers of low-income patients (known as disproportionate share hospitals [DSH]). These enhancements are coupled with a readjustment of cost-sharing for high-income beneficiaries, and a greater State role in targeting hospital funds. Such reforms would slow the rate of Medicare spending growth to 3.4 percent per year.

MEDICAID/SCHIP AND RELATED PROGRAMS
(Function 550 Mandatory)

The substitute provides outlays of $223.8 billion in fiscal year 2008, and $1.257 trillion over 5 years, for Medicaid, the State Children's Health Insurance Program [SCHIP], and related activities (reflected in function 550 mandatory spending). These levels are coupled with greater State flexibility in program and benefit design.

Although Medicaid is a joint Federal-State program, its structure still limits State flexibility in determining benefits, and reduces States' incentives to maximize the value of benefits purchased with Federal dollars.

Therefore, the substitute envisions reforms such as block granting acute-care benefits to States, enhancing flexibility and sensitivity to spending growth. Such a reform would moderate spending growth to 5.4 percent per year – still greater than medical inflation.



INCOME SECURITY
(Function 600 Mandatory)

Income Security (reflected in function 600) includes the government's income support programs such as Temporary Aid for Needy Families [TANF], Supplemental Security Income [SSI], the Earned Income Credit [EIC], food stamps, Federal employee retirement, and child support, among others. Together, these programs help provide an important safety net for the American people and are essential to maintaining the high standard of living that we enjoy in the United States. At the same time, many of these programs have been growing at a rapid pace in recent years and have deviated from their original purpose of caring for individuals during their time of need and helping them to re-enter the workforce as soon as practicable. To help achieve both of these important objectives, the Republican substitute budget includes numerous positive reforms to the income security programs. These reforms will ensure these programs continue to provide low-income individuals with the safety net they need while at the same time maximizing the ability of these individuals to provide for a better life for themselves and their families.

Overall, the budget funds mandatory income security programs at $325.4 billion in 2008 and $1.697 trillion over the next 5 years (function 600 mandatory spending), including the outlay effects of the refundable portion of the child tax credit. Under the Republican substitute budget, these programs will continue to grow at 2.6 percent over the next 5 years.

Earned Income Credit Reform

The substitute improves the Earned Income Credit by strengthening the program's incentives for recipients to find meaningful employment. In addition, the budget ensures that benefits are targeted to those for whom they were originally intended: workers with children who rely on the benefit to ensure they can stay off of welfare. Finally, the budget proposes to reduce fraud in the program by reserving the benefit for U.S. citizens and legal non-citizen workers and makes other reforms to ensure that the program more accurately reflects the economic realities facing its beneficiaries.

Supplemental Security Income Reforms

The substitute budget proposes to improve the SSI program by reducing fraud and overpayments. For example, it will allow the Social Security Administration [SSA] to fully collect overpayments to beneficiaries, many of which are never recovered today. At the same time, the budget recognizes the potential hardship this policy could place on individuals and allows the SSA Commissioner to lower the rate of recovery of overpayments or waive collection altogether if doing so would support the purposes of the program. The budget also adapts SSI policies to more accurately reflect the economic realities facing its beneficiaries

Food Stamp Reforms

The Republican budget targets food stamp benefits to those who need them the most by reducing fraud, and by helping strengthen the incentive for beneficiaries to return to work. For example, it encourages States to reduce fraud by reducing the administrative matching rate for States whose levels of food stamp fraud remain unacceptably high. The budget also enhances work incentives for certain beneficiaries, promoting self-sufficiency.

Other Reforms

The budget substitute *does not* include the administration's proposal to reform the Pension Benefit Guaranty Corporation [PBGC].

AGRICULTURE
(Function 350 Mandatory)

The budget substitute proposes a reform strategy that enhances market alignment in farm commodity, crop insurance, and agricultural export promotion and credit programs, making them more cost-effective and sustainable. Thus these programs also would use taxpayer dollars more efficiently to support farmers, and make the programs better able to withstand challenges from U.S. trading partners.

HIGHER EDUCATION
(Function 500 Mandatory)

The reauthorization of the Higher Education Act this year provides an opportunity to improve students' options and benefits while strengthening the fiscal integrity of these programs.

In the Deficit Reduction Act [DRA] of 2005, Congress and the President enacted programmatic reforms that significantly increased aid available to student borrowers. The real-time DRA benefits included increased loan limits and lower origination fees. Additional reforms could free up funds to increase benefits to students, while they are in school, and generate savings. Potential reforms could include limiting above-average subsidies to graduate students.

To ensure services and benefits to students are not compromised while the DRA reforms are being implemented – and to maintain the strength of the student loan programs – the substitute rejects the President's proposal to reduce lender subsidies by 50 basis points.

In addition, there remains concern that the student loan program scoring baselines do not accurately indicate true economic costs. This concern was validated by the publication of reports by two different congressional support agencies. Both of the reports – one published by the Congressional Budget Office and the other by the Government Accountability Office – found the subsidy cost estimates calculated under the Credit Reform Act do not fully capture all governmental costs associated with the Direct Loan program. The substitute rejects any proposals that allow questionable savings to be generated by expanding the direct student loan program – especially at the cost of the more efficient guaranteed loan program.

RECONCILIATION

As provided for in the Congressional Budget Act, the substitute amendment provides for a reconciliation bill. It instructs 10 authorizing committees to submit changes in law necessary to achieve the direct spending levels provided for in the substitute, and continue the reform of mandatory spending. These committees must submit their legislative text to the Budget Committee by 8 June 2007.

In this budget, the committees receiving reconciliation instructions, and their required amounts of savings, are as follows:

Spending Reconciliation by Authorizing Committee
(outlays in millions of dollars)

Committee	2008	2012	2008-12
Committee on Agriculture	-452	-3,277	-9,849
Committee on Armed Services	-50	-100	-410
Committee on Education and Labor	-3,456	-400	-4,906
Energy and Commerce	-8,344	-30,602	-97,359
Committee on Financial Services	0	-140	-400
Committee on Foreign Relations	-20	-90	-250
Committee on the Judiciary	-265	-1,010	-3,515
Committee on Natural Resources	-1,507	-535	-4,647
Committee on Transportation and Infrastructure	-460	-1,063	-4,272
Committee on Ways and Means	-10,109	-41,543	-153,122

Any committee receiving a reconciliation directive must change spending by the specified amount, or in the case of revenue, increase or decrease revenue by the specified amount. (The latter instruction is usually, but not always, a directive to the Committee on Ways and Means.) The committees are given a deadline for reporting their legislation, but may achieve their respective amounts of required savings in any manner they choose. When a directive is received, each committee holds a markup as it would on any other bill. The measure is not reported to the

House, but rather is submitted to the Committee on the Budget. The Budget Committee then binds together the submissions of all committees that have received reconciliation directives, and reports them together as a single bill. The Budget Committee may not make any substantive changes in the submitted text.

If only one committee is reconciled to make changes, it reports that measure directly to the House, and does not submit it to the Budget Committee.

POLICY STATEMENTS

The budget also contains the following statements of policy:

TAXES

It is congressional policy that the Federal Government should not raise taxes on American families or reverse the policies that have led to strong growth in the U.S. economy, and the tax laws enacted in 2001 and 2003 should be continued. Congress should move toward balancing the budget by reining in spending.

ENTITLEMENTS

Congress must immediately address the out-of-control growth of entitlement spending that may do substantial harm to the U.S. economy and threaten the standards of living in of future generations. Congress must also commit itself to consider, during this fiscal year, fundamental reform packages to secure the long-term solvency of Medicare, Medicaid, and Social Security.

BUDGET ACCOUNTABILITY

LINE ITEM VETO

The substitute creates a mechanism that provides greater accountability and transparency to the process of spending, adopting provisions of the Legislative Line Item Veto passed by the House in 2006. A summary of the measure is as follows:

- **Line Item Veto Authority.** Within 45 days of the enactment of a law, the President may transmit a special message proposing to cancel any of three classes of budget provisions--an amount of discretionary budget authority, a direct spending item, or a targeted tax benefit. He can transmit up to five special messages per bill (an exception is made for omnibus bills), and there is no limitation on combining the three classes in any given special message.

- **Procedures for Expedited Consideration.** For each transmittal, Congress must introduce a bill (termed an "Approval Bill") reflecting the proposed cancellations, bring that bill to the floor, and have a vote on it. Amendments or motions to strike provisions, or add provisions, are not allowed – it must be an up-or-down vote on the entire list of proposed cancellations.

- **Nature of the Approval Bill.** The approval bill must meet certain conditions. Primary among these is that Congress defines each cancellation that would produce budget authority or outlay savings, or would reduce revenue.

- **Savings Go to Deficit Reduction.** This bill would devote any savings from the Legislative Line Item Veto Act to deficit reduction. It would accomplish this primarily by reducing the limits established in the budget resolution by the amount of any savings.

- **Presidential Deferral Authority.** While Congress considers legislation to permanently cancel or repeal spending and tax provisions, the President may defer discretionary spending or suspend the implementation of direct spending or tax provisions. Those budget provisions may be deferred for no more than 45 calendar days. The President also is authorized to renew a deferral for an additional 45 days.

EARMARK TRANSPARENCY

The budget establishes a point of order against any bill unless the list of congressional earmarks, limited tax benefits, and limited tariff benefits is put in the legislative text of such measure. At present many earmarks are placed in the report accompanying the bill, not in the actual bill. This provision also requires that those earmarks be placed in an easily searchable format on the internet.

EMERGENCY SET-ASIDE FUND

The substitute establishes a set-aside fund that specifically budgets $6.45 billion for domestic emergencies. It authorizes the Chairman of the Budget Committee to release amounts from the set-aside fund for legislation designated as an emergency. For emergency-designated amounts above the level of the set-aside, it requires a Budget Committee vote to approve an adjustment for the additional amounts.

The Budget Committee may also refuse to provide the additional funds if it believes the designated emergencies do not meet the commonly accepted definition of emergency spending. If the committee does not vote to authorize the additional spending, the Budget Committee Chairman may not revise the levels of the set aside fund, and the emergency designation included in a bill has no effect.

The resolution also defines an emergency as an unanticipated situation that requires new budget authority and outlays to prevent the imminent loss of life or property, or in response to the loss of life or property. It also defines “unanticipated as sudden, urgent, unforeseen, and temporary.

The House-passed budget resolution for fiscal year 2007 contained this provision, but the Democrat budget has eliminated it.

PAY-AS-YOU-GO [PAYGO]

The substitute amends the current point of order against legislation that increases the deficit. It makes it out of order to consider any direct spending legislation, excluding the impact of any revenue provisions, that would increase the on-budget deficit or cause an on-budget deficit the following time periods: the current fiscal year; the budget year; the period of the 5 fiscal years following the current fiscal year; the period of the 5 fiscal years following the those 5 years.

DISCRETIONARY SPENDING LIMITS

The budget establishes discretionary spending limits in the House through 2010. The caps would act as an additional control over discretionary spending provided by annual appropriation bills.

ADDITIONAL PROCESS AND ENFORCEMENT PROVISIONS

- **Advance Appropriations.** The budget continues to cap advance appropriations at $23.565 billion.

- **Overseas Designation.** It exempts, from budget enforcement controls, spending for contingency operations related to the global war on terrorism, and for unanticipated defense-related needs.

- **Repeal of the ‘Gephardt Rule.’** The substitute requires a direct vote to increase the debt limit, rather than the current method whereby an increase in the limit is triggered indirectly by the adoption of a budget resolution.

- **Budget Compliance Statements.** The budget requires the Committee on the Budget to place in each committee report on legislation whether a reported bill complies with the Congressional Budget Act.

- **Cost Estimates.** It requires Congressional Budget Office cost estimates for conference reports and unreported measures.

- **Roll Call Votes for New Spending.** It requires a roll call vote for any bill that seeks to spend or authorize more than $50 million.