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The Option of Freezing Non-defense Discretionary Spending to Reduce the Budget Deficit

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Summary

Congressional concern over the size of the federal budget deficit has prompted calls for a reduction in federal expenditures. One proposal would freeze non-defense discretionary funding at its FY2005 level. Since non-defense discretionary outlays constitute slightly under 20% of overall federal outlays, limiting their growth would produce a modest reduction in the federal budget deficit. Congressional Budget Office (CBO) estimates indicate that freezing non-defense discretionary funding at its FY2005 level would produce a cumulative savings of approximately \$147 billion including reduced interest payments over the FY2006 to FY2010 time period. These savings would reduce the cumulative baseline budget deficit by approximately 12% over the period. This report will not be updated.

The Congressional Budget Office's (CBO's) FY2006 budget report shows a large estimated baseline deficit, \$295 billion in FY2006, followed by declining deficits in subsequent years. Legislative language directs how CBO is to produce its baseline estimates, such that they "estimate the future paths of federal revenues and spending under current laws and policies."¹ Hence these baseline projections of budget deficits do not include future policy changes, no matter how likely they are to be adopted by Congress. Examples of such policy changes might include continued funding for the

¹ CBO, *Budget and Economic Outlook: Fiscal Years 2006-2015*, p. xiii.

ongoing war on terrorism (including activities in Afghanistan and Iraq); extending certain expiring tax provisions; and adjusting the alternative minimum tax (AMT) for individuals.

When the cost of such policy changes is included in the estimates, the budget deficit grows rather than shrinks after FY2006.² The prospect of large budget deficits extending far into the future has prompted calls for a reduction in federal expenditures. One proposal for limiting future spending growth would freeze non-defense discretionary funding at the FY2005 level. Even if non-defense discretionary spending is held constant, other spending, receipts, and the economy continue growing. Nondefense discretionary spending would decline as a share of total expenditures, as a percentage of GDP, in constant (inflation adjusted) dollars, and per capita. Within a few years of the freeze, non-defense discretionary spending would fall to unprecedentedly low post-World-War-II levels by all these measures.

As can be seen in **Table 1**, non-defense discretionary outlays accounted for 19.3% of total outlays in FY2004. Although non-defense discretionary outlays have increased over the last decade, from 17.7% to 19.3% of total outlays, they still represent less than \$1 out of every \$5 the federal government spends.

In contrast, mandatory spending and net interest payments currently account for almost 61% of total outlays. Their percentage of total budget outlays is expected to increase over the next few years as Social Security and Medicare expenditures rise in response to demographic changes and medical cost pressures and as net interest payments rise as a result of a growing federal debt.

Discretionary Spending

The Congressional Budget Office defines federal discretionary spending as budget authority that is provided and controlled by appropriation acts and the outlays that result from the budget authority. Hence, the discretionary spending level can be changed through the appropriations process.

Mandatory spending is budget authority provided and controlled by laws other than appropriation acts and the outlays that result from the budget authority. Hence, mandatory spending can be altered only through changes in substantive law.

Non-defense discretionary spending includes, among other things, funding for the FBI, the National Park Service, the National Institutes of Health, NASA, most federal education programs, a broad array of agricultural programs, the Centers for Disease Control and Prevention, EPA, transportation, most homeland security, and most other

² See CRS Report RS22045, *Baseline Budget Projections Under Alternative Assumptions*, by Gregg Eisenwein and Marc Labonte.

Table 1. Components of Federal Outlays FY1994-FY2004

(as percentage of total outlays)

Fiscal Year	Mandatory Spending	Net Interest	Discretionary	
			Defense	Non-defense
1994	49.1%	13.9%	19.3%	17.7%
1995	48.7	15.3	18.0	17.9
1996	50.4	15.4	17.0	17.1
1997	50.6	15.2	17.0	17.2
1998	52.0	14.6	16.4	17.1
1999	52.9	13.5	16.2	17.4
2000	53.2	12.5	16.5	17.9
2001	54.1	11.1	16.4	18.4
2002	55.0	8.5	17.4	19.2
2003	54.7	7.1	18.7	19.5
2004	53.9	7.0	19.8	19.3

Source: OMB, *Budget of the United States Government for Fiscal Year 2006, Historical Tables*, Feb. 2005, Table 8.3.

CBO provides estimates of the annual budgetary effects of a selection of alternative policy scenarios.³ One of these scenarios is that discretionary non-defense funding is frozen at FY2005 levels. The dollar difference between the baseline paths for nondefense discretionary spending and the one assuming a funding freeze produces an estimate of the savings resulting from freezing discretionary spending. **Table 2** contains this measurement (calculated from CBO data) from freezing non-defense discretionary outlays at their FY2005 levels.

The savings from freezing non-defense discretionary outlays begin relatively small, \$7 billion in FY2006, and grow to \$51 billion in FY2010. The cumulative savings over the FY2006 to FY2010 period are approximately \$141 billion (excluding interest payment savings).

Table 2. Freeze Calculations, FY2005-FY2010

(in billions of dollars; outlays)

FY	Non-defense Discretionary (A)	Non-defense Discretionary Funding Frozen at FY2005 Levels (B)	Non-defense Discretionary Savings (A-B)	Net Interest Savings	Total Savings from Freezing Non-defense Discretionary Outlays
2005	\$466	\$466	\$0	\$0	\$0
2006	476	469	7	0	7
2007	485	468	17	1	18
2008	493	466	27	2	29
2009	502	463	39	4	43
2010	511	460	51	6	57
Cumulative Totals, FY2006-FY2010			141	13	154

Source: CBO, *Budget and Economic Outlook: Fiscal Years 2006-2015*, Jan. 2005. CRS calculations.

³ See pp. 7-9 in the CBO report *The Budget and Economic Outlook: Fiscal Years 2006-2015*, Jan. 2005.

However, because freezing non-defense discretionary spending reduces the size of the expected deficit, which in turn slows increases in federal debt held by the public, net interest payments will be smaller than they otherwise would be during this period. The estimated savings in net interest payments from freezing non-defense discretionary spending grow from \$1 billion in FY2007 to \$6 billion in FY2010. The cumulative net interest savings are \$13 billion.⁴ Hence, the estimated total deficit reduction from freezing non-defense discretionary outlays would be \$154 billion over the period.

The CBO baseline budget deficit projection for the FY2005 through FY2010 period is shown in **Table 3**. As mentioned earlier, it seems very likely that an alternative deficit estimate that includes likely future action, such as additional expenditures for the Iraq and Afghanistan campaigns and the extension of at least some if not all of the expiring tax provisions, would make the deficit estimates larger.

Table 3. CBO Baseline Deficit Projections

(in billions of dollars)

Fiscal Year	2005	2006	2007	2008	2009	2010	Cumulative Total
Deficit	-\$365	-\$298	-\$268	-\$246	-\$219	-\$201	-\$1,232

Source: CBO, *An Analysis of the President's Budgetary Proposals for Fiscal Year 2006*, March 2005.

The cumulative baseline budget deficit estimate over the FY2005 to FY2010 period is \$1.2 trillion. The savings in both outlays and debt service payments from freezing non-defense discretionary outlays at their FY2005 levels is \$147 billion over the same period. This would produce a cumulative reduction in the baseline budget deficit of just over 12%.

⁴ This report assumes that approximately half of the debt-service adjustment associated with CBO's projection of freezing all discretionary funding at FY2004 levels would accrue if the freeze in funding was limited solely to non-defense discretionary funding.