14-Oct-87

V. ESTIMATED EFFECT OF RECENT PROPOSALS
ACCEPTED BY DEMOCRATS ON THE HOUSE WAYS AND MEANS COMMITTEE
(BILLIONS OF DOLLARS)

Item	1988	1989	1990
I. PRESIDENT'S BUDGET PROPOSALS FOR RAISING REVENUE			
A. Employment Tax Provisions			
1. Expand employer share of FICA tax to include all cash tips............	0.2	0.3	0.3
B. Repeal of Current Exemptions			
1. Bus..	0.1	0.1	0.1
2. State-local government highway excise tax........................	0.1	0.2	0.2
C. Certain New User Fees			
1. Internal Revenue Service...	0.1	0.1	0.1
2. Bureau of Alcohol, Tobacco, and Firearms.........................	0.1	0.1	0.1
3. Customs Service..	0.2	0.2	0.6
4. Imposition of air and ship travel tax............................	*	*	*
D. Debt Collection: 3-Year Extension................................	0.3	0.3	0.3
Subtotal:	1.1	1.3	1.7
II. EXPIRING PROVISIONS			
A. Telephone Tax: 3-Year Extension..................................	1.3	2.3	2.5
B. Freeze Estate and Gift Rates at 55%..............................	*	0.2	0.2
C. FUTA Tax: 3-Year Extension.......................................	0.7	1.0	1.0
Subtotal:	2.0	3.5	3.7
III. ESOP ESTATE TAX DEDUCTION..	1.3	1.6	1.9
IV. ESTIMATED TAX...	1.8	0.4	0.3
V. ADDITIONAL PROPOSALS			
A. Income Tax Provisions			
1. Deny child care credit for overnight camp expenses..............	*	0.1	0.1
2. Limit interest expense deduction on home equity loans............	NA	NA	NA
3. Cap cash option under cafeteria plan.............................	0.8	1.4	1.9
4. Modify IRA rules...	*	*	*
5. Limit deferral for capital gain on real estate exchange..........	0.2	0.4	0.4
B. Estate Tax Provisions			
1. Phase out unified estate tax credit..............................	*	0.3	0.5
2. Valuation of property (estate tax freezes).......................	*	0.7	0.8
3. Change state death tax credit to deduction.......................	*	0.4	0.5
C. Business Reform Proposals			
1. Repeal completed contract method.................................	0.8	1.6	2.0
2. Disallow a portion of interest deduction where taxpayer sells property and receives a tax-exempt obligation......................	*	0.1	0.1
3. Modify below market loan rules...................................	*	*	*
4. Repeal cash accounting for large farms...........................	0.2	0.3	0.3
5. Require current accrual of market interest on bonds..............	*	0.2	0.2
6. Amortization of customer base intangibles........................	0.1	0.1	0.1
7. Repeal vacation pay reserve......................................	0.1	0.1	*
8. Modify treatment of certain limited partnerships.................	NA	NA	NA
9. Modify treatment of tax-exempt partners..........................	*	0.2	0.2
10. Reduction of tax avoidance in certain corporate dispositions....	0.3	0.5	0.6

14-Oct-87

V. ESTIMATED EFFECT OF RECENT PROPOSALS
ACCEPTED BY DEMOCRATS ON THE HOUSE WAYS AND MEANS COMMITTEE
(BILLIONS OF DOLLARS)

Item	1988	1989	1990
11. Debt financing and corporate acquisitions	0.4	0.6	0.7
12. Additional tax on corportate raiders	0.1	0.1	0.1
13. Modify computation of earnings and profits for intercorporate dividends	0.3	0.4	0.5
14. Limit consolidated return pass-through	0.3	0.4	0.4
15. Tax loss mergers and acquisitions	0.1	0.1	0.1
16. Modify deduction for tax benefited transfers	0.2	0.6	1.1
17. Limit net operating loss carryforwards	*	*	*
18. Deny graduated rates for personal service corporations	0.1	0.1	0.1
19. LIFO recapture on conversions	0.2	0.2	0.2
20. Modify minimum tax provision	2.8	5.0	2.7
21. Repeal deferral for income from runaway plants	1.0	0.2	0.2
22. Repeal deferral on foreign income	0.5	1.0	1.2
23. Minimum tax treatment of Mutual Life Insurance Companies	*	*	0.1
24. Modify taxation of investment income of foreign insurance companies	*	*	*
25. Modify treatment of certain insurance syndicates	*	*	*
26. Modify taxation of net investment income of trade associations	*	*	0.1
27. Modify full funding limitation on pensions, ESOPs	0.6	1.8	1.4
28. Deny targeted jobs credit in certain situations	*	*	*
29. Tax irrigation subsidies	0.1	0.1	0.2
30. Limit issuance of tax-exempt bonds by Indian tribes	*	*	*
31. Limit issuance of tax-exempt bonds to acquire output facilities	*	*	*
D. Compliance Provisions			
1. Escheat of tax refunds	*	*	*
2. IRS funding	NA	NA	NA
Subtotal:	9.2	17.0	16.8
TOTAL CHANGES	15.4	23.8	24.4

Note: Joint Committee on Taxation estimates.
Note: Estimates do not reflect interaction among provisions.
*$50 million or less.

KEY BUDGET DATES UNDER REVISED G-R-H LAW

Action	Fiscal Year 1988	Fiscal Year 1989-1993
President's Budget Transmitted	January 4	1st Monday after Jan. 3
Budget Resolution Completed	April 15	April 15
House Appropriations Committee reports last bill	June 10	June 10
Congress completes Reconciliation	June 15	June 15
House completes action on all appropriations bills	June 30	June 30
President submits to Congress the mid-session budget report (establishing the economic & technical assumptions to be used in sequestration)	Not applicable	July 15
Presidential notification regarding Military Personnel accounts	October 10	August 15
Initial OMB/CBO snapshot	October 10	August 15
CBO issues its initial report to OMB & Congress	October 15	August 20
OMB issues its initial report to the President & Congress	October 20	August 25
President issues initial order	October 20	August 25
President transmits to Congress a detailed message regarding the initial order	Within 15 days after the order is issued	Within 15 days after the order is issued

Fiscal year begins & initial order becomes effective	October 1 (order becomes effective on date issued)	October 1
CBO issues it revised report to OMB & Congress	November 15	October 10
OMB issues its revised report to the President & Congress	November 20	October 15
President issues final order (which becomes effective immediately)	November 20	October 15
Majority Leader in each House shall introduce a joint resolution which affirms any modifications in defense programs proposed in the President's notification report if the report is timely submitted (the joint resolution is considered under expedited procedures and is amendable)	Introduced within 5 session-days after report is submitted by Pres. (but before 11/25)	Introduced within 5 session-days after report is submitted by Pres. (but before 10/20)
Majority Leader in each House may introduce a joint resolution which modifies the final order (the joint resolution is considered under expedited procedures and is amendable)	Introduced within 10 session-days after revised OMB report is submitted	Introduced within 10 session-days after revised report is submitted
President transmits to Congress a detailed message regarding the final order	Within 15 days after order is issued	Within 15 days after order is issued
Comptroller General issues compliance report	December 15	November 15

Action	Fiscal Year 1989	Fiscal Year 1989-1993
Date from which deficit reduction is measured	January 1	January 1
President's Budget Transmitted	1st Mon. after January 3rd	1st Mon. after January 3rd
Budget Resolution Completed	April 15	April 15
House Appropriations Committee reports last bill	June 10	June 10
Congress completes Reconciliaiton	June 15	June 15
House completes Action on all Appropriations bills	June 30	June 30
President submits to Congress the mid-session budget report (establishing the economic & technical assumptions to be used in sequestration)	Not applicable	July 15
Presidential notification regarding Military Personnel accounts	October 10	August 15
Initial OMB/CBO snapshot	October 10	August 15
CBO issues its initial report to OMB & Congress	October 15	August 20
OMB issues its initial report to the President & Congress	October 20	August 25
President issues initial order	October 20	August 25
President transmits to Congress a detailed message regarding the initial order	Within 15 days after the order is issued	Within 15 days after the order is issued
Fiscal year begins & initial order becomes effective	October 1 (order becomes effective on date issued	October 1
CBO issues it revised report to OMB and Congress	November 15	October 10
OMB issues its revised report to the President and Congress	November 20	October 15
President issues final order (which becomes effective immediately)	November 20	October 15

Majority Leader in each House shall introduce a joint resolution which affirms any modifications in defense programs proposed in the President's notification report if the report is timely submitted (the joint resolution is considered under expedited procedures and is amendable)	Introduced within 5 session-days after report is submitted by President (but before 11/25)	Introduced within 5 session-days after report is submitted by Pres. (but before 10/20)
Majority Leader in each House may introduce a joint resolution which modifies the final order (the joint resolution is considered under expedited procedures and is amendable	Introduced within 10 session-days after revised OMB report is submitted	Introduced within 10 session-days after revised OMB report is submitted
President transmits to Congress a detailed message regarding the final order	Within 15 days after order is issued	Within 15 days after order is issued
Comptroller General issues compliance report	December 15	November 15

THE WHITE HOUSE
WASHINGTON

current G-R-H

- $45 billion sequester pending
  (President can veto if it passes)
- will have to submit budget in January with $72 billion deficit

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

September 23, 1987

MEMORANDUM FOR THE PRESIDENT

FROM: Jim Miller

SUBJECT: Facts about the Debt Ceiling Extension and Gramm-Rudman-Hollings (G-R-H) Fix.

I thought it most important to set the record straight on certain allegations made at yesterday's meeting.

(1) Allegation: This bill contains a $35 billion tax increase.

Facts: It contains no such thing. There is not a scintilla of tax increase anywhere to be found in this document.

(2) Allegation: This would be the lowest defense budget you've ever had -- lower than President Carter's last budget.

Facts: The Congressional defense budget is too low -- with or without this bill. However, the allegation is untrue. In real terms, even assuming the worst-case scenario (a revised $275 billion) appropriations would be higher than in all the Carter years, as well as in 1981 and 1982.

(3) Allegation: The lack of "flexibility" would mean the discharge of 400,000 uniformed personnel and 150,000 reservists.

Facts: Even under the worst-case scenario, no personnel would have to be discharged, though there would have to be significant reductions in non-personnel accounts (e.g., DoD would have to stretch out procurement and reduce operating rates).

(4) Allegation: This bill would absolutely destroy all you've accomplished.

Facts: Not so. A worst-case would reverse some past accomplishments, particularly in readiness improvements, and it would slow down achievement of some future goals. But it would not reverse much of

what's already been achieved in force modernization. Moreover, Defense presently has $210 billion in obligated balances (as well as $50 billion in unobligated balances).

(5) Allegation: They say on Capitol Hill that the White House has been supporting this bill all along.

Facts: They may say this, but it is not true. In extensive informal discussions with the Hill Leadership we have repeatedly voiced concerns about the bill, suggested ways of improvement, and indicated uncertainty over your final decision. We have never given a "green light" on this bill.

(6) Allegation: Despite G-R-H's being in existence for over one year, the deficit has increased, not decreased.

Facts: Absolutely wrong. The deficit in FY 1986 was $221 billion and will be $158 billion for all of FY 1987 -- a $63 billion reduction in just one year.

Although I continue to have strong reservations about certain provisions of this bill (including some parts that are simply petty), I believe that the pros outweigh the cons -- primarily because we have other means of dealing with the cons (reconciliation, continuing resolution, and reprogramming under Defense flexibility).

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

September 23, 1987

MEMORANDUM FOR THE PRESIDENT

FROM: Jim Miller

SUBJECT: Facts about the Debt Ceiling Extension and Gramm-Rudman-Hollings (G-R-H) Fix.

I thought it most important to set the record straight on certain allegations made at yesterday's meeting.

(1) Allegation: This bill contains a $35 billion tax increase.

Facts: It contains no such thing. There is not a scintilla of tax increase anywhere to be found in this document.

(2) Allegation: This would be the lowest defense budget you've ever had -- lower than President Carter's last budget.

Facts: The Congressional defense budget is too low -- with or without this bill. However, the allegation is untrue. In real terms, even assuming the worst-case scenario (a revised $275 billion) appropriations would be higher than in all the Carter years, as well as in 1981 and 1982.

(3) Allegation: The lack of "flexibility" would mean the discharge of 400,000 uniformed personnel and 150,000 reservists.

Facts: Even under the worst-case scenario, no personnel would have to be discharged, though there would have to be significant reductions in non-personnel accounts (e.g., DoD would have to stretch out procurement and reduce operating rates).

(4) Allegation: This bill would absolutely destroy all you've accomplished.

Facts: Not so. A worst-case would reverse some past accomplishments, particularly in readiness improvements, and it would slow down achievement of some future goals. But it would not reverse much of

what's already been achieved in force modernization. Moreover, Defense presently has $210 billion in obligated balances (as well as $50 billion in unobligated balances).

(5) Allegation: They say on Capitol Hill that the White House has been supporting this bill all along.

Facts: They may say this, but it is not true. In extensive informal discussions with the Hill Leadership we have repeatedly voiced concerns about the bill, suggested ways of improvement, and indicated uncertainty over your final decision. We have never given a "green light" on this bill.

(6) Allegation: Despite G-R-H's being in existence for over one year, the deficit has increased, not decreased.

Facts: Absolutely wrong. The deficit in FY 1986 was $221 billion and will be $158 billion for all of FY 1987 -- a $63 billion reduction in just one year.

Although I continue to have strong reservations about certain provisions of this bill (including some parts that are simply petty), I believe that the pros outweigh the cons -- primarily because we have other means of dealing with the cons (reconciliation, continuing resolution, and reprogramming under Defense flexibility).

what's already been achieved in force modernization. Moreover, Defense presently has $210 billion in obligated balances (as well as $50 billion in unobligated balances).

(5) Allegation: They say on Capitol Hill that the White House has been supporting this bill all along.

Facts: They may say this, but it is not true. In extensive informal discussions with the Hill Leadership we have repeatedly voiced concerns about the bill, suggested ways of improvement, and indicated uncertainty over your final decision. We have never given a "green light" on this bill.

(6) Allegation: Despite G-R-H's being in existence for over one year, the deficit has increased, not decreased.

Facts: Absolutely wrong. The deficit in FY 1986 was $221 billion and will be $158 billion for all of FY 1987 -- a $63 billion reduction in just one year.

Although I continue to have strong reservations about certain provisions of this bill (including some parts that are simply petty), I believe that the pros outweigh the cons -- primarily because we have other means of dealing with the cons (reconciliation, continuing resolution, and reprogramming under Defense flexibility).

Options to Maintain Adequate Defense Spending Levels

1) Negotiate an acceptable $23 billion package of deficit reduction measures

   Problems: —requires acceptance of $10-12 billion in revenues

2) Modify sequester in appropriations bill (continuing resolution) after sequester

   Problems: —60 vote points of order in the Senate

   —requires restoring domestic sequester

3) Submit defense supplemental appropriation after sequester imposed

   Problems: —could be bottled-up in committee

   —60 vote points of order in the Senate

   —may not move until next year

   —will certainly attract domestic spending increases

4) Negotiate a budget package of defense and taxes <u>after</u> sequester imposed

   Problems: —clearly highlights defense-for-taxes

   —will attract additional domestic spending

5) Utilize the defense flexibility included in the G-R-H fix

   Problems: —will not restore overall funding, but could allow President to shift funds away from Congressional priorities to Administration needs

   —requires Congressional approval and therefore negotiations with Congress

   —would likely require a supplemental appropriations for at least Operations & Maintenance

Events in the Wake of a Successful Veto

- Possible default next Thursday or on a subsequent debt limit fight

- Clean, short-term debt limit

- Further attempts to amend debt limit with G-R-H fix—success will depend on Democrats continued support of G-R-H (Democrats unlikely to continue support, but rather renew efforts to blame deficits on the President)

- Debt limit fight, perhaps later this year, and almost certainly before the election next year

- Further cuts in defense; e.g., to $285 billion

- Lose ability to wage any appropriations fight and hold down domestic spending, unless a budget compromise is achieved

- Makes it more difficult to sustain vetoes on other economic legislation such as the trade bill gramm/rudman draft

Today I am signing HR , a bill that extends the U.S. government's authority to borrow funds and that re-establishes statutory [redacted] targets to reduce the federal deficit.

It is unfortunate that consistently Congress gets right ~~on~~ to the edge of default before ~~it faces the~~ facing its responsibility to deal with the orderly operation of government. But Congress' view of running the government by crisis is not new with this bill or this administration. ~~In the years ahead,~~ My hope for future Presidents is that the practice of using the debt limit and the U.S. government's credit to leverage political decisions will end. [redacted]

Since the campaign of 1980, I have strongly supported efforts to restrict Congress' appetite to spend in deficit. Our call for a constitutinal amendment to balance the federal budget ~~receives over 70 percent support from~~ is supported by over 70 percent of the American people. Two years ago, the Congress tried to take a step in the right dirrection with the passage of the Gramm-Rudman-Holligns deficit reduction plan. & I agreed. Its goal was, ~~to~~ once and for all, to put in defcit targets, leading to a balanced budget in five years. But the ink had no sooner dried, before ~~than~~ Congress walked away from its own plan.

Now, ~~they have~~ Congress has decided to revive this Gramm-Rudman-Hollings, and while my commitment to a realistic approach to ~~bringing~~ bring the federal budget in balance remains strong, ~~the~~ so-called "fix" ~~approved by Congress~~ reaffirms the short-comings in the original law.

Rather than face the difficult choices ~~of reducing~~ to reduce federal spending, Congress has tried to shift the ~~blame~~ focus to our national security or to you, the tapxyers, in the terms of new taxes. Even with the reforms put in place in 1981 in taxes and spending, the record shows: [redacted] growth has continued on the spending and payroll side and also federal tax revenues have increased. For those who argue there are no other ~~areas~~ ways to make spending reductions, I say they are wrong. For those way say the only choice ~~s are~~ is undoing our national security efforts that have ~~led us to the point~~ brought us ~~to achieving~~ the first treaty with the Soviet Union that actually reduce nucelar weapons, I say they are wrong. For those who predict that a little more tax revenue will wipe out the deficit ~~problem~~, I saythey are wrong.

Congress' own record shows that every time taxes are increased, spending is increased and the deficit is not decreased. It is time for the people to demand a clear, concise, and consistent statement on how to reduce the deficit and whether it ~~is~~ will be accomplished thru spending cuts, tax increases or whittling away at our national security.

In the weeks ahead, Congress will have a chance to show its true commitment to deficit reduction. Let's put out a few markers today:

1) any spending bill that goes above my budget will be vetoed.

2) any reduction in national security will be thoroughly examined ~~ventilated~~ with the American public and its impact on our long-term security interests will be fully explained.

3) any effort to hide the real use of "new revenues" will be exposed.

I renew my call on Congress to pass budget reforms that will, at least, break up those massive catch-all spending bills into ~~the~~ 13 integral parts. Tat way, each piece can be reviewed on its own merits instead of being hidden under pages and pages of legislation and billions and billions of ~~requests~~ dollars.

Maybe, it is also time for Congress, to meet the $23 billion deficit reduciton target contained in the latest Gramm-Rudman-Hollings plan, to consider a budget freeze -- that way both domestix spending and national security receive a fair review.

MEMORANDUM TO THE PRESIDENT

From: John C. Whitehead JW
Acting Secretary of State

Subject: Veto of Gramm-Rudman-Hollings amendments

I wish to join Cap in strongly recommending that you veto the debt limit extention bill that will be coming to you shortly for signature. This bill contains amendments to the Gramm-Rudman-Hollings legislation that would be devastating to your national security and foreign policy programs.

In the area of foreign affairs we are fighting desperately to keep programs alive and to protect our interests around the world within projected FY 1988 budget levels that are already precariously low. If signed into law, the GRH amendments will inevitably require a sequester in order to meet the FY 1988 deficit target of $144 billion. We understand that a sequester could result in a reduction of five to ten percent from the already inadequate levels contained in this year's Budget Resolution. If this happens, we will further compromise our ability to maintain critical bases in countries such as Spain, Turkey and Portugal. We will be unable to support Mrs. Aquino in her efforts to stabilize the Philippines. We will have to close up shop in a number of strategically important areas around the world, thus compromising our intelligence gathering efforts and our ability to pursue U.S. political, economic and commercial interests.

I strongly disagree with those who argue that a veto of this bill will lead to the collapse of the financial markets. Based on my 38 years of experience on Wall Street, I am convinced that relative stability can be maintained in the market if there is a strong perception that the deficit next year will be lower than this year. The level of reduction, however, does not have to be as significant as that contemplated in the GRH amendments. A deficit next year that is $10 billion below this year's, I believe, would be adequate to convince investors that there is a commitment to get this problem under control. Such a reduction can be achieved without the wrenching damage that would occur as the result of a sequester.

I have not reviewed this position with Secretary Shultz but believe he would fully concur.

August 12, 1987

AGENDA—Budget and Mid-Session Review

G-R-H

- Review where we are—last House offer and likely outcome
- Restate principle objective; i.e., avoid a sequester this year and preserve the President's ability to be a party to any negotiated budget

Mid-Session Review

- Timing and content—what will the numbers be
- Statement by the President and/or OMB at the time of release—tone and content
- Congressional reaction (and impact on G-R-H negotiations)

FY 1989 Budget

- OMB timetable
- Themes and content
- Import of G-R-H target if; 1) they are unchanged ($72 billion), or 2) changed to $125-130 billion

August 2, 1987

TO : Senator Baker
FROM : Dan Crippen
RE : Catastrophic LSG

Background

The House-passed bill is five times more costly than the Bowen plan in the early years, is financed largely by a surtax on elderly recipients, and will add $60 billion to the deficit by 2010 (necessitating a premium or tax increase or general fund revenues in order to keep the Medicare Trust Fund solvent).

The Senate bill, as reported from the Finance Committee, is slightly more than two times more costly than the Bowen plan (although it will attract a drug amendment that will dramatically increase costs). Although the program is technically budget-neutral, it is also financed partly through the imposition of a surtax, which would have to increase dramatically to keep pace with program costs.

We are preparing materials, in concert with OMB, HHS, and the Treasury, highlighting the program costs, the impact of the taxing mechanism, and the cost to the elderly (the unaffordability). No matter how you cut it, these bills would produce the largest new domestic program of the last decade and produce another explosive entitlement program. Even the deficit-neutral Senate bill will not be affordable to the elderly, causing a crisis in the not-too-distant future (perhaps as early as 1989 when the first tax returns include Medicare payments) and tempt Congress to increase the payroll tax or provide general fund financing.

Senator Byrd, thus far with DOle's acquiescence, is threatening to take up the bill this week. Senator Helms and other Steering Committee members have put a hold on the bill, but no one is very anxious to filibuster against the elderly.

Options

1) Essentially do nothing, in hopes the Senate bill, after adding a drug and other amendments, is as bloated as the House bill and further hope that a veto could therefore be sustained.

2) Sensitize Senators to the explosive out-year growth in costs and premiums in hopes of obtaining modifications to restrain the program.

3) Develop a new alternative, including an overhaul of the current Medicare system, to change the debate and attempt to produce a more rational health system for the elderly.

To pursue either of last two options, the Senate will have to be deterred from passing the bill this week.

July 31, 1987

TO : Senator Baker
Ken Duberstein
FROM : Dan
RE : Veto Threats and Related Legislation

The "Veto Threats Working Group" met today (Friday) and agreed to bring the following to your attention:

FSLIC
The compromise conference report is expected to pass the House on Monday or Tuesday and the Senate before the end of the week. S&L lobbyists attempted to blow up the compromise in the House Rules Committee but, having failed, are now "supporting" the conference report.

NASA Authorization
A Commerce Department letter threatened veto over creation of a National Space Council, Grant College, and Fellowship Program. Last year's authorization was pocket-vetoed over the same provisions. The bill may be passed before the August recess and will likely include the offending language.

Debt Ceiling
The Senate finished consideration Friday night. The G-R-H fix was unchanged, but no substantial process reforms were adopted. A Johnston amendment extends the debt ceiling to May, 1989. Initial indications are that the House will go directly to conference and attempt to include the Foley variation (which DOJ thinks is unconstitutional), change the targets, and move toward the Chiles/Rostenkowski notion of $36 billion annual sequesters. The present short-term extension should provide Treasury with enough cash to operate until mid-August. Therefore, a confrontation, either in the Congress or over a veto, is possible without the imminent threat of default—another extension into September is likely.

Catastrophic Health Insurance
Byrd is attempting to take the bill up before the recess—thus far, Dole is amenable. The Steering Committee has placed a hold on the bill. An LSG is planned for Monday at 2:00 P.M. A subsequent meeting may be required with Dole and Finance Committee Republicans to at least stall consideration until September.

Welfare Reform
House Republicans will unveil their substitute on Wednesday. With a few additional changes, the Administration could support the alternative.

Reconciliation
The reporting date was changed to September 29 for all committees. The House plans floor consideration the first week in October.

Trade
Conferees should be appointed this week.

LEGISLATIVE TOP TEN
Week of August 3, 1987

1. Debt Limit Conference

   - Conferees to meet
   - GRH proposals from House leadership
   - Process reforms

2. Central America

   - Senator Graham and others
   - Speaker Wright meeting Monday
   - Consultations before Guat City?

3. Welfare Reform

   - House Rep. substitute cosponsors meeting
   - Sen. Long meeting/Senators who are former Governors mtg.

4. Catastrophic Health Insurance/Senate

   - Dole/Simpson/Wallop
   - Finance Cmte Republicans on premium increases in out years

5. FSLIC Conference Report

   - Garn/Dole on Conference Report -- contact

6. Housing Bill

   - Republicans conferees meeting/Conference schedule

7. Trade Bill

   - Notify leaders on EPC/Baker lead
   - Letters to conferees (Dole statement?)

8. Textile Bill

   - Full Ways & Means action/Gibbons-Frenzel et al

9. Persian Gulf

   - Briefings requested; not given yet by State/Defense

10. Arms Control

    - Arms control observor group update
    - ABM/SDI amendment (Nunn/Levin) on Senate DOD bill/cloture near?
    - Appropriators to be briefed

LEGISLATIVE AGENDA

AUGUST 3-7	AUGUST 3-7 Cont.	AUGUST 10-14
FLOOR ACTION	FLOOR ACTION	FLOOR ACTION
HOUSE DEBT LIMIT CONFERENCE REPORT APPROPRIATIONS BILLS — LABOR/HHS FSLIC CONFERENCE REPORT NUCLEAR REGULATORY COMMISSION AUTH HR 1315 AMERICAN GENOCIDE	SENATE DEBT LIMIT CONFERENCE REPORT FSLIC CONFERENCE REPORT T CATASTROPHIC HEALTH INSURANCE	CONGRESSIONAL RECESS UNTIL SEPTEMBER 9
COMMITTEE ACTION	COMMITTEE ACTION	COMMITTEE ACTION
HOUSE WAYS & MEANS: TEXTILE QUOTA BILL AGRICULTURE: FARM CREDIT ASSISTANCE ACT HR 3030 HFAC: FOREIGN AID AUTHORIZATION MARKUP	SENATE LABOR & HUMAN RESOURCES: FAMILY PLANNING AMENDMENTS JUDICIARY: FAIR HOUSING MARKUP ENVIRONMENT & PUBLIC WORKS: PRICE ANDERSON MARKUP E & PW: T CLEAN AIR MARKUP T CONFERENCE S. 825 HOUSING AUTH BILL IRAN/CONTRA HEARINGS	

FLOOR: HOUSE SENATE COMMITTEE: HOUSE SENATE JOINT/CONF T - TENTATIVE 14:25 31-JUL-87

August 3, 1987

TO : Senator Baker
FROM : Dan
RE : Catastrophic Health

Attached are two pieces from Joe Wright—a cover memo and comparison of the various bills. Note that none of the numbers come from OMB—they are provided by the actuaries at HHS and the Treasury. The HHS actuaries have been the source for all such calculations involving Social Security or Medicare in the past. Further, CBO has refused to estimate the costs of these bills more than 5-years out. The points about the Senate bill you may wish to raise at the GOP leadership meeting include:

- cost—while $4 billion the first year doesn't sound bad, the outyear costs are very large ($150 billion by 2010, barely 20 years from now)—this could easily be characterized as another Medicare (and the reason we have the entitlement problem we now face)—low buy-in entitlement with explosive long-term costs

- affordability—while the Senate bill is "actuarially sound" (i.e., raises as much revenue as it spends), the growth in costs will very quickly make it burdensome on the elderly and, eventually, will simply be unaffordable—when that happens, there will be an attempt to inject general revenues or raise payroll taxes to supplement the payments by the elderly

- tax increase—a portion of the premiums in the Senate bill are based on income level, which works out to be an effective tax increase on the elderly—the Senate mechanism is much better than the House, however, and an income-related premium is likely to be included in any Congressional outcome

- political consequences—of opposition or veto

Options

- Construct new alternative which provides catastrophic coverage, combines Medicare Parts A & B, allows for a private sector insurance alternative, etc., OR

- Attempt to modify the existing Senate bill by—

  - changing the index for the catastrophic floor to increase with program costs (rather than CPI)—this change alone would reduce out-year costs by approximately 40% (because medical costs are expected to increase much more than basic CPI)

  - add modest co-payments to all eligible services—with catastrophic protection, limiting the amount of out-of-pocket costs each year, co-payments would not break the elderly and would help utilization

  - a modest prescription drug amendment if we cannot avoid it

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

AUG 03 1987

MEMORANDUM TO SENATOR HOWARD BAKER

FROM: Joseph R. Wright Tim Harris for JRW
Deputy Director

SUBEJECT: Comparison of Catastrophic Health Proposals

Attached is a side-by-side of the major features of four versions of catastrophic health legislation--the Administration's, House-passed, House Republican, and Senate Finance Committee's. The essential features are:

Costs

The Administration and House Republican bills are similar in costs, about $8 billion in 1995 and around $70 billion by 2010. In contrast, the House and Senate bills are much more expensive, with the House at $27 billion in 1995 and $199 billion in 2010 and the Senate at $12 billion in 1995 and $142 in 2010.

Reasons for Cost Differences

Over the long-term, the largest difference in cost derives from the manner in which the "out-of-pocket" threshold--the amount at which the catastrophic insurance kicks in--is indexed. Both the Administration and House Republicans index their bill by Medicare program costs, while the House-passed and Senate Finance bills are indexed by the social security COLA. Program costs grow at a much faster rate than the social security COLA, with the cumulative difference getting larger and larger each year.

There are other additional differences in costs:

a) The House bill contains a major Medicare expansion to cover drug costs. None of the other bills have such a drug expansion, although one is expected to be offered on the floor of the Senate.

b) Other major expansions are included in the House-passed and Senate Finance bills, including increased Home Health coverage and increased availability of skilled nursing care facilities.

c) Both the Senate Finance Committee and the House-passed bills have lower thresholds and requirements for paying deductibles than the Administration and House Republican bills, thereby adding to costs.

Financing

The Administration and House Republican bills provide for modest increases in the current Medicare premium, to be borne equally by all recipients. Because of their higher costs, the other two bills have much higher premiums, which are primarily added as a surtax. The Senate provision hits the middle class particularly hard.

All the bills are deficit neutral except the House-passed, which begins to show a deficit in 1993, increasing to over $20 billion by 2005.

A Note on Estimates

These estimates are derived from Treasury and HHS sources. CBO has thus far only been willing to do five-year estimates, thereby ignoring the long-term impacts.

Catastrophic Health Legislation

	Administration	H.R. 2470	House Republican	S. 1127
Total Medicare Cost ($ in Billions)	1989: $2.7 1995: $7.8 2010: $67.6	1989: $10.3 1995: $27.0 2010: $198.7	1989: $2.8 1995: $8.2 2010: $72.0 (rough estimates)	1989: $4.4 1995: $11.7 2010: $142.2
"Out-of-Pocket" Threshold	$2,000	$1,043 for Part B, plus one Hospital deductible	$2,000	$1,700
"Out-of-Pocket" Index	Program Costs	Social Security COLA	Program Costs	Social Security COLA
Home Health - days covered	21 days	35 days	35 days	21 days plus 21 days w/ prior hospitalization
Skilled Nursing Fac.: - Days covered - Prior hospital stay required	 100 days Yes	 150 days No	 100 days Yes	 150 days No
Drug Benefit	None	$500 out-of-pocket cap; 20 % copayment	Medicaid benefit for elderly below 150% of poverty; $50 deductible	Expected floor amendment similar to HR 2470
Medicaid	No provision	Mandatory Buy-in Spousal Impoverishment	Spousal Impoverishment	States to reprogram savings

continued

Catastrophic Health Legislation

	Administration	H.R. 2470	House Republican	S. 1127
Other Expansions	None	Outpatient Mental Health Respite (in-home) Care	None	Extend coverage for immunosup. drugs. Include screening tests toward cap
Hospital Deductibles	Two	One	Two	One
Hospital Coinsurance	Eliminated	Eliminated	Eliminated	Eliminated
Financing	Flat premium Deficit neutral	Three flat premiums plus surtax (% of AGI) Deficit Increasing	Flat premium, Plus other modest offsets Deficit neutral	Flat premium, surtax (% of tax liability) Deficit neutral

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

27 JUL 1987

MEMORANDUM FOR HOWARD H. BAKER, JR.
CHIEF OF STAFF TO THE PRESIDENT

FROM: James C. Miller III
Director

SUBJECT: Chief Financial Officer (CFO)

This position will provide leadership, policy direction, and oversight of Federal financial information and systems, credit and asset management, cash management, and controls against fraud and abuse.

A CFO in OMB will emphasize financial management reform efforts in the Executive Office and Government-wide. The President's report to Congress, "Management of the United States Government FY 1988," outlines an ambitious program of financial management reform. The CFO will spearhead the effort to:

- o Consolidate by 1988 the 124 existing financial systems into a single Government-wide information system operating in all major agencies;
- o Create a uniform system to facilitate efficient and accurate reports to Congress and watchdog agencies;
- o Modernize antiquated systems that are unnecessarily labor intensive and consequently high cost;
- o Strengthen the controller function in the agencies and ensure coordination with their budget staff.

The CFO will be the focal point for ensuring that the financial reforms take place. The CFO will work closely with the Financial Management Service of the Department of Treasury in carrying out these reforms.

July 28, 1987

TO : Senator Baker
FROM : Dan
RE : Mid-Session Review

As we discussed, Miller intends to issue pass-backs to the agencies tomorrow. Contrary to earlier expectations, he <u>will</u> send Cap a pas-back of $302 billion. If you concur, he needs to be instructed <u>not</u> to issue the DOD pass-back, but continue with the others as planned. "We may not ultimately be able to meet $108, but it is premature to give up on $312 for DOD."

A secondary issue is the handlng of appeals by Cabinet members. You should encourage Miller to handle all of it as his level and only offer Budget Review Boards (whihc would normally be chaired by <u>you</u>) only to individual Secretaries if a complete impasse is reached. Ultimately, there may be appeals to the President.

July 25, 1987

TO : Senator Baker
FROM : Dan
RE : Revenues in the President's Budget

The President's budget for FY 1988 included $42 billion in deficit reduction. Spending reductions (including interest savings) amounted to $20 billion and increased revenues $22 billion. The proposed revenue changes break down as follows:

Receipts/Taxes	$6.1 billion
Credit Reform	$1.3 billion
Loan Asset Sales	$4.2 billion
Privatization	$5.4 billion
User Fees	$3.2 billion
Other	$2.1 billion

<u>Receipts and Taxes</u>

$2.4 billion—	Increased compliance through additional funding for IRS
$1.6 billion—	Extension of Medicare payroll tax to state and local employees
$ .8 billion—	Repeal of exemptions from federal motor fuels taxes—including gasohol, public and private bus companies, and state and local governments
$ .4 billion—	Increase in coal excise tax for Black Lung Program
$ .3 billion—	Extend coverage of Social Security tax to certain currently exempt earnings—including inactive duty earnings for reservists, students and agricultural workers, children (18-21) employed by parents, and spouses employed by other spouse
$ .2 billion—	Require employers to pay Social Security tax on total tips
$ .1 billion—	1.5% increase in rail pension contributions
$ .1 billion—	Maintain current level (.22%) and expand coverage of general import duty to defray Customs Service expenses
$ .1 billion—	Extend coverage of Federal/State Unemployment Insurance to railroad employees
$ .1 billion—	IRS fees for letters of determination and private letter rulings
$ .1 billion—	Require railroads to pay 25% of windfall retirement benefits
$ .1 billion—	Increase fees on nuclear power plants to cover 50% of costs of NRC and FEMA

July 25, 1987

TO : Senator Baker
FROM : Dan
RE : Mid-Session Review

By Tuesday or Wednesday of this week (July 28-29), OMB must issue the "pass-backs" to all agencies indicating the level of spending reductions each agency must produce for the mid-session review. Unless the targets are changed by the August recess (which would not happen if a clean long- or short-term debt ceiling is enacted), the mid-session review must show a deficit of $108 billion. There are essentially four options:

1) require enough savings to keep defense at $312 (BA). The required savings under this option would be $12 billion—a level virtually impossible to achieve and that would invite numerous appeals by the agencies (to you and the President) and foster critical press and cynical Congressional statements.

2) reduce the defense request to $302. The required level of savings would be $6 billion—painful enough to still prompt some agency appeals and leaks to the press.

3) develop a phony plug. We could, for example, advocate selling even more assets—presumably loans—propose unrealistic economics, include the age-old "management savings", or simply include unspecified reductions. This alternative would invite criticism and charges of implicitly giving up on the targets.

4) admit that $108 is not achievable. Congress has already breached the fact that $108 is unrealistic, even if the target has not been changed in law. We could easily show a deficit well below the $150-149-144 billion levels that are being considered on the Hill.

Miller wants to pursue option #2 (assume defense at $302 billion) and, if the targets are not changed, confront the President with the option of reducing his defense request to $302 or missing the $108 target—essentially attempting to force Cap's hand.

July 25, 1987

Rationale for Clean Debt Limit

" We're for this (G-R-H), but only with process reform—that's the only way it will work."

1) G-R-H (without process reform) is simply another ploy to raise taxes

- Congress knows that the American people don't want more taxes
- Congress may not be able to even pass a tax bill
- Congress knows that the President will veto their tax proposal
- Rather than be responsible and enact the kind of budget the President submitted, Congress is attempting to—
  - put the entire budget on auto-pilot to force a tax increase or threaten our nation's security—holding defense of the country hostage for tax increases
  - if Congress has its way, we would have to reduce the number of troops by 400,000, the number of civilian employees by 110,000, the number of ships by ____, the number of planes by ____, and the number of tanks by ____.
- The President submitted a budget which, whiling preserving the defense build-up, would produce a lower deficit than the Congressional budget without new taxes
- Instead, Congress is attempting to enact a budget for next year which cuts $23 billion from defense, increases domestic spending by $41 billion, and raises taxes by $19 billion
- The Congress is not willing to make the hard choices—only spend the taxpayers' money

2) Recitation of this year's events—

- Congressional budget—
- Effects of sequester on defense and domestic programs and as a tax trap
- President's budget
- negotiating position—"...need process reform to avoid sequester..."

July 24, 1987

TO : Senator Baker
Ken Duberstein
FROM: Dan
RE : Veto Threats and Related Legislation

The "Veto Threats Working Group" met today (Friday) and agreed to bring the following to your attention:

FSLIC

The conference report is close to completion. Unless negotiations by JAB III are successful, we expect the conference report to be passed by both Houses the week of August 3. By waiting until the last minute before the August recess, a veto would mean 4-6 weeks delay in recapitalizing FSLIC . Further, a veto before or during the August recess would give lobbyists the opportunity to incite their constituents to contact members during the recess. A difficult override vote could be the first order of business in September—the outcome of which could set the tone for the remainder of the year.

NASA Authorization

A Commerce Department letter threatened veto over creation of a National Space Council, Grant College, and Fellowship Program. The bill may be passed before the August recess and will likely include the offending provision. [We are researching the final disposition of last year's authorization—it may have been vetoed over the same provisions.]

Debt Ceiling

A veto remains a distinct possibility—over an unacceptable G-R-H fix (e.g., the Foley variation which DOJ thinks is unconstitutional) or lack of process reforms. The anticipated short-term extension, until August 7, should provide Treasury with enough cash to operate until mid-August. Therefore, a confrontation, even beyond the scheduled adjournment, is possible without the imminent threat of default.

Reconciliation

Markup in both Houses have been deliberately slowed to postpone reporting until after the August recess. The final disposition of any G-R-H fix, including target changes, could have a material effect on the outcome.

Mid-Session Review

Without a change in G-R-H targets before the recess, the Administration will be required to show a deficit of $108 in the mid-session review. It may come down to 1) reducing the defense request, or 2) missing the target, or 3) a phony plug.

July 19, 1987

TO : Senator Baker
FROM : Dan
RE : Domenici call of Friday (7/17)

Domenici returned your call about 4:00 P.M. He reported that he had agreed with Chiles on a G-R-H fix that would result in some sequester this year and a likely $36 billion sequester next year. When I asked, he replied that the size of this year's sequester was up in the air, but would be something like $21 billion (amazingly similar to the size of the proposed tax increase).

He then delivered up a lecture about how unrealistic the President was being by citing the $155 billion deficit this year. He thought we were doing everyone a disservice by ignoring the large and growing deficits in the out-years. He repeated his claim that for "only" $11 billion in taxes (curiously similar to the amount he advocated in the original Domenici plan) we could buy higher defense and maybe more domestic cuts.

He did offer that, based on an earlier conversation I had had with Bill Hoagland, that there wasn't much in the package for the Administration. He was still attempting to get agreement on process reforms, including a vote on a balanced budget amendment, but didn't hold out much prospect.

He concluded by advising that you get together with the President on others and advise him that he may want to veto the debt bill over the G-R-H fix.

In short, Domenici was frustrated and irritated and unwilling to give us much help in avoiding a sequester this year or holding out for tough process reforms.

July 17, 1987

TO : Senator Baker
Ken Duberstein
FROM: Dan
RE : Veto Threats and Related Legislation

The "Veto Threats Working Group" met today (Friday) and agreed to bring the following to your attention:

Homeless Aid Authorization
The last day for action on the conference report is Wednesday (7/22). Although the bill was opposed in both the House and Senate, no veto recommendations were sent.

FSLIC
The conference report, and therefore the conference itself, is not completed. Congress is delaying the process in an attempt to increase pressure to sign. By waiting until the last minute before the August recess, it will be at least 6 weeks before replacement legislation could be enacted, increasing the nervousness about the S&L industry. Further, a veto just before the August recess would give lobbyists the opportunity to incite their constituents to work over the members during the recess.

Trade Legislation
The Senate is scheduled to finish on Tuesday. A draft Presidential statement has been prepared that essentially says the President would veto the Senate bill, veto the House bill, is hopeful the conference can produce a signable product and that it is now up to the Democratic leadership to decide if they want a bill signed into law or a campaign issue.

Catastrophic Health Care
The House bill should be voted on this week. The multi-committee product is three times more expensive than the Administration's proposal, is financed by an effective income surtax on the elderly, increases the deficit by $10's of billions in the out-years, and threatens to bankrupt the Medicare Trust Fund by the end of the 1990's. House Republicans are fashioning a substitute that is more restrained but still far afield of the original Bowen plan. An LSG is scheduled for Monday.

Welfare Reform
Moynihan announced that he would introduce his bill on Tuesday. While he doesn't appear to have any Republican cosponsors at this point, Durenberger and others will be tempted. Dole is reported to have told Moynihan that Republicans were going their separate way. The House may include welfare reform in their reconciliation/tax bill when it is reported from Ways & Means (sometime before the August recess). An LSG is scheduled for Monday.

NASA Authorization
Commerce letter threatened veto over creation of National Space Council, Grant College, and Fellowship Program. The bill may be passed before the August recess, including the offending provision.

HB

July 11, 1987

TO : Senator Baker
FROM : Dan
RE : Update on FSLIC

Sustainability

Garn has not completed his canvas of the Senators who supported him on stripping the bill in the Senate. His count thus far is roughly:

20 votes to sustain veto
3 leaning to sustain
1 vote to override veto
6 leaning to override
4 no opinion
5 not contacted

Will has the sense that Garn is not pressing hard at this time, but asking only for initial positions. Therefore, the "leanings" and "undecideds" may be gettable. To have 20 firm supporters and only 1 firm opponent out of this pool of 39 is encouraging.

Timing

The drafting of the conference report has stalled for no good reason. It seems that Proxmire wants to wait until the last minute before the August recess to put more pressure on the President to sign. We would not be able to get another bill until well into September and the S&L's would have the recess to work over their representatives to gain commitments to override.

Content of "Next" Bill

Based on Treasury's assessment and Will's conversations with Wright's staff, there is a good chance of getting a more favorable bill the next time around. It will obviously depend on the votes on the conference report and the timing of a veto.

Market Reaction

While there is always the possibility of precipitating some reaction, there are no signs of impending panic among depositors. The regions where the worst problems exist, oil-producing and agricultural states, are faring somewhat better economically. Depending upon the length and severity of a battle over the bill, I wouldn't expect a strong reaction at this point.

July 11, 1987

TO : Senator Baker
FROM: Dan
RE : Steel and the Pension Benefit Guarantee Corporation (PBGC)

Summary

Predicated on the potential exposure of the PBGC to additional steel companies filing for Chapter 11, the EPC is considering a modified "bail-out" for the steel industry. The primary option under consideration would reimburse companies for each unit of capacity that is closed. In return, the government would be able to limit long-term exposure to the PBGC and may eventually receive some form of payback (preferred stock, profit interest, warrants, relinquishment of NOL's, etc.). This proposal is being pushed by Baldrige and Brock and is strongly opposed by Miller and Sprinkel. James Baker is generally in favor of "doing something," but is a little unsettled by the prospect of a bail-out and somewhat concerned about the precedent; e.g., auto companies also have large unfunded pension plans. Congress, including Senators Heinz and Metzenbaum, are considering legislation that is potentially more costly than the EPC option and may not address adequately the PBGC problem.

Background

The PBGC currently has $7 billion in liabilities and $3 billion in assets on their books. Fully 80% of this shortfall is due to steel companies—LTV added $2 billion alone. Total underfunding of guaranteed pension systems, which represents PBGC's potential exposure, is approximately $50 billion ($136 per insured employee). While not all of the $50 billion is at risk, future shake-outs in the steel, auto, rubber, and airline industries, could result in booking net liabilities several times the current $4 billion.

The deficit and potential exposure do not present immediate cash-flow problems. Not unlike a ponzi scheme, in addition to annual premiums from the 110,000 plans they insure, the PBGC assumes the (insufficient) assets of a pension plan when they take on the liability. Thus, they are able to make payments to current beneficiaries by using these assets and premiums in the near term, but will ultimately not be able to meet their obligations. Estimates have the PBGC running out of cash in 10-12 years.

PBGC's current problems rest mostly with the steel industry. Five companies, Bethlehem, Armco, National, Inland, and USX, all of which are considering Chapter 11 filings, could add another $4-6 billion in liabilities if they enter bankruptcy proceedings. Obviously, the ability to promise and insure (through PBGC) generous but unfunded, pension programs to steel workers is one of the principle problems of the U.S. steel industry. Last year the industry paid out $1.6 billion to retirees while paying in only $200 million to their retirement funds. Even at this insufficient level of funding, pension costs added approximately $3/hour to steel's labor costs.

The ultimate solution is to close more plants. Even though steel capacity has fallen almost 25 million tons since 1984 (to 112 million tons), the industry needs to shed another 20 million tons in order to regain sustained profitability. The cost of closing plants—$100,000 per employee for retirement alone—often exceeds the losses incurred by keeping them open. Closing 20 million tons of capacity is estimated to cost $1-1.6 billion.

Thus, there are great incentives to enter bankruptcy and eliminate pension costs (as well as strengthen their hand with unions and creditors). The Chapter 11 filings by LTV and Wheeling-Pittsburgh give these companies a great cost advantage over the rest of the industry, adding even more pressure for the rest to follow suit.

Current Issues

There are two somewhat separable issues:

1) Actions necessary to restore solvency—

The PBGC has proposed an increase in the basic premium they charge to all pension funds they insure ($8.50/worker/year) as well as add a variable rate premium based on the unfunded liability of each plan—raising $ 800 million per year. The Congressional Budget Resolution assumes only $100 million in new premiums and therefore implies only a modest increase in the basic premium.

They also seek a change in ERISA to increase the minimum funding standards of private pensions to help reduce future exposure. They would like, but have not thus far advocated, a change in bankruptcy law so that the PBGC is deemed a secured creditor and moved up in the queue under Chapter 11.

2) Actions to deal with steel companies—

The Economic Policy Council is headed toward recommending to the President a modified bail-out of the steel industry which will sound like Chrysler II. The federal government would reimburse companies for each unit of capacity that is closed. In return, the government would be able to limit long-term exposure to the PBGC and may eventually receive some form of payback in preferred stock, profit interest, warrants, relinquishment of NOL's, etc. The plan is expected to cost the federal government $1.6 billion (as opposed to the $4-6 billion in potential liabilities for the PBGC).

Brock and Baldrige argue that this proposal will save money in the long-run because the PBGC will have to eventually be "saved" with general revenues. Therefore, by doing nothing, the government will be "bailing-out" the industry through the PBGC. Further, this option could allow the elimination of up to 20% of steel capacity and restore the industry to some level of economic health. This approach would force a sharing of the pain among employees, the companies, and the government and therefore may not be a precedent for other industries. Finally, they argue that if the Administration doesn't act, Congress will, and with a much more costly program.

Sprinkel and Miller argue that they are opposed to a bail-out of any kind—that the companies got themselves into this mess. They are convinced that the cost estimate of $1.6 billion in government expenditures is too low and point out that it does not account for the costs to steel consumers through higher prices (as much as $900 million a year). Finally, they suggest that the lay-offs associated with closing plants (as many as 46,000) will be blamed on the Administration.

The New York Times

Founded in 1851

ADOLPH S. OCHS, *Publisher 1896-1935*
ARTHUR HAYS SULZBERGER, *Publisher 1935-1961*
ORVIL E. DRYFOOS, *Publisher 1961-1963*

Get Serious About Protecting Pensions

When a company goes bankrupt and leaves a pension fund without sufficient assets to cover benefit payments, the Government's Pension Benefit Guaranty Corporation picks up the tab. What happens when this insurance fund runs out of cash?

Claims against the fund now exceed projected premium income by more than $4 billion, and the deficit is sure to rise in the next few years. Congress is morally bound to keep the benefits flowing. The big question is whether it will try for enduring reforms or settle for a temporary fix.

•

When the pension insurance agency was created in 1975, the annual premium levied against each of the 110,000 pension plans covered was just $1 per worker. That wasn't realistic: liabilities exceeded income in the first year. The premium has since been raised to $8.50, but cumulative liabilities are still growing faster than income. The fund has managed to remain self-financing only on a cash basis. Each year's premiums cover payments immediately due, but they do not suffice to build reserves to cover obligations in place for future decades.

The obvious remedy, another modest across-the-board increase in the premium, won't provide more than short-term relief for a fund already burdened by unfunded long-term obligations of $136 per worker. And it increases firms' incentives to liquidate healthy, fully funded pension plans and escape all future premium obligations.

That's why the Reagan Administration wants Congress to link premiums to risk. Premiums for the 90 percent of pension plans that are fully funded would remain at $8.50 per worker. Underfunded plans, which create a potential liability for the insurance fund, would pay up to $100 a year per employee. To protect the system against inflation, both the standard $8.50 premium and the risk surcharges would be indexed to average wage increases.

The new variable rate system would more than double the insurance fund's income next year, without affecting the insurance costs of responsible employers. As important, it would induce companies with underfunded plans to close the gap.

Risk-based premiums would not change the behavior of companies on the brink of bankruptcy or reduce the cost to the pension agency once a company goes over the brink. But another proposal backed by Kathleen Utgoff, the pension agency's director, could make a big difference.

Under current law, pension funds are "unsecured creditors" in bankruptcies, and thus receive money only after bondholders are paid. Typically, the pension agency recoups about 10 cents on every dollar of unfunded pension liabilities. If Congress made the pension agency a secured creditor, the payout would be considerably greater. Secured creditor status for the agency would also reduce the incentive for other creditors to force troubled corporations into liquidation.

Congress, under heavy pressure to shore up the pension agency, may be tempted simply to raise the premium enough to meet the fund's monthly cash obligations a bit longer. But every year without serious reforms means more defections by healthy pension funds and more unfunded liabilities to be borne by well-run pension plans that remain. Current and future retirees deserve better.

July 9, 1987

TO : Senator Baker
FROM : Dan
RE : Debt Limit Scenario(s)

If we follow Miller's advice and either do nothing or support Gramm—

1) Byrd will offer the Rostenkoski proposal.

2) Gramm will try to amend by changing $36 billion annual reduction to fixed targets. I expect he will succeed because Byrd and the Democrats will want bipartisan cover for the imposition of an automatic sequester and to get the debt bill out of the Senate.

3) The House will toy with adding the Foley twist, i.e., forcing the President to sign or veto a sequester order, but ultimately accept the Senate provision.

4) The President will be faced with recommendations to veto from at least Cap, Schulz, and Carlucci, all on the eve of default.

5) If he signs under this scenario, we would probably be able to avoid a sequester this year (although would have to accomplish some deficit reduction on paper). However, we would face a $50-60 billion sequester next year, even if we successfully negotiate a budget deal this year.

July 9, 1987

TO : Senator Baker
FROM : Dan
RE : Rationale for Long-term Debt Limit

1) Our offer to negotiate was predicated on agreement on a package of G-R-H and process reforms. The Democrats are highly unlikely (indeed have as much as said so) to give us any of the tough process reforms; i.e., votes on balanced budget and line item veto or any form of enhanced recission. Therefore, accepting any type of G-R-H fix which incorporates and automatic sequester is unacceptable—it does not give the President the tools he needs to control spending during the year and prevent a sequester or mitigate the damage if a sequester is imposed. It is simply a trap.

2) Without a broad agreement, passage of the debt limit is imperiled, and the threat of default looms.

3) The consequences of a default are too severe to be screwing around on the debt limit bill.

4) If there ever is agreement, there are other vehicles to use—CR, etc.

5) Accepting a clean, short-term debt limit implies that the long-term bill will be included in the tax bill when we get it in September, perhaps making it more difficult to veto because of default.

July 8, 1987

Deficit Outlook and Sequester Impact

WARNING: The following numbers are somewhat conjectural. In addition to using preliminary, rough deficit projections, a sequester is based not on the absolute deficit number, but a revised (Gradison) baseline and the average of OMB's and CBO's projections. In addition to changing economics and technical reestimates, we do not know what the baseline will be until after all appropriations (CR) are enacted. Finally, projecting the effects of one year's sequester on the baseline for following years is difficult at best.

Nonetheless, the following represents a best guess, in rough magnitudes, of what might happen under an automatic sequester with varying targets. The essential point is that under any of the G-R-H fixes being discussed, we face a substantial ($30-70 billion) sequester next September-October. We would need a budget compromise of $30-40 billion both this year and next to avoid next fall's sequester.

With no budget compromise and a veto of reconciliation

Assuming no deficit reduction this year (i.e., we fail to strike a deal) but also assuming no new spending is enacted this year (dubious—appropriations are already over baseline and education, catastrophic health insurance, welfare reform all spend money), the result would be—

	FY 1987	FY 1988	FY 1989
Deficit	165	180	190
Gradison Baseline		160	175
G-R-H Targets	144	108	72
Therefore, sequesters would be:			
With Current Targets		50	40
Defense BA		(45)	(35)
With 1-year Slip in Targets *		0-15	40-65
Defense BA		(0-12)	(35-60)
With Rostenkowski—$36 B annual reductions		36	36
Defense BA		(30)	(30)
With Rostenkowski—fixed targets		0-10	50-60
Defense BA		(0-10)	(40-50)

* With a one-year slip in targets, we may be able to avoid a sequester this September because of lower defense spending and other accounting changes. If so, the sequester next year could be as much as $65 billion.

With a budget compromise that might be acceptable to the President

If we ultimately struck a deal for FY 1988 that included no taxes above the President's budget, less defense than his request, some of his non-tax revenues, and more domestic savings than the Congress now has in mind, the result would be—

	FY 1987	FY 1988	FY 1989
Deficit	165	140	170 *
Gradison Baseline		125	155
Therefore, sequesters would be—			
With Current Targets		15	80
Defense BA		(12)	(70)
With One-Year Slip		0	45
Defense BA			(40)
With Rostenkowski—$36 B annual reductions		0	36
Defense BA		(0)	(30)
With Rostenkowski—fixed targets		0	40
Defense BA		(0)	(35)

* Achieving an acceptable compromise this year would involve a number of one-time "savings", such as asset sales, and therefore not reduce the FY 1989 deficit by more than $15-20 billion.

July 7, 1987

Next Steps on Budget/Debt Limit

- Convince President he never met a sequester he liked

  - HHB materials to President on sequester effects and Democratic strategy
  - Presentation to President by Weinberger, Schulz, Carlucci on sequester

- Prepare to call for clean, long-term debt limit

  - HHB meeting with Dole and Michel to receive update on negotiations
  - HHB meeting with Domenici
  - Dole/Domenici/Michel/Latta declaration that Democrats won't give on process reform
  - Dole and Michel to see President
  - Gramm and Armstrong to see President (optional HHB meeting)
  - HHB and JAB III to see Byrd, Bentsen, Speaker, Rostenkowski, et al

- Call for clean, long-term debt

- Decide in Mid-Session review to do "the best we can," achieving deficit reduction in excess of the Congress, but failing to meet $108

- Begin internal consideration of alternative budget or negotiating parameters to prepare for:

  - Discussions with Republicans on G-R-H
  - Possible Presidential announcement prior to August recess of—
    - Alternative budget, or
    - Willingness to negotiate

    NOTE: Which of these options to pursue will depend critically on what the defense establishment is willing to concede at that point—if they are willing to go with, e.g., $301, then alternative budget may the best option—if they are stuck on $312, may have to "negotiate". We assume, at this point, that neither option would include any new taxes.

- Begin quiet media campaign to point out Congressional failure to meet $108, this year's target of $144, etc.

BUDGET/RECONCILIATION SYNOPSIS

<u>BACKGROUND</u>

-- Next step in the budget process is reconciliation.

-- Committee action to comply with reconciliation instructions required by July 28. Floor action possible in House and Senate week of August 3. Final passage in September.

-- Key features of reconciliation:

  o $65 B in taxes over 3 years.
  o Debt limit increase.
  o Budget process reform and G-R-H "fix" likely.

-- Democrats want reconciliation to include debt limit increase to make President face default if he vetoes. Rostenkowski also wants reconciliation to include sequester fix so that tax increase will be signed.

-- Expect Senate attempt at short-term debt limit extension until September, using the "Gephardt Rule" bill deemed to have passed House per CBR.

-- Gramm indicates no debt limit action of any kind unless it includes his G-R-H "fix" making sequester automatic.

-- Signs point to a confrontation with Gramm as early as mid-July and a conflagaration in September of reconciliation, debt limit, G-R-H "fix" and omnibus continuing resolution. Expect renewed calls for "summit".

-- Issues

- o Approach to Gramm-Rudman-Hollings fix:
  - -- Automatic sequester (Oct.'88 problem).
  - -- Target changes
  - -- Other process reforms
- o Path to a clean debt limit extension
- o Reconciliation Game Plan
- o Response to Budget Summit proposals

will - USTR
(C[illegible]

G.W.

Harold Brown [illegible]

Rit [illegible]

organization [illegible]

July 6, 1987

Next Steps on Budget/Debt Limit

- Convince President he never met a sequester he liked
    - HHB materials to President on sequester effects and Democratic strategy
    - Presentation to President by Weinberger, Schulz, Carlucci on sequester
- Prepare to call for clean, long-term debt limit
    - HHB meeting with PVD
    - Dole and PVD declaration that Democrats won't give on process reform
    - Dole and Michel to see President
    - Gramm and Armstrong to see President
    - HHB and JAB III to see Byrd, Chiles, et al
- Call for clean, long-term debt
- Decide in Mid-Session review to do "the best we can," achieving deficit reduction in excess of the Congress, but failing to meet $108
- Begin internal consideration of alternative budget or negotiating parameters to prepare for:
    - Discussions with Republicans on G-R-H
    - Possible Presidential announcement prior to August recess of—
        - Alternative budget, or
        - Willingness to negotiate

      NOTE: Which of these options to pursue will depend critically on what the defense establishement is willing to concede at that point—if they are willing to go with, e.g., $301, then alternative budget may the best option—if they are stuck on $312, may have to "negotiate". We assume, at this point, that neither option would include any new taxes.
- Begin quiet media campaign to point out Congressional failure to meet $108, this year's target of $144, etc.

July 6, 1987

Review of Budget Issues

1) Avoid Sequester—

1. Convince President he never met a sequester he liked
    - danger to defense, international affairs and Republican programs
    - Democratic strategy to trap into taxes
    - use NSC (Weinberger, Schulz, Webster, Carlucci)
    - have CIA produce analysis of defense capability after sequester
2. Armstrong and Gramm to see President
3. HHB and JAB III to see Congressional Leadership
4. call for clean, long-term debt limit
5. fight to prevent a "Gramm-fix" in the Senate

Pros:

- doing nothing insures a sequester of some type
- even if lose on Gramm, will have debt limit out of reconciliation, free of tax and other fights

Cons:

- "abandons" G-R-H with political and market fallout
- alienates some Republicans in Congress, potentially losing their support on subsequent budget and other issues
- may lose
- a Gramm fix may appear in other legislation

2) Develop plan, with or without taxes, that:

1. meets $108 deficit

    Pros:

    - Would show that it is possible to meet $108 target.
    - Could show that taxes are not needed.
    - Further deliniates differences with Congress/Democrats.

    Cons:

    - requires giving up on President's defense request before any deal/offer to Congress
    - need $15 billion in additional domestic savings, over and above President's budget ($20+ billion without defense reduction)
    - process and proposed reductions would be leaked, inviting ridicule for more "unrealistic" spending cuts
    - Cabinet would descend on West Wing and the President
    - may impact ability to "compromise" and eventualy admit can't make $108 without taxes

2. achieve as much deficit reduction as Congressional resolution

   - President would accept:
     — some reduction in defense request
     — more domestic spending
     — less non-tax revenues
   - Congress would have to give on:
     — more defense and 150 spending
     — more domestic reductions, both entitlements and appropriations
     — less (no) taxes
     — more non-tax revenues—asset sales, user fees, etc.

Pros:

- could avoid tax increase
- should achieve more domestic spending reductions
- marginally improves spending for defense and foreign affairs

Cons:

- requires modification or elimination of G-R-H
- will leave a substantial deficit for FY 1989 (the budget submission in Jan.)—with little prospect for improvement during an election year
- Congress may reject without some tax increase

3) Develop appropriations strategy, preferably in the confines a "new' budget

   1. need for a marker, other than President's budget
   2. do not have Republican support on appropriations bills
   3. will not achieve much reduction in CR fight

4) Timing of any offer or negotiations on budget

   1. after July 17, but before debt limit/G-R-H fight resolved?
   2. before markup of reconciliation/tax bills completed?
   3. after House votes on tax increase?
   4. as part of Mid-Session review?
   5. use of August recess to:
      — rail against tax increases?
      — promote new Presidential alternative?

August 3, 1987

TO : Senator Baker
FROM : Dan
RE : Catastrophic Health

Attached are two pieces from Joe Wright—a cover memo and comparison of the various bills. Note that none of the numbers come from OMB—they are provided by the actuaries at HHS and the Treasury. The HHS actuaries have been the source for all such calculations involving Social Security or Medicare in the past. Further, CBO has refused to estimate the costs of these bills more than 5-years out. The points about the Senate bill you may wish to raise at the GOP leadership meeting include:

- cost—while $4 billion the first year doesn't sound bad, the outyear costs are very large ($150 billion by 2010, barely 20 years from now)—this could easily be characterized as another Medicare (and the reason we have the entitlement problem we now face)—low buy-in entitlement with explosive long-term costs

- affordability—while the Senate bill is "actuarially sound" (i.e., raises as much revenue as it spends), the growth in costs will very quickly make it burdensome on the elderly and, eventually, will simply be unaffordable—when that happens, there will be an attempt to inject general revenues or raise payroll taxes to supplement the payments by the elderly

- tax increase—a portion of the premiums in the Senate bill are based on income level, which works out to be an effective tax increase on the elderly—the Senate mechanism is much better than the House, however, and an income-related premium is likely to be included in any Congressional outcome

- political consequences—of opposition or veto

Options

- Construct new alternative which provides catastrophic coverage, combines Medicare Parts A & B, allows for a private sector insurance alternative, etc., OR

- Attempt to modify the existing Senate bill by—

    - changing the index for the catastrophic floor to increase with program costs (rather than CPI)—this change alone would reduce out-year costs by approximately 40% (because medical costs are expected to increase much more than basic CPI)

    - add modest co-payments to all eligible services—with catastrophic protection, limiting the amount of out-of-pocket costs each year, co-payments would not break the elderly and would help utilization

    - a modest prescription drug amendment if we cannot avoid it