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BUDGET ISSUES

Trust Funds in the Budget

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Mr. Chairman, Members of the Subcommittee:

It is a pleasure to appear here today to talk about budget accounting and budget enforcement as they relate to trust funds and other special funds in the budget. As requested, my statement today will discuss three areas: (1) the structure of the federal budget—especially categorizations within the unified budget, (2) the budget outlook, discretionary caps, and enforcement situation as we enter a projected era of unified budget surpluses, and (3) potential implications of changes in the treatment of the aviation programs.

Budget Structure

The unified budget was adopted in 1969 as a way of capturing all federal receipts and expenditures. This was seen as important to permit the federal budget to be used as an instrument of economic/fiscal policy. In addition, if the budget is to help the Congress and the President allocate federal resources, it should cover all activities and transactions that are federal in nature and not subject to the economic disciplines of the marketplace. Removing something that is federal in nature from the budget does not make it less a government activity. If relevant activities of the budget are omitted, the budget presents an incomplete picture of the true magnitude of the federal government's activities. Equally important, the budget display needs to show distinctions between types of federal programs and the information necessary for evaluating the budget year and future years. Such a balance between a unified overview and sufficient compositional information ensures that programs included in the budget are subject to the kind of priority-setting and oversight deliberations the Congress must make during the budget and appropriations debate.

As all of you know, the Congress provides funds to agencies through budget accounts. These accounts vary in their orientation, specificity, and size.¹ A relatively few large accounts are associated with three-quarters of budgetary resources, and the rest are comparatively quite small. Accounts may be oriented to program, process, organization, or object—and more than one orientation is likely to be found in a given agency. For example, the Federal Aviation Administration (FAA) has four major budget accounts covering funding for airport grants, operations, capital improvements, and research and development.

¹Budget Account Structure: A Descriptive Overview (GAO/AIMD-95-179, September 18, 1995).

The Congress has also recognized the variation among federal programs and activities in how it provides funding to these activities. For example, because the school year and the fiscal year do not match, the Congress generally advance-funds education programs so that the school year begins with funding for the first quarter in place. Some funds expire in 1 year if not obligated; others are available for several years, and some are permanently available for obligation.

What Is a Trust Fund? How Do Trust Funds Fit Into the Federal Budget?

The federal budget consists of several types of funds: the general fund, special funds, public enterprise funds, intragovernmental funds, and trust funds.² All of these except trust funds are considered to be “federal funds.” All unified budget transactions fall within either of two fund groups: (1) federal funds and (2) trust funds.

Although some budget summary tables show only 12 major trust funds, in fiscal year 1997 there were 110 trust funds.³ These covered a wide range of purposes: from social insurance (social security and medicare), employee compensation (pensions and health benefits), insurance, natural resources and environmental cleanup to transportation. Social Security is by far the largest trust fund, followed by federal employee retirement funds (civilian and military) and the medicare trust funds.

The term “trust fund” as used in the federal budget is neither the same as a private trust fund nor does it have unique characteristics within the federal budget. The manager of a private trust has a fiduciary obligation to the beneficiary and must manage the trust’s assets on behalf of that beneficiary according to the stipulations of the trust. The manager cannot unilaterally alter the terms of that trust. In contrast, the federal government both owns the assets of most trust funds and can, through legislation, raise or lower the fund’s collections or payments, or alter the purposes of the trust fund.⁴

²There are both revolving and nonrevolving trust funds, but that difference is not relevant to this analysis.

³This is based on the Congressional Research Service report Federal Trust Funds: How Many, How Big, and What Are They For?, updated June 30, 1998.

⁴The federal government manages some trust funds in a fiduciary capacity, such as trust funds owned by Indian tribes. These are not discussed in this testimony.

Within the federal budget there is no substantive difference between a trust fund and a special fund. Both are internal accounting devices used to track the collection and use of funds earmarked for specific purposes. The only difference between a “special” fund and a “trust fund” is the word “trust” in the legislation establishing the account.

If a trust/special fund collects more in receipts than it spends in a year, its annual surplus adds to the unified budget surplus—or reduces the unified deficit if it spends more than it receives. For example, for fiscal year 1998, within the unified budget’s \$70 billion surplus, a federal funds deficit of \$83 billion was offset by a Social Security Trust Funds surplus of \$99 billion and other trust fund surpluses of \$54 billion. Even these surplus figures, however, can be misleading since a significant portion of trust fund revenue comes from transfers within the budget. The largest of these general fund transfers is interest credited to the trust funds. Interest is credited to a trust fund because under current law trust funds “lend” any annual cash surpluses to the general fund.⁵ These surpluses are commingled with other revenues and used to finance other governmental activities. While all of these general fund transfers were instituted for a purpose—often to better allocate costs—the fact remains that they are *intragovernmental* transfers. Without such transfers, the trust funds as a whole would run a deficit.

How Do Trust Funds Fit Into the Budget Enforcement Regime?

The Budget Enforcement Act⁶ (BEA) established a budgetary control regime that divided the budget into two major parts: discretionary spending, defined as spending that stems from annual appropriations acts, and direct spending, or spending that flows directly from authorizing legislation; this latter is often known as mandatory. As all of you know, discretionary spending is controlled by annual dollar limits (spending caps). Mandatory spending and receipts legislation are controlled by a pay-as-you-go (PAYGO) requirement that legislation enacted during a session of Congress be deficit neutral.

⁵As part of the change in treatment of the Highway Trust Fund in the Transportation Equity Act for the 21st Century (TEA-21) (P.L. 105-178), interest is no longer paid to the Highway Trust Fund.

⁶Balanced Budget and Emergency Deficit Control Act of 1985 as amended by the Budget Enforcement Act of 1990 (BEA) as further amended by the Omnibus Budget Reconciliation Act of 1993 and the Budget Enforcement Act of 1997.

There is no single rule for budgetary control of trust funds. Knowing that a given account has been designated a trust fund does not tell you either whether spending is controlled through the appropriations process or whether it is subject to any limitations. Trust funds are classified as discretionary or mandatory depending on the nature of the substantive legislation creating the fund—i.e., depending on the nature of the activity funded by the trust fund. For example, Medicare and employee pensions are “direct spending,” or mandatory, programs. Outlays are solely a function of the design of the program, such as eligibility requirements and benefit formulas. As a result, under the BEA enforcement provisions, spending for these programs is subject to the PAYGO rules.⁷ In contrast, spending for discretionary—i.e., appropriated—programs is governed by the spending caps regardless of whether that spending flows from federal funds or trust funds. Spending from discretionary trust funds, such as the transportation trust funds, often is controlled by obligation limits, which limit outlays.

As you know, when the Congress created the various transportation trust funds, it dedicated trust fund receipts to trust fund purposes, but retained annual control over the timing of the expenditures. Therefore, spending from these trust funds is dependent on annual appropriations and has counted under the discretionary caps.

Budget Outlook and the Discretionary Caps

After nearly 30 years of unified budget deficits, current projections are for surpluses “as far as the eye can see.” Although many recent budget agreements (Gramm-Rudman-Hollings, the Budget Enforcement Act, and the Balanced Budget Agreement) were designed to achieve this fiscal position, the BEA’s enforcement regime does not end with the advent of a surplus. Direct spending is still subject to the PAYGO rules, and discretionary spending is still subject to specified dollar caps.⁸

According to the Congressional Budget Office (CBO), discretionary spending in 1999 made up about one-third of total outlays. Under the caps, these outlays will remain almost unchanged in dollar terms between fiscal

⁷Social Security has its own set of budget enforcement rules which protect its balances and remove its transactions from the deficit/surplus estimates and calculations made according to BEA.

⁸CBO has opined that BEA enforcement applies regardless of whether or not there is a deficit. OMB has noted that there is still an “on budget” [budget less social security and postal service] deficit so the question is moot.

years 1999 and 2002. Even if discretionary spending grows with inflation between fiscal years 2002 and 2009, it will fall to 29 percent of total outlays.

Discretionary caps were first imposed by the BEA in 1990. Their structure has varied. The matrix below shows the current structure of the discretionary caps and its evolution. For most categories, there are limits on both budget authority and outlays. However, because spending from the transportation trust funds is controlled by obligation limits, for the highway and mass transit categories, there are only outlay caps.⁹

Table 1: Discretionary Spending Categories by Fiscal Year

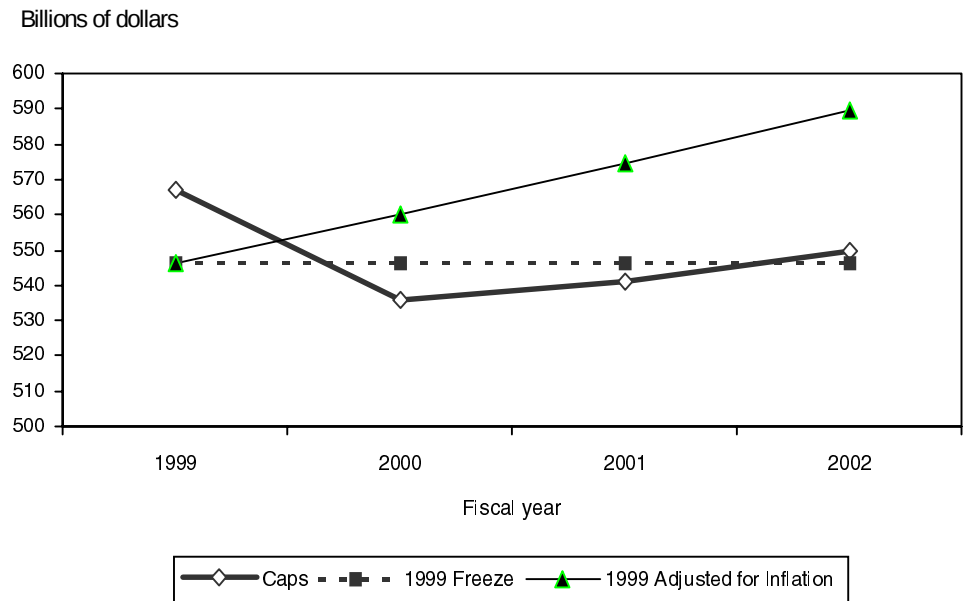
1997	1998	1999	2000
Violent Crime Reduction	Violent Crime Reduction	Violent Crime Reduction	Violent Crime Reduction
Discretionary	Defense	Defense	Discretionary
	Nondefense	Nondefense	
		Highway	Highway
		Mass Transit	Mass Transit

Over the next few years, the limits on discretionary spending are very tight, as shown in figure 1. The statutory caps are below the fiscal year 1999 freeze level (the 1999 freeze line) and substantially below the fiscal year 1999 level adjusted for inflation.

If the appropriations designated as emergency for fiscal year 1999 were to be repeated as nonemergency spending this year, budget authority for fiscal year 2000 would have to be cut by \$26 billion below the fiscal year 1999 appropriated level. Even if those emergency appropriations from fiscal year 1999 are not repeated for fiscal year 2000, budget authority must be cut \$10 billion below the fiscal year 1999 nominal level.

⁹Accounts in the highway category provide contract authority, which is liquidated from the Highway Trust Fund. Budget accounts for mass transit include both contract authority, liquidated from the Highway Trust Fund, and authorizations of appropriations from the General Fund of the Treasury. Contract authority is a form of budget authority that permits obligations to be incurred in advance of appropriations.

Figure 1: How Tight Are the Budget Authority Caps?



In its outlook volume, CBO noted the outlay caps “may be even harder to meet.” Outlays are projected to rise by \$21 billion between fiscal years 1998 and 1999. However, if the Congress froze appropriations at the fiscal year 1999 nominal dollar level, outlays in fiscal year 2000 would be \$13 billion over the outlay caps.

In summary then, the Congress and the President face a real challenge on the discretionary side of the budget this year. To comply with the current statutory caps, discretionary spending must be cut from its fiscal year 1999 appropriated level: budget authority by \$10 billion and outlays by \$13 billion, even assuming that none of the emergency spending is continued.

Potential Implications of Changing Budget Treatment for Aviation Programs

You asked me to discuss briefly the Airport and Airway Trust Funds in this context. In our March 1995 report, we discussed the budgetary treatment of transportation trust funds.¹⁰ We noted that there is some tension between the collection of earmarked revenues and the trade-offs the Congress must make about spending priorities.

Last year the Congress chose to make a change in the operations of the Highway Trust Fund—both its highway account and its mass transit account. The major changes were: (1) creation of separate outlay caps for highway and mass transit and (2) specification of annual guaranteed minimum spending levels—tied in the case of highways to Highway Trust Fund receipts.

You asked me to discuss issues related to providing treatment for the Airport and Airway Trust Fund analogous to that for the Highway Trust Fund. As background, I should note that obtaining a picture of aviation financing is more complicated than obtaining a picture of highway financing. Almost all highway programs are carried out by bureaus within the Department of Transportation. In contrast, although the FAA is responsible for the greatest share of aviation-related activities, the Department of Defense (DOD) and the National Aeronautics and Space Administration (NASA) also play major roles.¹¹

In addition, most highway programs are funded by the Highway Trust Fund, but aviation-related activities receive far more general fund support. NASA and DOD aviation-related activities are funded in those agencies' appropriations and financed through general funds. The FAA receives funding both from the Airport and Airway Trust Fund and from general fund appropriations.

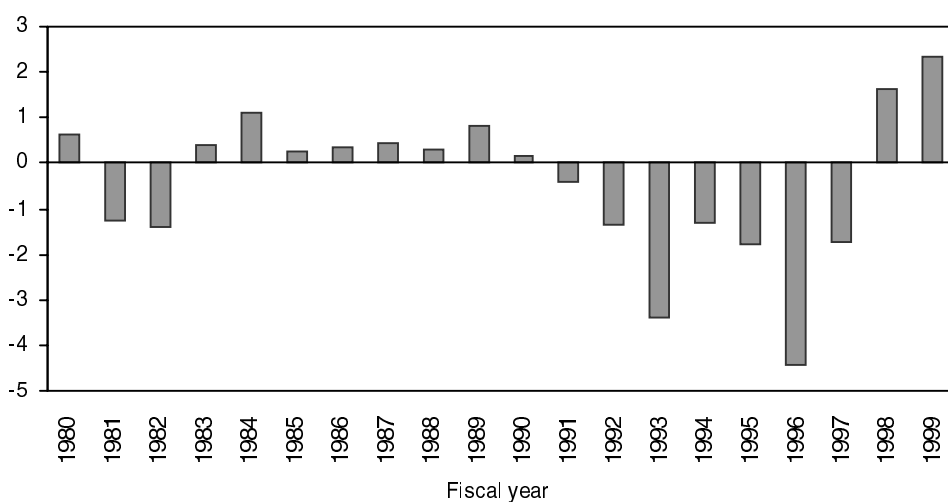
¹⁰Correspondence to Honorable Frank R. Wolf on Transportation Trust Funds. GAO/AIMD-95-95R, March 15, 1995.

¹¹DOD provides air traffic control services to military and civil users. The latest figures available from DOD indicated that it cost the department approximately \$680 million to provide services related to the National Airspace System in fiscal year 1995. NASA's aviation activities include aviation research and in fiscal year 1999, the Congress appropriated \$1.2 billion to NASA for these activities.

The Airport and Airway Trust Fund is used almost entirely to support FAA activities. Figure 2 shows reported trust fund receipts minus outlays for fiscal years 1980 through 1999. As this figure shows, in recent years the outlays from the trust fund have exceeded the receipts collected.¹²

Figure 2: Airport and Airway Trust Fund, Tax Receipts Minus Outlays

Billions of dollars



Note: Positive amounts indicate years when taxes exceeded spending. Negative amounts indicate years when spending exceeded taxes.

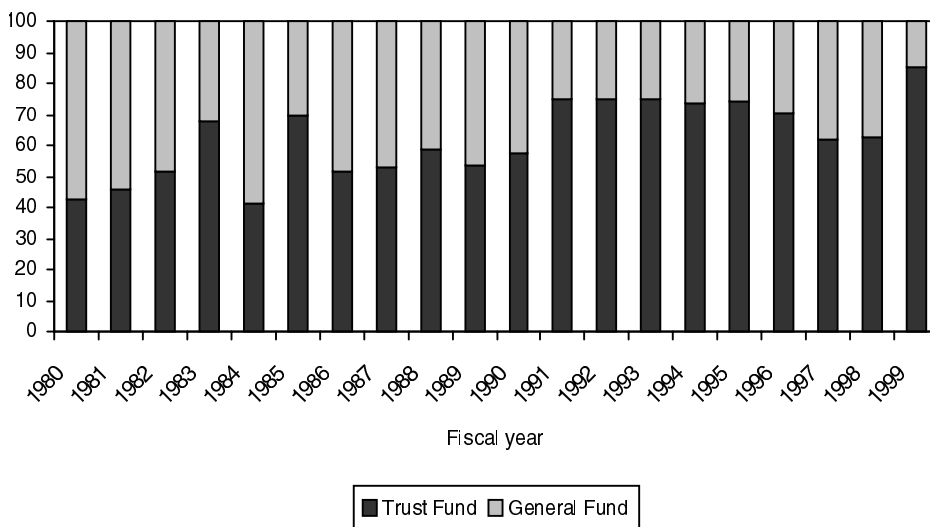
Source: As reported by the Department of Transportation.

As noted, the FAA also receives a significant share of its funding from general fund appropriations. Figure 3 shows the composition of FAA appropriations for fiscal years 1980 through 1999.

¹²The Airport and Airway Trust Fund balance at the end of fiscal year 1997 was \$6.4 billion.

Figure 3: Composition of FAA Appropriations

Percentage of appropriations



Finally, you asked about the budgetary implications of creating a new separate spending category for aviation. In part, that depends on the design of the category. In the past, separate caps within the overall discretionary spending limit were designed to place firewalls between different areas of spending and to limit trade-offs to programs within each category. For example, creation of separate defense and nondefense caps did not guarantee minimum funding levels for either category, but it did limit the extent to which one could be increased at the expense of the other. The same would be true for a separate cap for aviation spending—regardless of whether funding was from the trust fund or the general fund.

However, if a separate category is designed as a guaranteed minimum funding level, there are additional issues. For example, if creation of a separate spending category for aviation resulted in increased spending on aviation, and the remaining caps were not lowered to offset this, total discretionary spending would increase, and the surplus would fall (or the deficit increase). If aviation spending were increased and this increase was carved out of the general discretionary cap, then the remaining activities within that general category would compete for fewer total dollars.

Conclusion

In general, providing guaranteed funding levels to any one activity in the budget protects that activity from competition with other areas for scarce resources. The design of any guarantee can have implications for other federal activities and for federal resources. Whether to provide such a guarantee and to what activities is fundamentally a decision about priorities that only the Congress and the President can make.

This concludes my statement. My colleagues and I would be happy to answer any questions you or your colleagues may have.

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