

November 1988

DEFICIT
REDUCTIONS FOR
FISCAL YEAR 1989

Compliance With the
Balanced Budget and
Emergency Deficit
Control Act of 1985





**United States
General Accounting Office
Washington, D.C. 20548**

**Comptroller General
of the United States**

B-221498

November 15, 1988

The President
The President of the Senate
The Speaker of the House
of Representatives

I hereby submit my report for fiscal year 1989 as required by section 253 of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended. Section 253 requires that the Comptroller General review the reports prepared by the Director of the Office of Management and Budget (OMB) under section 251 of the act and the orders issued by the President under section 252 of the act, and render an opinion on whether the act's requirements regarding the reports and orders have been met. Section 253 also states that the Comptroller General may provide recommendations to improve the procedures of the act.

The act requires that OMB follow a complex set of procedures and rules to project deficit levels and, in the event that OMB projects a deficit in excess of the amount permitted by the act, to determine the amount and distribution of the sequestering (withdrawal) of budgetary resources. The act also requires that the President, based on OMB's projections, issue appropriate orders.

We are of the opinion that, notwithstanding a few matters discussed in appendix II, OMB's reports and the President's orders substantially complied with the act's requirements. We note, however, that compliance by OMB and the President with the provisions of the act does not necessarily signify substantial progress in reducing the deficit. We therefore discuss below the more fundamental need for a new foundation for budgeting and reducing the deficit in the federal government.

Objectives, Scope, and Methodology

The primary objective of our review was to determine whether OMB and the President complied with the act's requirements in their reports and orders of August 25 and October 15, 1988. Our work entailed a variety of tests and interviews to determine whether the procedures and rules imposed by the act were followed. We focused on assessing compliance with the act's provisions which pertain to deficit projections for fiscal year 1989.

Our review did not encompass an assessment of the validity or reasonableness of the economic and technical assumptions made by OMB in its

Effective Deficit Reduction Requires a Different Approach

In our judgment, 4 years of experience with the Balanced Budget and Emergency Deficit Control Act of 1985 have demonstrated that we cannot reach a balanced budget through the sequestering process as presently structured. The act has helped curb the growth of the deficit, but, in its present form, the act is insufficient by itself to bring about the intended deficit reduction objective.

The inability of the act's procedures to achieve the intended objective flows from the fact that about three-quarters of the budget is exempt from a sequester. In certain cases—such as interest on the national debt and payments under some existing contracts—the exemption is unavoidable. In another example, the President's authority to exempt military personnel costs from a sequester reflects concern for national security. In still other cases—such as Social Security and other retirement programs—the exemptions represent a consensus that certain benefits should be protected.

We do not challenge the judgments underlying these exemptions. However, as a result of them, too little of the budget remains subject to sequestering for that procedure to yield substantial deficit reduction, other than by cuts that would effectively dismantle essential functions of government. The 1987 amendments to the act, which lengthened the deficit reduction schedule, and the subsequent "budget summit" agreement in 1987, which produced legislation setting aside the sequester for fiscal year 1988 and substituting a different deficit reduction package, showed that such disruption of governmental functions was unacceptable to the President, the Congress, and the American people.

Furthermore, experience in prior years has shown that attempting to meet a year's deficit target exclusively by actions on the spending side of the budget, through a significant sequester, has resulted in the use of budgetary devices such as deferring year-end paydays to the following fiscal year and selling government assets. The act will encourage the use of other such devices in the future, which will only compound the deficit problem.

In view of the modest results to date under the act and the equally modest prospects for the future, we believe that the new President and the new Congress should reexamine the approach to deficit reduction embodied in the act. A new foundation for budgeting is needed. Towards that aim, we believe that there are sound lessons to be learned from the budgeting approach seen in the November 1987 White House-Congress budget summit negotiations and agreement. In two forthcoming GAO

Compliance Matters

We identified several accounts where we believe that OMB misapplied provisions of the act. We note, however, that the errors, in the final analysis, did not affect OMB's calculation of the amount of the projected deficit for fiscal year 1989. They primarily related to OMB's classification of certain accounts, or portions thereof, as sequestrable or exempt. Such classification matters would have been of immediate importance had OMB's final report identified the need for a sequestration. If that had happened, it would have been important to have amounts properly classified for purposes of calculating the sequestration percentages and identifying the amounts against which a sequestration would be applied. Absent a sequestration at this time, the compliance problems we have identified are important only insofar as they could distort future sequestration calculations unless corrected by OMB.

Those various compliance matters with possible future importance are discussed below.

Ongoing Compliance Problems

We reiterate our disagreement with OMB's continuing treatment of two accounts, the Railroad Retirement Board's Supplemental Annuity Pension Fund (60-8012-0-7-602) and the Corporation for Public Broadcasting's Public Broadcasting Fund (20-0151-0-1-503). For the same reasons we discussed in our compliance report last year,² we believe that the Supplemental Annuity Pension Fund should be treated as exempt and that no potential outlay savings from a possible sequestration should be indicated for the Public Broadcasting Fund, if the account has already properly obligated its funds, as was the case at the time of OMB's second report.

Other Compliance Matters

In addition, our initial review of eight other accounts indicated that OMB either misclassified an account, or part thereof, as sequestrable or exempt, or listed an incorrect level of sequestrable budgetary resources. Neither problem affected the deficit calculations for fiscal year 1989.

In these eight cases, our views corresponded with CBO's treatment of the accounts in its reports issued under the act. In seven of the eight cases,

²Deficit Reductions for Fiscal Year 1988: Compliance With the Balanced Budget and Emergency Deficit Control Act of 1985 (GAO/OCG-88-1, December 15, 1987).

Requests for copies of GAO reports should be sent to:

U.S. General Accounting Office
Post Office Box 6015
Gaithersburg, Maryland 20877

Telephone 202-275-6241

The first five copies of each report are free. Additional copies are \$2.00 each.

There is a 25% discount on orders for 100 or more copies mailed to a single address.

Orders must be prepaid by cash or by check or money order made out to the Superintendent of Documents.

the OMB examiners we talked to agreed that CBO's treatment was correct. The seven accounts are the following:

- Government Printing Office Revolving Fund (04-4505-0-4-808),
- Tax Court Independent Counsel (23-5023-0-2-752),
- The Department of the Interior's Miscellaneous Trust Fund (14-9971-0-7-302),
- The Department of the Interior's Revolving Funds for Loans (14-4409-0-3-452),
- Payments to the Farm Credit System Financial Assistance Corporation (20-1850-0-1-351),
- Bureau of Engraving and Printing Fund (20-4502-0-4-803), and
- The Federal Emergency Management Agency's National Insurance Development Fund (58-4235-0-3-451).

The eighth case involved the Department of Transportation's Regional Rail Reorganization Program (69-4100-0-3-401). The OMB examiner stated that the matter was under review at OMB, and we note that the amount in question was so small (\$540,000) as to be immaterial.

Additional Material on Objectives, Scope, and Methodology

We conducted a variety of tests and interviews to determine whether OMB and the President complied with the provisions of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended. We reviewed OMB's outlay rates to see whether the aggregate outlay rates for sequestrable discretionary resources were, as required by the act, within one-half of one percent of the rates in OMB's report last year. We also examined the outlays projected for certain Medicare activities to see whether, as required, they did not differ by more than one percent from OMB's February 1988 current services projection (for fiscal year 1989) for the same activities.

Because OMB's first report this year, dated August 25, 1988, was issued before most regular appropriation bills for 1989 had been enacted, we examined a sample of accounts to ensure that OMB used the required inflation rate for developing, from fiscal year 1988 levels of budgetary resources, a projection of 1989 resources and outlays. Since all of the appropriation bills had been signed prior to OMB's October 15, 1988, report, we did not have to perform this test for the final report.

The act essentially required that OMB, in making its projections for 1989, use the same economic and technical assumptions that it used in the President's mid-session budget report, issued on July 28, 1988. We therefore compared OMB's reports with the President's mid-session report to see if the mid-session assumptions were used.

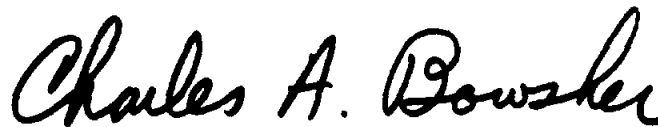
We also compared the OMB reports with those issued a few days earlier by CBO. We examined each case where there was a difference of \$5 million or more between OMB's estimate of sequestrable resources and that of CBO. We also examined certain other cases that came to our attention. The results of this work brought to light some matters that would be relevant only if a sequestration occurs in the future (as discussed in appendix II).

Finally, we interviewed majority and minority staff members of the key budget-related committees of the Congress to elicit their views on compliance issues and also discussed compliance issues with officials of OMB, CBO, and selected agencies. We also used these interviews to identify problems and possible improvements in the act's procedures.

Our work was conducted in Washington, D.C., mainly between August 25, 1988 (the date of OMB's first report), and November 4, 1988.

“Transition Series” reports, we set forth our budget proposals incorporating key features of the budget summit experience, our views on restructuring the existing budget to make it more useful for deficit reduction and other budgetary decisions, and related proposals to strengthen financial management at the central and agency levels in the government.¹

Copies of this report will be provided to the Director of the Office of Management and Budget, the Director of the Congressional Budget Office, and interested congressional committees. Copies will be made available to other interested parties on request.



Charles A. Bowsher
Comptroller General
of the United States

¹Transition Series: The Budget Deficit, (GAO/OCG-89-1TR) and Transition Series: Financial Management Issues, (GAO/OCG-89-7TR).

deficit projection. Accordingly, we do not render an opinion on the accuracy of OMB's estimates of revenues, outlays, and the deficit.

Unlike OMB's reports last year, OMB's reports this year did not project a deficit excess which would require a sequester, and, therefore, we did not address any sequester calculations in our compliance work this year.

The secondary objective of our work was to identify possible ways to improve the procedures of the act. We approached this by evaluating the results of our own work and through interviews with governmental officials who have expertise in the budget process. Appendix I provides more detailed information on our methodology.

Results

These tests and interviews gave us reasonable assurance that OMB and the President substantially complied with the legally prescribed procedures and rules. We believe that OMB misapplied the act's provisions to a few accounts. However, these matters, in the final analysis, did not affect the amount of OMB's deficit projection for fiscal year 1989. The errors were mainly of a type that would be important only if OMB's final report had identified the need for sequestering—for example, misclassifications of accounts as sequestrable or exempt. Appendix II contains more detailed information on these compliance matters.

During our review, participants in the budget process told us about the problems which they perceived in the operation and effects of the act. Concerns were raised about the act's constraints on outlay rates; its budget baseline, added to an already confusing set of budget projections; its report-timing requirements; and its failure to address the deficit implications of legislation enacted after the final OMB report. On the last point, we observed that in the week following OMB's final report, legislation was passed (and eventually signed) that, according to Congressional Budget Office (CBO) estimates, will add approximately \$500 million to the deficit for fiscal year 1989.

Although it would be possible to address these matters by amending the act, we found no convincing evidence that this would contribute materially to the achievement of the act's objective of a balanced budget by fiscal year 1993. Accordingly, rather than making recommendations on improving the act's procedures, we are suggesting a different deficit reduction approach.

