



BIPARTISAN POLICY CENTER

Background for Components of Step 2 (Savings of \$1.2 Trillion)

The following are detailed descriptions of the recommendations in Step 2 of the deficit reduction framework that the Task Force has outlined. The proposals include healthcare savings, cuts to other mandatory spending programs, modest additional cuts to discretionary spending, and revenue increases. The list of policies are drawn from [Restoring America's Future](#) (BPC), the BPC Task Force's original deficit reduction proposal, and also have been expanded to include measures from: the Simpson-Bowles [Fiscal Commission](#) (FC), the [Coburn-Lieberman](#) health reform Plan (CL), President Obama's [Deficit Reduction Plan](#) (Obama), Sen. Tom Coburn's [Back in Black](#), and the [Congressional Budget Office](#) (CBO) budget options. Additionally, some of the proposals were reportedly endorsed by the Biden-Cantor discussions (BC), or were included in the [House Republican budget](#) (House GOP).

*Bolded plan(s) under each option represents the (in some cases, slightly modified) description that is used

**All savings numbers are either CBO estimates, or savings projections from the original proposals

Medicare Savings

Update Medicare's cost-sharing rules, provide catastrophic coverage, and introduce a Part B premium surcharge for beneficiaries that purchase near first-dollar Medigap coverage

Identical or similar proposal endorsed by: BPC, FC, CL, Obama

Savings: \$93 billion

BPC proposal on cost-sharing/catastrophic coverage

Medicare's benefit structure, specified in legislation, has changed little since the program was implemented in 1966. In many areas, it has become obsolete.

For example, prescription drug coverage was widely adopted by private insurance companies during the 1970s, but was not included in Medicare until 2006, when a separate program (Part D) was implemented. Medicare also has not reflected trends in private insurance, such as protection against the costs of catastrophic illness and increased patient cost sharing. Patient cost sharing in Medicare is uneven, with very high deductibles for

inpatient care and no cost sharing at all for home health and laboratory services. Bringing the benefit structure up to date can reduce outlays while improving some dimensions, such as providing catastrophic protection and reducing the very high deductible for hospitalizations.

Some features of Medicare's benefit structure reflect the best thinking of 50 years ago and have not been updated since. For example, a large hospital deductible is assessed for each spell of illness and a separate deductible applies to Part B services. Home health and laboratory services have no deductible. This proposal will create a modern benefit structure for Medicare that is calibrated in a way that reduces spending overall. The modernized benefit structure will include a combined annual deductible of approximately \$560 in 2011. Once the deductible is met, a coinsurance rate of 20 percent will apply to all services, up to an annual out-of-pocket maximum of \$5,250. The deductible and out-of-pocket maximum will be indexed to increases in spending per beneficiary.

To avoid having the modernized benefit structure become outdated, the Independent Payment Advisory Board (IPAB), which ACA created to contain Medicare spending, will review the benefit structure every two years and recommend changes to parallel developments in the private insurance market. These recommendations will become law unless Congress acts to block them.

If private insurance continues to increase patient cost sharing and IPAB reflects this in its recommendations for Medicare, then savings from the proposal would be greater than what is reflected in the scoring.

This plan will provide more protection from the high costs of medical care associated with serious illness, while at the same time supplying beneficiaries with incentives to use medical care more judiciously. Individuals with multiple hospitalizations during a year will be better off, although those using other services may pay more for their care. The change might reduce beneficiaries' interest in purchasing private supplemental insurance (Medigap), because they will – for the first time – have catastrophic protection through Medicare and premiums for Medigap will increase.

Because Medigap coverage increases Medicare spending, less Medigap usage could further increase savings from this proposal (although these potential savings are not reflected in the scoring). The changed benefit structure will not impact the approximately 18 percent of beneficiaries with the lowest incomes, because Medicaid covers their Medicare cost sharing.

Obama proposal on Medigap

Medigap policies sold by private insurance companies provide beneficiaries additional support for covering healthcare costs by covering most or all of the cost sharing Medicare requires. This protection, however, gives individuals less incentive to consider the costs of health care services and thus raises Medicare costs and Part B premiums. Of particular

concern are Medigap plans that cover substantially all Medicare copayments, including even the modest co-payments for routine care that most beneficiaries can afford to pay out of pocket. To encourage more efficient health care choices, the Administration proposes a Part B premium surcharge equivalent to about 15 percent of the average Medigap premium (or about 30 percent of the Part B premium) for new beneficiaries that purchase Medigap policies with particularly low cost-sharing requirements.

*Note: This Medigap proposal is the same as the president's except that the one proposed here does not exempt current beneficiaries.

Reduce Medicare coverage of patients' bad debts

Identical or similar proposal endorsed by: FC, CL, Obama

Savings: \$20 billion

For most eligible provider types, Medicare currently generally reimburses 70 percent of bad debts resulting from beneficiaries' non-payment of deductibles and copayments after providers have made reasonable efforts to collect the unpaid amounts. Similar to the Fiscal Commission, this proposal will align Medicare policy more closely with private sector standards by reducing bad debt payments to 25 percent for all eligible providers over three years starting in 2013.

Accelerate home health savings in the ACA

Identical or similar proposal endorsed by: FC, CL

Savings: \$9 billion

The Affordable Care Act included several policies changing reimbursements for home health providers. The Commission recommends accelerating these changes to incorporate productivity adjustment beginning in 2013 and directing the Secretary of Health and Human Services (HHS) to phase in rebasing the home health prospective payment system by 2015 instead of 2017.

Introduce home health co-payments*

Identical or similar proposal endorsed by: Obama

CBO Option

Savings: \$40 billion

The Congressional Budget Office projects that the use of home health services, and the resulting costs to the Medicare program, will grow rapidly over the next 10 years, rising from about \$23 billion in 2012 to \$52 billion in 2021. One reason for the high level of spending is that Medicare beneficiaries are not required to pay any of the costs of home health services covered by the program.

This option would charge Medicare beneficiaries a copayment amounting to 10 percent of the total cost of each home health episode—a 60-day period of services— starting on January 1, 2013. That change would yield net federal savings of \$14 billion over the 2012–2016 period and \$40 billion over the 2012–2021 period. For Medicare beneficiaries who use home health services, the average increase in Medicare copayments in 2013 would be about \$600.

An argument in favor of this option is that it would directly offset a portion of Medicare’s home health outlays and encourage some beneficiaries to use those services in a cost-conscious manner. The use of services would also decrease, most likely among the approximately 10 percent of beneficiaries with fee-for-service Medicare only—that is, beneficiaries who do not have supplemental insurance, such as medigap or “wraparound” retiree coverage, and who are not enrolled in Medicaid or a health maintenance organization.

An argument against this option is that it would increase the risk of significant out-of-pocket costs for the 10 percent of Medicare enrollees who have fee-for-service coverage only—a population that tends to have lower income than do beneficiaries with private supplemental insurance. As a result, implementing the option could cause some of those individuals to forgo beneficial care. Among the majority of enrollees who have supplemental insurance, little or no drop in use would be expected because their supplemental policies would presumably be expanded to cover the home health copayment proposed in this option. For that reason, the approximately 25 percent of enrollees with individually purchased medigap policies would probably face higher premiums, and the costs of employment-based supplemental policies could also rise.

Finally, this option would result in increased spending by Medicaid for home health care for individuals who have both Medicare and Medicaid coverage; the federal share of higher Medicaid outlays is included in the estimated change in outlays.

Obama Proposal (primary difference is that it starts in 2017 and only affects new beneficiaries)

Savings: \$400 million

Medicare beneficiaries currently do not make co-payments for Medicare home health services. This proposal would create a home health copayment of \$100 per home health episode, applicable for episodes with five or more visits not preceded by a hospital or other inpatient post-acute care stay. This would apply to new beneficiaries beginning in 2017. This proposal is consistent with a MedPAC recommendation to establish a per episode copayment. MedPAC noted that “beneficiaries without a prior hospitalization account for a rising share of episodes” and that “adding beneficiary cost sharing for home health care could be an additional measure to encourage appropriate use of home health services.”

Use Medicare’s buying power to increase rebates from pharmaceutical companies

Identical or similar proposal endorsed by: BPC, FC, Obama

Savings: \$154 billion

The ACA increased required rebates in Medicaid for single source drugs from 15.1 percent to 23.1 percent. Under Medicare’s Part D program that covers prescription drugs, shopping for the best prices on single-source drugs has been delegated to the private insurers that provide the drug coverage. Each insurer negotiates rebates with manufacturers (often through pharmacy benefit managers or PBMs) based on its ability, through tiered benefit designs, to shift volume to those manufacturers that offer the largest rebates. Part D’s first year of operation – 2006 – produced rebates that averaged only 8.1 percent for drugs not available as generics. The federal government can more effectively use its potential purchasing power by requiring a minimum rebate for all single source drugs, and thereby achieve substantial budget savings. This proposal will apply the Medicaid approach to Medicare Part D, effectively increasing the rate of rebates by 15 percentage points.

CBO description

Medicare’s voluntary outpatient drug benefit, known as Part D, is delivered by private drug plans; federal subsidies for that coverage, net of the premiums that enrollees pay, totaled \$52 billion in 2010. (Those subsidies include payments to stand-alone prescription drug plans and prescription drug plans associated with Medicare Advantage plans, but they exclude subsidies provided to employers for prescription drug coverage provided by their

retiree health plans.) One way that those drug plans limit the cost of the Part D benefit is by negotiating rebates from the manufacturers of brand-name drugs in return for favorable coverage of those drugs, such as lower copayments for preferred drugs. That strategy is most likely to be effective for “single-source” drugs that are not available in generic form but face competition from other brand-name drugs to treat the same medical condition. The Congressional Budget Office estimates that in 2008, rebates under Part D averaged about 14 percent of gross spending on all brand-name drugs and a slightly higher percentage of spending on single-source brand-name drugs.

Prior to the establishment of Part D in 2006, Medicare beneficiaries who were also eligible for full benefits under Medicaid—known as “dual eligibles”—received drug coverage through Medicaid. Drug manufacturers are required to pay a significant rebate on their sales to Medicaid enrollees. In 2010, the minimum rebate in the Medicaid program was increased from 15.1 percent to 23.1 percent of the average manufacturer price (AMP)—that is, the price that manufacturers receive for sales to retail pharmacies; additional rebates are required if a drug’s price rises faster than general inflation. When Part D was established, dual eligibles were enrolled automatically in a low-income-subsidy (LIS) program, which typically covers the premiums and most of the cost sharing required under the basic Part D benefit. Overall, LIS beneficiaries account for about 40 percent of Part D enrollees and about 56 percent of Part D spending; most, but not all, LIS recipients are dual eligibles. Currently, the prices and rebates for drugs used by LIS enrollees are established in the same way as those for other Part D enrollees—that is, through negotiations between Part D plans and drug makers.

This option would require manufacturers of brand-name drugs to pay the federal government a rebate on drugs purchased by enrollees in the LIS program, starting in 2013. The program would reflect the current rebate system for Medicaid: Manufacturers would be responsible for a total rebate of at least 23.1 percent of the AMP, plus an additional rebate for price increases that exceeded the rate of inflation since the drug’s introduction. The difference between that amount and the amount of discounts and rebates that manufacturers already provide to Part D drug plans (as defined below) would be paid to the federal government. If the average Part D rebate for a given drug already exceeded the sum of 23.1 percent of the AMP plus the inflation-based rebate, however, no rebate would be paid to the federal government for that drug.

Manufacturers would be required to participate in the new Part D rebate program in order for their drugs to be covered by Parts B and D of Medicare, by Medicaid, and by the Veterans Health Administration. To reduce the amount of rebates owed to the federal government, rebates provided to Part D plans would have to apply to all drug purchases by all Part D enrollees. Therefore, if manufacturers set different rebate levels for different subgroups of beneficiaries, only the lowest rebate provided would be subtracted when determining the amount owed to the federal government on purchases by LIS beneficiaries. In particular, under this option, the 50 percent discount on brand-name drugs that manufacturers now have to provide for certain drug purchases would not reduce the rebate owed to the federal

government on purchases by LIS beneficiaries because that 50 percent discount applies only to a subgroup of drug purchases (those made by beneficiaries who are not enrolled in the LIS program for drugs purchased within a specified range of spending).

Under this option, manufacturers would continue to have an incentive to provide rebates to drug plans in exchange for preferred coverage of brand-name drugs, but that incentive would be smaller than under current law because the federal rebate would make the additional sales that would result from preferred coverage less profitable. The rebates obtained by drug plans for purchases by Part D enrollees would therefore be reduced, CBO expects. Moreover, drug makers would be expected to set higher “launch” prices for new drugs to limit the impact of the new rebate, particularly for new drugs that do not have close substitutes. Higher launch prices in response to a minimum rebate requirement in Part D would have varying effects on other drug purchasers. Employment-based health insurance plans would probably negotiate for larger rebates to offset the higher launch prices, but state Medicaid programs would pay a higher price for new drugs. Even after accounting for such offsets, CBO estimates that this option will generate savings to the federal government—about \$38 billion over the 2012–2016 period and about \$112 billion over the 2012–2021 period.

The main advantage of this option is that Medicare would pay less for drugs used by LIS beneficiaries in Part D. Advocates of this option might argue that manufacturers previously paid a rebate to Medicaid for drugs purchased by the dual-eligible population (who constitute the majority of LIS beneficiaries) before those beneficiaries were reassigned to the Part D benefit, so there is a recent precedent for requiring such rebates for that population.

A disadvantage of the option is that the net reduction in the prices paid for drugs under Part D might reduce the amount of funds that manufacturers invest in research and development of new products. Relative to current law, the option would not significantly reduce the incentive to develop “breakthrough” drugs because those drugs could be launched at prices that were high enough to largely offset the rebate. However, the new rebate would apply to LIS beneficiaries who are not dual eligibles, so the magnitude of the total required rebates would be larger than when dual eligibles received their drug coverage from Medicaid; consequently, the adverse impact on manufacturers’ incentives would probably be larger than it was prior to the creation of Part D.

Bundle Medicare's payments / reform provider payments for post-acute care to reduce costs*

Identical or similar proposal endorsed by: BPC, Obama

BPC Proposal – Bundle Payments

Savings: \$42 billion

Medicare's inpatient prospective payment system provides an undesirable incentive to hospitals to shorten lengths of stay and discharge patients to skilled nursing facilities or rehabilitation facilities. This motivation can be corrected by broadening the applicability of the inpatient Diagnosis Related Group (DRG) payment to post-acute services. A larger DRG payment will go to the hospital providing acute care, which will also be responsible for the costs of post-acute services. The new bundled payment rates will be budget neutral, with a plan to capture 80 percent of the efficiencies gained from the broader payment unit for the program and allow hospitals to retain 20 percent.

In general, broader units of payment can encourage providers to take into account the costs incurred by others in treating a patient, and therefore motivate coordinated care. The ACA takes a number of steps toward broader units of payment for Medicare, but more can be done. These savings opportunities might be particularly large for post-acute care, because payment limitations for inpatient care on a per admission basis likely already induce hospitals to discharge patients to post-acute facilities as early as possible, even if overall costs are inflated as a result. The payment bundles can be broadened to include post-acute care by raising payments to DRGs based on historical experience of use of post-acute care, and then requiring hospitals to cover payment for these services. Broadening the bundle will likely increase efficiency, partly by engaging hospitals as potentially sophisticated purchasers of post-acute care. These efficiency gains can be captured by the program through monitoring changes in the use of post-acute services and adjusting DRG payment rates to reflect the changing experience. Hospitals can either develop contractual relationships with select post-acute facilities or provide the services themselves in facilities that the hospitals purchase or create.

Obama Proposals – Reform Provider Payments

Savings: \$42 billion

- **Encourage efficient post-acute care.** Medicare covers services in skilled nursing facilities (SNFs), long-term care hospitals (LTCHs), inpatient rehabilitation facilities (IRFs) and home health. Over the years, expenditures for these services have increased dramatically, and payments in excess of the costs of providing high quality

and efficient care place a drain on Medicare. Recognizing the importance of these services, the Administration supports the following policies:

- **Adjust payment updates for certain post-acute care providers.** MedPAC analysis indicates that Medicare payment significantly exceeds the cost of patient care in post-acute care settings, resulting in high Medicare margins. This proposal would gradually realign payments with costs through adjustments to payment rate updates in 2014 through 2021 for these providers. These adjustments build on recommendations from MedPAC's March 2011 Report to the Congress, in which they recommended that the Congress eliminate payment updates for each of these provider types in 2012.
- **Equalize payments for certain conditions commonly treated in IRFs and SNFs.** Post-acute care related to a number of conditions, including hip and knee replacements, hip fractures, and certain pulmonary diseases are currently provided in both IRFs and SNFs, although Medicare payments are significantly greater when treated in IRFs. This policy would reduce the differences in payment for treatment of specified conditions to encourage care in the most clinically appropriate setting beginning in 2013.
- **Encourage appropriate use of inpatient rehabilitation hospitals.** Medicare pays IRFs at a rate that reflects specialized rehabilitation care to patients with the most intensive needs. IRFs must demonstrate this by meeting a compliance threshold which specifies a minimum percentage of patients with designated medical conditions that require intensive rehabilitation services. Starting in 1984, this compliance threshold was set at 75 percent, but it was reduced to 60 percent in 2007. This proposal would return the compliance threshold to its previous 75 percent level beginning in 2013 to better ensure that the higher IRF payments apply to cases requiring this level of care.
- **Adjust SNF payments to reduce hospital readmissions.** The Affordable Care Act created payment adjustments for inpatient hospitals with high rates of readmissions, many of which could be avoided through better care. However, a comparable adjustment does not exist for SNFs. MedPAC analysis shows that nearly 14 percent of Medicare patients that are discharged from a hospital to a SNF are readmitted to the hospital for conditions that could have been avoided. To promote high quality care in SNFs, this proposal reduces SNF payments by up to three percent beginning in 2015 for facilities with high rates of care-sensitive, preventable hospital readmissions.

Better Align Graduate Medical Education Payments with Patient Care Costs*

Identical or similar proposal endorsed by: FC, Obama, Coburn (also a CBO option)

Obama's proposal

Savings: \$9 billion

Medicare compensates teaching hospitals for the indirect costs stemming from inefficiencies created from residents "learning by doing." The Medicare Payment Advisory Commission (MedPAC) has determined that these Indirect Medical Education (IME) add-on payments are significantly greater than the additional patient care costs that teaching hospitals experience, and the Fiscal Commission, among others, recommended reducing the IME adjustment. This proposal would reduce the IME adjustment by 10 percent beginning in 2013, and save approximately \$9 billion over 10 years.

Fiscal Commission proposal

Savings: \$60 billion

Medicare provides supplemental funding to hospitals with teaching programs for costs related to residents receiving graduate medical education (GME) and indirect costs (IME). The Commission recommends bringing these payments in line with the costs of medical education by limiting hospitals' direct GME payments to 120 percent of the national average salary paid to residents in 2010 and updated annually thereafter by chained CPI and by reducing the IME adjustment from 5.5 percent to 2.2 percent, which the Medicare Payment Advisory Commission has estimated would more accurately reflect indirect costs.

CBO Mandatory Spending Option 17

Savings: \$69 billion

This option would consolidate all mandatory federal spending for GME into a grant program for teaching hospitals. Total funds available for distribution would be based on the 2011 aggregate payments for DGME and Medicaid GME plus the 2011 aggregate payments for IME reduced to reflect a 2.2 percent IME adjustment. Total funding for the grant program would grow with inflation as measured by the consumer price index for all urban consumers minus 1 percentage point per year. Payments would be apportioned according to the number of residents at a hospital and the portion of the hospital's inpatient days accounted for by Medicare and Medicaid patients.

In CBO's estimation, this option would save approximately \$25 billion over the 2012–2016 period and roughly \$69 billion over the 2012–2021 period. By 2021, the annual savings would represent about 60 percent of federal spending for GME projected under current law.

Under Medicare's prospective payment system for inpatient medical services, hospitals with teaching programs receive additional funds for costs related to graduate medical education (GME). One component of that additional funding, direct graduate medical education (DGME), covers a portion of a teaching hospital's costs for compensation of physicians serving as medical residents and for institutional overhead. DGME payments are based on a hospital's 1984 costs per resident (indexed for changes in consumer prices), the number of residents, and Medicare's share of total inpatient days at that hospital. The other component, indirect medical education (IME), is intended to cover teaching-related costs that are not attributable either to residents' compensation or to other direct costs of running a residency program. Examples of IME costs are the added demands placed on staff as a result of teaching activities and the greater number of tests and procedures ordered by residents as part of the learning and teaching process. Teaching hospitals also tend to treat a larger proportion of severely ill patients, which raises costs. Under current law, for every increase of 0.1 in the ratio of full-time residents to the number of beds, the IME adjustment provides teaching hospitals with about 5.5 percent more in payments. However, the Medicare Payment Advisory Commission (MedPAC) has consistently found that the IME calculation overstates the effect of teaching status on incurred costs. In its most recent (March 2010) report to the Congress on Medicare's payment policy, MedPAC estimates that an IME adjustment of about 2 percent more closely reflects the indirect costs that teaching hospitals actually incur.

An argument for reducing the subsidy for GME is that federal payments under current law exceed hospitals' actual teaching costs. As MedPAC's analysis suggests, a smaller subsidy would create savings for the federal budget without unduly affecting hospitals' teaching activities. A smaller subsidy would also remove an incentive for hospitals to have a greater number of residents than may be necessary. If hospitals responded to the reduction in the subsidy by lowering residents' compensation, residents would bear more of the cost of their medical training, which might deter some people from entering the medical profession. However, medical training enables individuals to earn a significantly higher income in the future, and market incentives appear to be sufficient to encourage people to become physicians.

An argument against this option is that reducing the federal subsidy for GME could lead some teaching hospitals to train fewer residents or devote less time and fewer resources to beneficial educational activities. Also, to the extent that some teaching hospitals use a portion of their additional payments to fund care for uninsured individuals, decreasing those payments could reduce the number of patients that hospitals treat or lower the quality of care that those hospitals provide. Another argument against

the option is that states could lose some discretion to direct Medicaid GME payments to hospitals because the federal government would be administering the grant program. Finally, even if payments were initially equal to hospitals' costs, the payments would grow more slowly than inflation and thus might not keep pace with increases in costs.

Reduce or Eliminate the Critical Access Hospital (CAH), Medicare-Dependent Hospital (MDH), and Sole Community Hospital Programs (SCH) in Medicare*

Identical or similar proposal endorsed by: BC, Obama (also a CBO option)

President Obama's proposal to reduce these programs

Savings: \$6 billion

*Note: Reportedly, Biden and Cantor agreed to **\$14 billion** in savings from these programs

Medicare makes a number of special payments to account for the unique challenges of delivering medical care to beneficiaries in rural areas. These payments continue to be important; however, in specific cases, the adjustments may be greater than necessary to ensure continued access to care. The Administration proposes to improve the consistency of payments across rural hospital types, provide incentives for efficient delivery of care, and eliminate higher than necessary reimbursement. First, the Administration proposes to end an add-on payment for hospitals and physicians in low-population States. Currently, hospitals and physicians in certain low-population States receive a special payment adjustment that exceeds the amount indicated by their labor costs or certain other costs. This proposal would end this add-on payment in 2013, to better align providers' payments with their costs, and will save approximately \$2 billion over 10 years. Secondly, to improve payment accuracy for Critical Access Hospitals (CAHs), the Administration proposes to reduce payments from 101 percent to 100 percent of reasonable costs and to eliminate the CAH designation for those that are fewer than 10 miles from the nearest hospital. This will ensure that this unique payment system is better targeted to hospitals meeting the eligibility criteria. These two CAH proposals will save approximately \$4 billion over 10 years. Together, these rural proposals will save approximately \$6 billion over 10 years.

CBO Mandatory Spending Option 24: Eliminate subsidies to rural hospitals

Savings: \$62 billion

Hospitals designated as critical access hospitals (CAHs), Medicare-dependent hospitals (MDHs), and sole community hospitals (SCHs) are exempt from the Inpatient Prospective

Payment System (IPPS) through which Medicare pays for services provided by most acute care hospitals. Eligibility for the CAH, MDH, and SCH designations is based on several factors, including size and location. Most of the hospitals exempt from the IPPS are small, rural facilities. Some of those hospitals receive payments equal to 101 percent of the costs of providing care, while others receive payments based on a blend of IPPS rates and their costs. Hospitals benefiting from the special adjustments for CAHs, MDHs, and SCHs are paid about 25 percent more, on average, for inpatient and outpatient services than the payments that would otherwise apply. Currently, one-third of hospitals benefit from those designations and account for about 10 percent of total Medicare spending for hospital inpatient services.

This option would eliminate the CAH, MDH, and SCH programs and end the higher Medicare payments made to those facilities. Instead, payment to those hospitals, as with other hospitals paid through the IPPS, would be determined prospectively on the basis of the following: patients' diagnoses and the severity of their illness or injury; geographic variations in hospital "input" costs (for example, for professional labor or medical supplies); and certain other hospital- and patient-specific factors, such as the hospital's teaching status and Medicaid caseload. By eliminating the CAH, MDH, and SCH programs and the higher payments to hospitals participating in those programs, this option would reduce federal outlays by \$23 billion over the 2012–2016 period and by approximately \$62 billion over the 2012–2021 period.

An argument in favor of eliminating the CAH, MDH, and SCH programs is that doing so would move Medicare toward a payment structure that compensates all hospitals in a consistent manner. Smaller rural hospitals would no longer be able to participate in programs that compensated them at relatively higher rates. Additionally, this option might improve efficiency in the health care system. IPPS payments are intended to encourage efficiency by compensating hospitals for the costs that reasonably efficient providers would incur in furnishing high-quality care (including adjustments for local input costs). By placing CAHs, MDHs, and SCHs under the IPPS, those hospitals would face greater incentives to provide efficient care.

A potential drawback of this option is that the special payments currently made to the CAHs, MDHs, and SCHs may offset the higher costs of operating smaller facilities in rural areas. If those hospitals are not able to reduce their costs under the IPPS, the increased financial pressure resulting from the elimination of special payments to CAHs, MDHs, and SCHs might force some of those hospitals to convert to outpatient facilities or even to close. To the extent that occurred, patients who reside in those areas might have difficulty getting access to care.

Increase Part B deductible for new beneficiaries

Identical or similar proposal endorsed by: Obama

Savings: \$4 billion

Beneficiaries who are enrolled in Medicare Part B are required to pay an annual deductible. This deductible helps to share responsibility for payment of Medicare services between Medicare and beneficiaries. To strengthen program financing and encourage beneficiaries to seek high-value health care services, we propose to apply a \$25 increase in the Part B deductible in 2014, 2016, and 2018 for new beneficiaries. Current beneficiaries or near retirees would not be subject to the revised deductible.

Eliminate Provider Carve-Outs from IPAB

Identical or similar proposal endorsed by: FC

Savings: --

The Affordable Care Act established the Independent Payment Advisory Board to recommend changes in Medicare payment policies if per-beneficiary Medicare spending grows too quickly. However, the law exempted certain provider groups, most notably hospitals, from any short-term changes from IPAB's authority. The Commission recommends eliminating these carve-outs.

Make Reforms to Medicare's Quality Improvement Organizations (QIO)

Identical or similar proposal endorsed by: Obama, Coburn

Savings: \$3 billion

Quality Improvement Organizations (QIOs) are private, mostly not-for-profit organizations that contract with Medicare to improve the effectiveness, efficiency, economy, and quality of services delivered to Medicare beneficiaries.

President Obama's FY2012 Budget recommended a series of specific changes to QIOs. Like previous efforts in Medicare to modernize contracting by consolidating 40 fiscal intermediaries to 15 Medicare Administrative Contractors, these reforms increase

competition, align procedures with the Federal Acquisitions Regulations, and strengthen the Trust Funds. These changes should be implemented to save taxpayers more than \$3 billion over a decade:

By requiring the Secretary to determine the geographic scope of contracts, including overlapping contracts in local, regional, or national areas when appropriate, this proposal will increase competition and eliminate overhead.

The proposal also eliminates conflicts of interest between beneficiary protection and quality improvement activities, which may arise when a single contractor is responsible for building relationships with providers to improve quality while also functioning as the entity charged by Medicare to hold providers accountable for failures in the delivery of care to beneficiaries.

The proposal expands the pool of contractors eligible for QIO work, which will increase competition, and ensure that beneficiaries and providers are served effectively by contractors with specific skills.

Finally, extending the QIO contract length from three years to up to five years, and aligning QIO contract terminations with Federal Acquisition Regulations will improve efficiency and increase the Secretary's flexibility in administering these contracts.

One-year SGR fix

Cost: \$12 billion

This one-year fix would serve as a bridge until the second phase of savings is enacted, wherein the formula would be permanently fixed and paid for.

Medicaid and Other Healthcare Savings

Eliminate state gaming of Medicaid tax gimmick

Identical or similar proposal endorsed by: FC, Obama

Savings: \$26 billion

Many States impose taxes on health care providers to help finance the State share of Medicaid program costs. However, some States use those tax revenues to increase payments to those same providers, and use that additional spending to increase their Federal Medicaid matching payments. The Administration proposes to limit these types of State financing practices that increase Federal Medicaid spending, by phasing down the Medicaid provider tax threshold, from the current law level of 6 percent in 2014, to 4.5 percent in 2015, 4 percent in 2016, and 3.5 percent in 2017 and beyond. By delaying the effective date until 2015, the proposal protects States from reductions in the short term.

Apply a single blended matching rate to Medicaid and CHIP starting in 2017

Identical or similar proposal endorsed by: Obama

Savings: roughly \$21 billion

Under current law, States face a patchwork of different Federal payment contributions for individuals eligible for Medicaid and CHIP. Specifically, State Medicaid expenditures are generally matched by the Federal Government using the Federal medical assistance percentage (FMAP); CHIP expenditures are matched with enhanced FMAP (eFMAP); and the Affordable Care Act provides increased match for newly-eligible individuals and certain childless adults beginning in 2014. Beginning in 2015 this proposal would replace these complicated formulas with a single matching rate specific to each State that automatically increases if a recession forces enrollment and State costs to rise.

*Note: This blended rate proposal is the same as the president's except that the one proposed here starts in 2015 instead of 2017.

Re-base Medicaid disproportionate share hospital (DSH) allotments in 2021

Identical or similar proposal endorsed by: Obama

Savings: \$4 billion

This proposal continues the Affordable Care Act policy to better align Medicaid DSH payments with reductions in the number of uninsured in 2021 and beyond. Supplemental DSH payments are intended to help support hospitals that provide care to disproportionate numbers of low-income and uninsured individuals. The Affordable Care Act reduced State DSH allotments by \$18.1 billion through 2020 to reflect the reduced need as a result of the increased coverage provided in the Act. The Administration proposes to compute 2021 State DSH allotments based on States' actual 2020 DSH allotments, better aligning future Medicaid supplemental payments to hospitals with reduced levels of uncompensated care.

Limit Medicaid reimbursement of durable medical equipment (DME) based on Medicare rates

Identical or similar proposal endorsed by: BC, Obama

Savings: \$4 billion

Under current law, States have experienced the same challenges in preventing overpayments for DME that previously confronted Medicare. The Medicare program is in the process of implementing innovative ways to increase efficiency for payment of DME through the DME Competitive Bidding Program, which is expected to save the Medicare program more than \$17 billion and Medicare beneficiaries approximately \$11 billion over 10 years. This proposal extends some of these efficiencies to Medicaid, starting in 2013, by limiting Federal reimbursement for a State's Medicaid spending on certain DME services to what Medicare would have paid in the same State for the same services.

Shorten exclusivity period for brand name biologic drugs

Identical or similar proposal endorsed by: Obama

Savings: \$4 billion

Access to affordable lifesaving medicines is essential to improving the quality and efficiency of health care. The Administration's proposal accelerates access to affordable generic biologics by modifying the length of exclusivity on brand name biologics to encourage faster development of generic biologics while retaining appropriate incentives for research and development for the innovation of breakthrough products. Beginning in 2012, this proposal would award brand biologic manufacturers seven years of exclusivity rather than 12 years under current law and prohibit additional periods of exclusivity for brand biologics due to minor changes in product formulations, a practice often referred to as "evergreening." Reducing the exclusivity period increases the availability of generic biologics to encourage faster development of generic biologics while retaining appropriate incentives for research and development for the innovation of breakthrough products. The Administration's proposal strikes a balance between promoting affordable access to medications and encouraging innovation to develop needed therapies. The proposal will result in \$3.5 billion in savings over 10 years to Federal health programs including Medicare and Medicaid.

Prohibit "pay for delay" agreements to increase the availability of generic drugs and biologics

Identical or similar proposal endorsed by: Obama

Savings: \$3 billion

The high cost of prescription drugs places a significant burden on Americans today, causing many to skip doses, split pills or forgo needed medications altogether. The Administration proposes to increase the availability of generic drugs and biologics by authorizing the Federal Trade Commission (FTC) to stop companies from entering into anti-competitive deals, known also as "pay for delay" agreements, intended to block consumer access to safe and effective generics. A 2010 Federal Trade Commission study that evaluated the universe of brand-generic settlements and 2008 drug expenditure data found that on average, these agreements delayed entry of a generic by 17 months and cost American consumers as much as \$3.5 billion per year. More recently, the FTC reported that the number of pay-for-delay agreements skyrocketed from 19 in 2009 to 31 in 2010.

Such deals block access to generics and can cost consumers billions of dollars because generic drugs are typically priced significantly less than their branded counterparts. These agreements reduce competition and raise the cost of care for patients both directly, through higher drug and biologic prices, and indirectly through higher health care premiums. The Administration's proposal facilitates greater access to lower-cost generics and will generate \$2.7 billion over 10 years in savings to Federal health programs including Medicare and Medicaid.

Track High Prescribers and Utilizers of Prescription Drugs in Medicaid

Identical or similar proposal endorsed by: Obama, Coburn

Savings: \$4 billion

States currently have the capability to implement monitoring systems for prescription drugs, but are not taking full advantage of these systems' potential benefits. President Obama's FY2012 budget proposed requiring the Department of Health and Human Services to track drug claims for indications of fraud, waste, or abuse by providers or beneficiaries and to take steps to reduce wasteful or abusive prescribing practices.

Reduce waste, fraud, and abuse in Medicaid

Identical or similar proposal endorsed by: Coburn, Obama

Savings: \$1 billion

Medicaid funds should not be wasted on fraudulent claims, abuses of the rules, or general waste in implementing the program. The following policies will save \$110 million over the next 10 years while reducing waste, fraud, and abuse:

- **Require manufacturers that improperly report items for Medicaid drug coverage to fully repay States.** Federal law requires manufacturers to report a list of their "covered outpatient drugs" to CMS for Medicaid drug coverage, but some manufacturers improperly report items that do not belong (e.g., syringes). This proposal would recoup costs of covering improperly-reported items discovered after Medicaid reimbursement has occurred; the proposal leverages the Medicaid drug rebate program by directing manufacturers to pay a "rebate" equal to the amount the State paid for these items.
- **Track high prescribers and utilizers of prescription drugs in Medicaid.** States already have the capability to implement monitoring systems for prescription drugs, but are not currently taking full advantage of these systems' potential benefits. This proposal requires States to track drug claims for indications of waste, fraud, or abuse by providers or beneficiaries and to take steps to reduce wasteful or abusive prescribing practices.

- **Enforce Medicaid drug rebate agreements.** Under this proposal, HHS would, when cost-effective, conduct regular audits and surveys of Medicaid drug rebate agreements to ensure the Medicaid program is receiving proper prices and rebate amounts.
- **Increase penalties on drug manufacturers for fraudulent non-compliance with Medicaid drug rebate agreements.** This proposal would increase the statutory civil monetary penalties on manufacturers that knowingly report false information under their drug rebate agreements for calculation of Medicaid rebates.
- **Require drugs to be properly listed with the FDA to receive Medicaid coverage.** Though FDA law requires manufacturers to list their drugs with FDA, compliance is inconsistent. Recently, Medicare required that drugs must be properly listed with the FDA to receive Part D coverage; this proposal would add the same requirement in Medicaid.

Other Healthcare Savings

Require states to cap awards for noneconomic and punitive damages for medical malpractice

Identical or similar proposal endorsed by: BPC, FC, Coburn

Savings: \$62 billion

CBO Description

Individuals may pursue civil claims against physicians, hospitals, and other health care providers for alleged torts, which are breaches of duty that result in personal injury. That system of tort law has twin objectives: deterring negligent behavior on the part of providers and compensating claimants for losses they incur (including lost wages, medical expenses, and pain and suffering) as the result of an injury caused by negligence. Malpractice claims are generally pursued through the state courts, and states have established various rules by which those claims are adjudicated. Nearly all health care providers obtain malpractice insurance to protect against the risk of having to pay a very large malpractice claim. The cost of that insurance results in higher medical costs because, in order to pay for the premiums, providers charge their patients higher fees. Furthermore, research suggests that placing limits on malpractice torts will reduce the quantity of prescribed health care services by a small amount.

This option would impose certain nationwide curbs on medical malpractice torts. Many states have enacted some or all of these limits, whereas others have very few restrictions on malpractice claims. The tort limits include caps on noneconomic damages (also known as pain and suffering) and on punitive damages; a shortened statute of limitations; restrictions on the use of joint-and-several liability; and changes to rules regarding collateral sources of income. The specific components of medical malpractice tort reform under this option are as follows:

- A cap of \$250,000 on awards for noneconomic damages;
- A cap on awards for punitive damages of \$500,000 or two times the value of awards for economic damages, whichever is greater;
- A statute of limitations of one year from the date of discovery of the injury for adults, and three years for children;

- A fair-share rule (replacing the rule of joint-and several liability) under which a defendant in a lawsuit would be liable only for the percentage of the final award that was equal to that defendant's share of responsibility for the injury; and
- Permission to introduce evidence of income from collateral sources (such as life insurance payouts and health insurance) at trial.

Malpractice tort limits would reduce total health care spending in two ways. First, by reducing the average size of malpractice awards, tort limits would reduce the cost of malpractice insurance premiums. That reduced cost of malpractice insurance paid by providers would flow through to health plans and patients in the form of lower prices for health care services. Second, as noted above, tort limits would also reduce utilization of health care services by a small amount as practitioners prescribed somewhat fewer services when faced with less pressure from potential malpractice claims. In the estimation of the Congressional Budget Office, the combined effect of those two factors would be a reduction of about 0.5 percent of total health care spending. For this option, CBO assumed that a change enacted in October 2011 would have an impact that increased over time, achieving its full effect after four years, as providers gradually changed their practice patterns. In terms of federal health care spending, the percentage decline in spending for Medicare is estimated to be larger than the decline in spending for other federal health programs or for national health spending. That estimate is based on empirical evidence showing that the impact of tort reform on the use of health care services is greater for Medicare than for the rest of the health care system.

By reducing spending on health care in the private sector, this option would also affect federal revenues. Much private-sector health care is provided through employment-based insurance that represents nontaxable compensation. Because premiums paid by employers for health insurance are excluded from employees' taxable income, reducing such premiums would, on average, increase the share of employees' compensation that was taxable and thereby increase federal tax revenues by an estimated \$13 billion over the next 10 years.

This option would reduce mandatory spending for Medicare, Medicaid, the Children's Health Insurance Program, subsidies for coverage purchased through health insurance exchanges, and the Federal Employees Health Benefits program by a total of roughly \$50 billion from 2012 to 2021. Discretionary savings would amount to \$400 million over the 2012–2016 period and \$1.6 billion over the 2012–2021 period, if the amounts appropriated for federal agencies were reduced accordingly.

An argument in favor of this option is that it would reduce spending for health care services. Another rationale is that, by reducing premiums for medical malpractice insurance, the option could help alleviate shortages of certain types of physicians in some areas of the country. For example, annual malpractice premiums for obstetricians exceed \$100,000 in

some areas. Such high premiums may deter some obstetricians from practicing in those areas or from practicing at all.

An argument against this option is that tort limits could prevent those who have suffered substantial harm as a result of medical negligence from obtaining full compensation for their injuries. In addition, reducing the amount of money that could be collected in the case of a medical injury might cause providers to exercise less caution, resulting in an increase in the number of medical injuries attributable to negligence.

The evidence is mixed on whether tort limits have an adverse effect on health outcomes. Some researchers who have observed a reduction in the use of health care services as the risk of litigation falls have also found that reducing that risk produces a small increase in the mortality rate. Another study found that reform of joint-and-several liability had positive impacts on health but caps on noneconomic damages had negative impacts. Other studies have concluded that tort limits have no effect on mortality or other measures of health.

Targeted increases to TRICARE pharmacy benefit co-payments

Identical or similar proposal endorsed by: BPC, BC, Coburn, **Obama**

Savings: \$15 billion

The Administration supports a generous health care benefit to recognize the service of military members and retirees. This includes providing affordable options to access prescriptions. However, the co-payments for military members have lagged behind other Federal and private plans. For example, the average co-payment for a costly brand-name drug purchased at a drug store by a Federal retiree in the most popular Federal Employees Health Benefits Program (FEHBP) plan option is estimated to be \$45, compared to \$9 for a military retiree. In an effort to slow the growth in DOD's health care costs, the President's 2012 Budget included minor pharmacy co-pay adjustments, for which both the House and Senate indicated support. This new proposal would move the TRICARE pharmacy program closer to parity with the most popular Federal employee health plan, BlueCross BlueShield Standard and closer to the health plans that most Americans have from their employers. The proposal would provide an incentive for consumers to choose less expensive pharmacy options by eliminating co-pays for generic mail-order drugs while, at the same time, shifting retail co-pays from a dollar figure to a percentage co-pay. This option would have no impact on active duty members, but would affect active duty families and all military retirees regardless of the age of the beneficiary.

Initiate annual fees for TRICARE-For- Life enrollment (TFL)

Identical or similar proposal endorsed by: BPC, BC, Coburn, **Obama**

Savings: \$6.7 billion

One of the ways military retirees and their families are recognized for their essential service is through health insurance coverage called TRICARE. Upon turning 65, beneficiaries transition to Medicare coverage, with TFL becoming second payer. The TFL program pays the beneficiaries' Medicare out-of-pocket costs for medical services, generally leaving the beneficiary with no out-of-pocket costs aside from Medicare Part B premiums and drug co-pays. In the private sector, this type of "Medigap" policy would likely require premiums, deductibles, and co-pays. In 2009 the average annual premium for a "Medigap" policy was \$2,100. By contrast, there are no premiums under the TFL programs. The Administration is proposing to introduce modest annual fees for the TFL program, beginning with a \$200 annual fee in 2013. The fee then would increase to align with the modest increase in the fees under the regular TRICARE program for individuals under age 65 that was proposed in the President's 2012 Budget. This proposal is estimated to save approximately \$6.7 billion in mandatory spending over 10 years.

Decrease investment in prevention and public health fund

Identical or similar proposal endorsed by: **Obama**

Savings: \$4 billion

The Prevention and Public Health Fund has supported effective, evidence-based public health activities that restrain health care costs and improve health outcomes, such as immunizations and reductions of health care associated infections. The Administration proposes to scale-back the Fund by reducing resources by \$3.5 billion over 10 years starting in 2014, while maintaining high priority activities that improve health outcomes and restrain the rate of growth in private and public sector health care costs. Prioritizing Prevention Fund activities would allow for significant investments in prevention and public health activities of more than \$6 billion over five years and \$13.8 billion over 10 years, while providing \$3.5 billion in savings.

Include Social Security benefits in income calculation to determine Exchange subsidy eligibility

Identical or similar proposal endorsed by: Obama

Savings: \$15 billion

Starting in 2014, eligibility for Exchange tax credits and cost sharing reductions, Medicaid, and CHIP will be determined based on an individual's or families' MAGI, as defined under the Affordable Care Act. Similar to legislation currently under consideration by the Congress, the Administration proposes to amend that definition to include the total amount of Social Security benefits in the calculation of MAGI, rather than just the taxable portion, when determining eligibility for these programs to better target those in need.

Other Mandatory Savings

Use a More Accurate Cost-of-Living Adjustment (COLA) for All Federal Benefit Programs

Identical or similar proposal endorsed by: BPC, FC, Coburn

Savings: \$145 billion

The COLA for all federal benefit programs (e.g., federal and military pensions) is linked to changes in the Consumer Price Index for Urban Wage Earners (CPI-W). Many analysts and economists, however, believe that the CPI-W can overstate inflation because it does not fully account for changes in consumer spending resulting from increases in prices. (For example, when the price of apples goes up, people can reduce the impact by substituting oranges.) This proposal recommends switching the basis for COLA adjustments in these programs from the CPI-W to the “chain-weighted” Consumer Price Index for All Urban Workers (CPI-U). This alternative measure more accurately reflects price changes due to inflation and will grow at an estimated 0.3 percentage points more slowly than the CPI-W over the next 10 years. Using the Chained CPI-U will reduce federal outlays while still providing better protection against inflation than most private pensions.

Reform Civilian Retirement

Identical or similar proposal endorsed by: BPC, FC, Coburn, Obama

BPC: Adjust the formula to account for highest five consecutive years of earnings

Savings: \$5 billion

The federal government calculates pension benefits using the average of an employee’s highest three consecutive years of earnings. This proposal offers a technical adjustment to that formula, replacing the current metric with the average of an employee’s highest five consecutive years of earnings.

The federal government has two major retirement plans for civilian employees: the Civil Service Retirement System (CSRS), which covers federal employees hired before 1984, and the Federal Employees Retirement System (FERS), which Congress instituted in 1986. Both systems provide benefits that are based on the average of an employee’s highest three consecutive years of earnings. This proposal extends the calculation for both programs to a five-year average.

Using the longer period will better align federal pension practices with those in the private sector, which commonly uses a five-year average to calculate base pensions. The change will also generate budget savings without reducing current retirees' benefits, and will create an incentive for some federal employees to work longer in order to boost their pensions, thereby helping the government retain experienced personnel.

Coburn, Obama: Eliminate FERS special supplement for new annuitants

Savings: \$1 billion

Because Social Security retirement benefits cannot begin before the age of 62 (at the early retirement age), Congress included in FERS a temporary supplemental benefit for workers who retire before age 62. This —FERS supplement|| is paid to workers who retire at the age of 55 or older with at least 30 years of service or at the age of 60 with at least 20 years of service. It is also paid to law enforcement officers, firefighters, and air traffic controllers who retire at the age of 50 or later with 20 or more years of service. The supplement is equal to the estimated Social Security benefit that the individual earned while employed by the federal government. It is paid only until the age of 62, regardless of whether the retiree chooses to apply for Social Security retired worker benefits at 62 years old.

Obama: Increase FERS contributions

Savings: \$20 billion

The Administration is proposing that the employee contribution toward accruing retirement costs would increase by a total of 1.2 percent (0.4 percent a year over three years beginning in 2013), but the employee's total pension would remain unchanged. While Federal agency contributions for currently accruing costs of employee pensions would decline, these employers would pay an additional amount toward unfunded liabilities of the retirement system that would leave total agency contributions unchanged over the 10- year budget window.

Coburn (also a Third Way proposal): Equalize FERS contributions

Savings: \$121 billion

As the required federal government contributions to FERS skyrocket, federal worker contributions are not expected to keep pace. This reform equalizes FERS contributions between the employee and employer. OPM estimates the cost of the FERS basic annuity at an amount equal to 12.5 percent of pay (CRS). The federal government contributes 11.7 percent of this amount and the other 0.8 percent is paid by employees. This reform would also put federal employees on par with state and local employees.

Reform military retirement

Identical or similar proposal endorsed by: BPC, FC, Obama

Savings: \$4 billion

This proposal will gradually replace the current military retirement system's defined-benefit plan with one modeled on the Federal Employees Retirement System (FERS). FERS includes Social Security, a modest defined-benefit plan, and a defined contribution plan in which employee contributions are matched by the federal government. The proposed military plans also will allow vesting before 20 years of service and provide protection from inflation. Military retirees could receive benefits as early as age 57 (depending on their length of service), as is the case for civilian retirees. Military personnel with more than 15 years of service will remain a part of the current system, but all others will transition into the new structure.

The current military retirement system operates with a "cliff-vesting" benefit schedule: service members who retire after 20 or more years of service are 100 percent vested and receive full benefits from the moment they depart, while service members who separate at any point before 20 years receive no benefit. Under the present system, members who serve for 20 years receive immediate, inflation-protected annuities for life at an accrual cost of more than 30 percent of basic pay, a rate that is far above that of civilian pension programs.

This retirement system is inequitable because most members do not complete 20 years of service and thus receive no benefits, inefficient because it uses deferred compensation rather than current pay to incentivize service member retention, and costly because payments begin immediately upon leaving the service. Military personnel typically retire in their early- to mid-40s and move to second careers. The cliff-vesting provisions also result in an inflexible military manpower system, with excess personnel in the cadre that have 12-20 years of service – many of whom would naturally have chosen to retire from the military had they been eligible for retirement benefits at an earlier point in their careers. Recent Pentagon proposals have concurred with the concept of transitioning to a FERS-styled program.

A reformed system will improve equity by providing retirement benefits for all personnel who serve at least 10 years, and enhance efficiency by using current pay and bonuses to incentivize retention. Under any such plan, current pay will have to rise to make up for the reduced incentive for members to remain in the service, and separation pay will be needed to ease the transition to civilian life. Even with such adjustments, however, this reform is projected to reduce the retirement system's cost by at least 50 percent.

Reduce farm program spending

Identical or similar proposal endorsed by: BPC, FC, BC, Coburn, Obama, House GOP

Savings: Roughly \$35 billion

Agriculture has always been a fixture of the American landscape and a critical piece of the nation's economy. In the 20th century, the United States rose to the forefront of global agricultural production, serving as a major supplier of food to countries ravaged by war, and pioneering production techniques that transformed farming methods worldwide. Today, with 2.2 million domestic farms – of which 97 percent are family-owned – the United States remains a net exporter of agricultural goods.

The federal government plays an important role in the farm sector because agricultural markets do not always efficiently balance supply and demand in the way that one would expect normal markets to behave. Consumers typically do not respond to changes in the price of staple food items by buying proportionally smaller or larger quantities of food, and farmers cannot easily respond to price changes by reducing or increasing production. These imbalances are exacerbated by the long time lag between crop planting or livestock breeding and harvest, as well as agriculture's innate susceptibility to shocks from environmental changes or natural disasters.

In light of these factors, the Agriculture Department (USDA) provides support to U.S. farmers through various programs, including: three types of commodity payments aimed at stabilizing farm income; crop insurance to protect against crop failure and disaster relief; direct and guaranteed loans to make credit available for planting and marketing; agricultural research and education; regulatory programs to preserve the integrity of the food supply from pests and diseases; conservation programs to protect soil, water, and other natural resources; marketing and export promotion programs; and food aid.

This section of the report focuses on USDA activities that are classified as mandatory spending: commodity programs, crop insurance, and most of the conservation programs. As mandatory spending, funding levels for these programs are determined directly by the multi-year "farm bill" that Congress drafts every five years. These programs totaled \$17.6 billion in 2009.

Commodity Programs: Price and Income Support

Given the inherent volatility of prices and production in the agriculture sector, USDA makes commodity payments to farms through the Commodity Credit Corporation (CCC) in order to help stabilize farm income. These programs shift some of the risks of market fluctuations onto the federal government.

About 38 percent of U.S. farms received some form of government payment in 2008. USDA classifies these farms into three major categories:

- **Commercial farms:** Farms with sales of \$250,000 or more, in which the farm operators report farming as their major occupation. Large commercial farms make up 12 percent of all farms in the nation, and 70 percent of these farms receive some form of government assistance. Of the total share of USDA payments in 2008, commercial farms received 62 percent, at an average value of \$45,400 per farm. Large commercial farms, however, produced 77 percent of all crops in that year.
- **Intermediate farms:** Farms with sales below \$250,000, in which the farm operators report farming as their major occupation. Intermediate farms make up 27 percent of all U.S. farms, and 44 percent receive some form of government assistance. Intermediate farms received 19 percent of USDA payments in 2008, at an average of \$11,900 per farm.
- **Rural residence farms:** Farms in which the farm operator's major occupation is not farming. Rural residence farms make up 61 percent of U.S. farms, and 30 percent of these farms receive government assistance. In 2008, rural residence farms received 19 percent of government payments, at an average of \$4,700 per farm.

Because the payments compensate farmers for highly variable commodity prices, CCC outlays can vary dramatically from year to year. Each commodity payment, however, has an annual payment limit per farm or farmer.

Crop Insurance and Emergency Assistance

The Federal Crop Insurance program protects farmers from losses caused by drought, flooding, pest infestation, and other natural disasters. USDA's Risk Management Agency (RMA) administers this program, which allows farmers to choose among insurance policies that provide various levels and types of protection. The insurance policies are sold and serviced by private insurance companies that receive federal reimbursements for administrative expenses. The insurance companies share the underwriting risk with the federal government and, in theory, can gain or lose depending on the extent of crop losses and claims.

Conservation Programs

USDA's conservation programs are designed to protect soil, water, wildlife, and other natural resources. USDA's Natural Resources Conservation Service (NRCS) and the Farm Service Agency (FSA) administer 20 distinct conservation programs that provide technical

or financial assistance to farmers who wish to practice conservation on their agricultural lands. Most of USDA's conservation programs respond to existing resource problems. Some funding pays landowners to retire land from production for a period of time. Other funding is designed to improve resource conditions through contour farming, nutrient management, controlling soil erosion, groundwater and wetlands conservation, grasslands conservation, wildlife habitat protection, tree planting, pest control, irrigation, and waste management.

Proposals

A. Reduce and Limit Payments to Commercial Farms and Certain Producers

Description of Recommendation: USDA's commodity payments to agriculture producers put small farms at a disadvantage, with 62 percent of commodity payments going to large commercial farms even though those farms comprise only 12 percent of all farms. This disproportionate share of commodity payments creates incentives for large commercial farms to expand their operations by buying out smaller farms, because the risks of expansion are being shared by the federal government. Because of this disadvantage (on top of other struggles), smaller farms have difficulty surviving in the marketplace.

This proposal seeks to remedy the aforementioned inequity by: (1) eliminating all payments based on production history to large commercial producers (with combined farm and non-farm adjusted gross incomes (AGI) of greater than \$250,000); and (2) lowering the cap on direct payments based on production history from its current \$40,000 level to \$20,000 (although counter-cyclical payments will remain intact). These changes will reduce average government payments per commercial farm by about \$20,000 and promote greater distributional equity in payments to farms, as smaller farms will still benefit from the payments.

Background: USDA gives price support to producers, concentrated in five commodities: corn, wheat, cotton, rice, and soybeans. Beneficiaries must share the risk of producing a crop and comply with land and resource conservation requirements. USDA helps producers in three ways: direct payments based on production history (as opposed to market prices), counter-cyclical Average Crop Revenue Election (ACRE) payments based on the average state revenue for that crop, and guarantees of minimum prices per bushel or pound for certain crops covered by the Commodity Credit Corporation (CCC). Capped since 1970, the limits for direct payments are set at \$40,000 (separate from counter-cyclical payments). There are proportional caps for ACRE payments and no limits on CCC payments.

B. Reform Federal Crop Insurance Program (FCIP) and Reduce Premium Subsidies

Description of Recommendation: Since 2000, the Federal Crop Insurance Program (FCIP) has seen a significant increase in federal expenditures to insurance providers that subsidize their administrative and operating costs (A&O). During the same period, however, higher crop prices and increased coverage on acreage yielded higher premium revenues for

insurance companies without a corresponding increase in administrative costs. As such, the A&O subsidy and companies' share of underwriting gains – profits that remain after paying claims and expenses – more than doubled from \$1.8 billion in 2006 to \$3.8 billion in 2009. At the same time, the number of policies serviced actually fell. The average rate of return for crop insurance companies from 2004 through 2008 was 24 percent, as opposed to 11 percent for private property and casualty insurance companies over the same period.

This proposal will reduce FCIP administrative and operating costs (A&O) subsidies to levels consistent with recent studies that estimate a reasonable rate of return for crop insurance companies. The Task Force plan will also reduce the FCIP premium subsidy for farmers from its current 60 percent level to 50 percent. This change will not substantially affect the quantity or quality of services provided to farmers because total insurance premiums and government subsidies have been rising faster than administrative costs. Reducing the premium subsidy to 50 percent will equalize the sharing of costs and risks between the government and the producer.

Background: FCIP protects farmers from losses caused by drought, floods, pest infestation, and other natural disasters. Farmers can choose various amounts and types of protection (for example, against yield losses only or against yield losses and low prices) in policies sold and serviced by private insurance companies; 80 percent of farms participate in this program. USDA spends about \$6.5 billion per year on crop insurance for farmers; however, a Government Accountability Office (GAO) study found that 40 cents of every dollar in this program goes to the private companies that sell and service policies and does not reach farmers.

C. Consolidate and Cap Agriculture Conservation Programs

Description of Recommendation: There is significant overlap among the various conservation programs that USDA funds, which creates inefficiencies that strain the federal budget. This proposal will eliminate that overlap by consolidating 16 of the programs into one capped entitlement that grows with inflation. By consolidating redundant programs, USDA should generate savings without severely affecting its ability to meet conservancy goals. Additionally, consolidation could reduce confusion about the programs, as their overlap creates a difficulty for farmers in distinguishing one form of assistance from another. Under the transformed landscape, constituents will clearly understand which program to tap for conservation purposes.

Programs considered for consolidation include: the Conservation Technical Assistance Program, Soil Surveys, Snow Surveys and Water Supply Forecasts, Plant Material Centers, the Grazing Lands Conservation Initiative, Agricultural Management Assistance, the Chesapeake Bay Watershed Program, the Cooperative Conservation Partnership Initiative, Environmental Quality Incentives (EQUIP), the Agricultural Water Enhancement Program, Conservation Innovation Grants, Grown and Surface Water Conservation, the Farmable Wetlands Program, the Conservation Reserve Enhancement Program, Emergency Forestry

Conservation Reserve Program, and the Voluntary Public Access and Habitat Incentives Program.

Background: The FSA and the NRCS administer 20 distinct conservation programs that provide technical or financial assistance to farmers who wish to practice conservation on their lands. Payments from conservation programs tend to go to smaller- and mid-sized producers, as opposed to large ones. By 2020, expenditures for mandatory conservation programs that USDA funds will nearly exceed direct and counter-cyclical price-support programs for producers.

Increase fees for aviation security

Identical or similar proposal endorsed by: BPC, BC, **Obama**, House GOP

Savings: \$25 billion

Reflecting its commitment to keeping air travel and commerce safe, the Administration has invested heavily in personnel, technology, and infrastructure to mitigate the constantly-evolving risks to aviation security. As risk changes, however, so too must the way in which we fund our aviation security efforts. In 2001, the Aviation and Transportation Security Act created the Aviation Passenger Security Fee, which was to be collected to offset the costs of the Transportation Security Administration's (TSA's) aviation security-related activities. The fee, in conjunction with a separate fee charged directly to air carriers, was put in place to ensure that the costs of aviation security were borne by the direct beneficiaries (e.g., air passengers, airlines) of aviation security services. The fee was originally intended to recover the full costs of aviation security. Since its establishment, however, the fee has been statutorily limited to \$2.50 per passenger enplanement with a maximum fee of \$5.00 per one-way trip. This recovers only 43 percent of TSA's aviation security costs, which have risen over the years while the fee has remained the same.

The Administration proposes both to raise the fee and change the manner in which it is collected. Modeled after Chairman Paul Ryan's proposal in the House's 2012 Concurrent Resolution on the Budget, the Administration's proposal would:

- Replace the current "per-enplanement" fee structure with a "per one-way trip" fee structure so that passengers pay the fee only one time when travelling to their destination.
- Remove the current statutory fee limit and replace it with a statutory fee minimum of \$5.00, with annual incremental increases of 50 cents from 2013 to 2017, resulting in a fee of \$7.50 in 2017 and thereafter.
- Allow the Secretary of Homeland Security to adjust the fee (to an amount equal to or greater than the new statutory fee minimum) through regulation when necessary.

Adjust Pension Benefit Guarantee Corporation fees to better cover unfunded liabilities

Identical or similar proposal endorsed by: BPC, FC, BC, Coburn, Obama

Savings: \$16 billion

BPC Description (includes basing variable premium on riskiness of investment allocation)

Pension Benefit Guarantee Corporation (PBGC) expenses rose considerably with the 2008 financial crisis, as a large number of firms went bankrupt or were forced to terminate their pension plans without sufficient assets to pay promised benefits. This proposal seeks to improve the PBGC's long-term financial condition, and align premium costs more closely with the risks that participating companies pose. To accomplish this goal, the PBGC should increase the fixed-rate premium by 15 percent and raise the variable-rate premium from \$9 to \$12 per \$1,000 of underfunding. Additionally, although not reflected in the savings estimates, the Task Force recommends that the PBGC base the variable premium partly on the riskiness of a private pension plan's investment allocation (e.g., how much is invested in stocks versus bonds).

The PBGC is a federal agency that insures participants in private employers' defined-benefit pension plans against losses if their plans are terminated without sufficient assets to pay promised benefits. In such a case, the PBGC assumes the plan's assets and liabilities, and makes monthly annuity payments to qualified retirees. The PBGC assesses fees on participating firms, consisting of a fixed annual payment (\$34 in 2009) for each participant (worker or retiree) in the plan; for an underfunded plan, a variable payment equal to \$9 for each \$1,000 by which the plan is underfunded; and, for a plan terminated in or after January 2006, a \$1,250 payment for each participant in each of the first three years after the company exits bankruptcy.

In 2008, the PBGC reported a deficit of about \$11 billion, meaning its assets were \$11 billion less than the present value of benefits owed to workers and retirees in terminated plans (or plans whose termination the agency viewed as "probable"). This proposal will adjust both the fixed and variable components of the premiums to improve PBGC's long-term financial outlook. The fixed component increase can be done either by raising the current fee per covered individual from \$34 to \$39, or by changing the assessment base to some measure of insured benefits and setting the premium at a rate that yields 15 percent more in collections.

Meanwhile, raising the variable-rate premium will raise the cost for employers who maintain underfunded plans or plans that are heavily invested in more volatile assets. This will provide a further incentive for employers to fully fund their plans, and to invest in

assets less likely to experience large swings or heavy losses. This change can be made through an adjustment of the variable premium rate that is based on the percentage of a pension portfolio's assets invested in stocks versus bonds. Greater allocations in bonds will reduce the volatility of portfolio assets, and therefore reduce future claims to the PBGC. Companies can still choose to invest in the stock market, where they might see higher returns than in bonds, but, in doing so, they – rather than the government – will bear more of the consequences of the investments' risk.

Obama Description (includes giving PBGC authority to adjust fees)

All Americans deserve a secure retirement. The Administration has proposed to create new opportunities to save for retirement by establishing a system of automatic workplace pensions and doubling the small employer pension plan start-up credit. In addition, the Administration has issued regulations that would increase 401(k) fee disclosure, so that workers can make more informed choices about how to invest their retirement savings. The Pension Benefit Guaranty Corporation (PBGC), which protects the retirement security of 44 million workers in defined benefit pension plans, is also critical to the success of a robust pension system. When underfunded plans terminate, PBGC assumes responsibility for paying the insured benefits. PBGC is responsible for paying current and future retirement benefits to more than 1.5 million workers and retirees.

PBGC receives no taxpayer financing, and relies primarily on premiums paid by insured plans. PBGC premiums are currently much lower than what a private financial institution would charge for insuring the same risk and are insufficient for PBGC to meet its long-term obligations. As of the end of September 2010, PBGC faced a \$23 billion deficit. The Administration proposes to encourage companies to fully fund their pension benefits and ensure PBGC's continued financial soundness by giving the PBGC Board the authority to adjust premiums to better account for the risk the agency is insuring. This proposal would raise much-needed revenue for PBGC while providing incentives for firms both to continue offering pensions and to improve plan funding so they can keep their pension promises. Without action, the PBGC's deficit will increase and we may face, for the first time, the need for an infusion of taxpayer funds to keep PBGC solvent.

The proposal consists of two parts: 1) a gradual increase in the single-employer flat-rate premium that will raise approximately \$4 billion by 2021; and 2) PBGC Board discretion to increase the single-employer variable-rate premium to raise \$12 billion by 2021. Beginning in 2014, the Board would be given discretion to increase variable-rate premiums, which are based on plan underfunding. Currently, premiums are set at \$9 per \$1,000 of underfunding. Under the proposal, two-thirds of the Board would have to certify that changes to the variable premium schedule would be estimated to generate at least \$12 billion through 2021. If the Board were unable to certify the premium schedule, it would be required to make adjustments to ensure generated revenues of at least \$12 billion. The Board would be prohibited from raising premiums to generate more than \$13 billion. In determining variable-rate premiums, the Board would consider a number of factors, including a plan's

risk of losses to PBGC, the amount of a plan's possible claims, and other factors the Board's directors determine appropriate. In addition, the Board would be required to consult with stakeholders prior to setting a new premium schedule and would also establish a hardship waiver and other limitations on plan-specific premium increases. PBGC would be required to publish a notice of its determination in the Federal Register, including the basis for the determination and the amount of the expected increase in income.

Actuarially adjust flood insurance subsidies for risk*

Identical or similar proposal endorsed by: BPC, Obama

BPC: Eliminate all premium subsidies

Savings: \$12 billion

The National Flood Insurance Program's (NFIP) premium subsidy for structures that were built before the completion of regional flood insurance rate maps (FIRMs) was designed to encourage the purchase of flood insurance by property owners who were previously unaware of the flood risks they faced due to the lack of public knowledge. This subsidy, however, has outlived its original purpose. Regional flood insurance rate maps have been drawn for virtually the entire nation, and property owners can easily find information on the flood risks and associated insurance rates for their area.

This proposal will phase out all pre-FIRM flood insurance premium subsidies over five years. By eliminating the subsidy, the NFIP will charge actuarially fair rates to all flood insurance policyholders. This will make policyholders of these older structures pay a fair share for their insurance protection, or create appropriate incentives for them to relocate. Currently, the NFIP must pay a considerable portion of annual premium receipts to service a debt of \$19.3 billion borrowed after Hurricanes Katrina and Rita in 2005. Because the remaining premium revenue is less than the average cost of annual claims, a large backlog of claims awaiting payment is developing. Increasing premiums will reduce the program's shortfall and also allow the NFIP to reduce the backlog in claims.

The NFIP is administered by the Federal Emergency Management Agency (FEMA) to insure buildings and their contents against losses due to flooding. The program charges two sets of premiums. The first set applies to "pre-FIRM" structures – buildings erected before 1975 or before the completion of a community's official FIRM. These premiums are heavily subsidized; the government pays an average of about 60 percent of their cost. The other set of premiums applies to "post-FIRM" buildings. Post-FIRM premiums are designed to be actuarially sound (i.e., they cover the costs of all insured losses). Post-FIRM premiums are calculated under a formula that assesses the risk of flooding in a particular building, given

the structure's elevation relative to the flood level. Pre-FIRM structures are not subject to the same risk assessment, despite constituting more than 20 percent of NFIP's insurance policies. This proposal will create parity between insurance rates on pre-FIRM and post-FIRM structures.

Obama: Eliminate the premium subsidies for certain properties

Savings: \$4 billion

Currently, 1.2 million or 20 percent of all NFIP properties are charged premiums well below the actuarial value of the insured liability. On average (including subsidized and unsubsidized policies) NFIP premium collections cover approximately 70 percent of the actuarial value of the insured liability. To address this concern, the Administration supports a proposal, as passed by the House in H.R.1309, which would impact approximately 375,000 or 30 percent of the 1.2 million subsidized policies. Specifically, the proposal would:

- Increase premiums over five years for a subset of subsidized properties: non-residential or non-primary residences, residences sold to new owners, and severe repetitive loss properties.
- Redefine severe repetitive loss properties as residences with at least four paid claims greater than \$5,000 or with two paid claims that cumulatively exceed the market value of the house.
- One year after enactment, increase premiums for all policy holders fitting the above named categories (non-residential or non-primary residences, residences sold to new owners, and severe repetitive loss properties) by no more than 20 percent per year until the amount collected covers the full expected cost of the insurance.
- New policies that fit this category of subsidized properties one year after enactment would immediately pay the full cost actuarial premium.

The Administration also supports other measures in H.R.1309 that would increase the maximum policy coverage for structure and contents and authorize studies and pilots to test alternative approaches to flood insurance that are sustainable and cost-effective.

Auction radio spectrum to expand wireless broadband and invest in a broadband network for public safety users

Identical or similar proposal endorsed by: FC, BC, Coburn, **Obama**

Savings: \$18 billion

Expanding access to mobile Internet and other wireless communications will benefit American families and businesses and support a more competitive economy. The Federal Communications Commission (FCC) estimates that mobile data use will increase by 35 times over 2009 levels by 2014, thus creating greater demand for spectrum. Recognizing this, the Administration committed last year to repurpose 500 megahertz of spectrum through auctions and other means to meet the growing demand for spectrum placed on commercial network capacity from smartphones and other mobile technologies. The Administration also has strongly promoted vital improvements in the communication capabilities of first responders and other public safety users. A wide variety of public safety organizations and the National Governors Association have also supported a first responders broadband network.

To further these goals, the Administration proposes to raise more than \$24 billion by extending the FCC authority to auction spectrum and by providing new authority to hold incentive auctions, through which current spectrum licensees voluntarily relinquish spectrum rights in exchange for a fair portion of auction proceeds. In addition, the Administration would free-up spectrum currently used by Federal agencies for auction, including by providing enhanced flexibility through the existing Spectrum Relocation Fund to help agencies repurpose and relocate. This will enhance the Administration's ongoing interagency effort to develop options for relocating Federal agencies from valuable spectrum. In cases where auctions are not appropriate, the FCC would be directed to collect \$4.8 billion in fees over the next 10 years to promote efficient resource use. Spectrum assigned to television broadcasters and public safety uses would be exempt from this fee. The proposal would also allow spectrum licenses for satellite services that are primarily domestic (such as satellite TV services) to be assigned via competitive bidding, as they had been prior to a 2005 court decision.

As long envisioned by the Administration and members of both parties in the Congress, the Administration would invest \$7 billion of spectrum auction proceeds and reserve spectrum valued at nearly \$3 billion for use in a modern, nationwide, and interoperable public safety broadband network. This network will provide first responders access to secure, interoperable video and voice communications. By achieving interoperable communications nationally and utilizing commercial infrastructure tailored to the requirements of first responders, this investment holds the potential to improve public safety communications and applications, promote cost-efficient networks through greater economies of scale, and achieve the security and reliability necessary for first responder communications. The

Administration believes the build-out of a public safety network would be best managed by a new independent corporation—with a Board representing local, State and Federal public safety users—to promote nationwide interoperability and meet the collective requirements of public safety users.

Index Mandatory User Fees to Inflation

Identical or similar proposal endorsed by: FC

Savings: \$2 billion

The federal government charges user fees or licensing fees for a variety of products and services it provides to individuals and businesses. Where applicable, these fees should be indexed for inflation and should match market rates so that the burden of maintaining these programs is not shifted to taxpayers.

Restructure the power marketing administrations to charge market rates

Identical or similar proposal endorsed by: FC

Savings: \$2 billion

CBO Description

The Department of Energy's three smallest power marketing administrations (PMAs)—the Western Area Power Administration, the Southwestern Power Administration, and the Southeastern Power Administration—provide about 1 percent of the nation's electricity. The PMAs generate electricity mainly from hydropower facilities constructed and operated by the Army Corps of Engineers and the Bureau of Reclamation. Current law requires that the electricity be sold at cost—a pricing structure intended ultimately to reimburse taxpayers for the costs of operating those facilities, a share of the costs of construction, and interest on the portion of total costs that has not been repaid. The financing terms for repaying the construction costs are generally favorable. For example, the interest rates used for older projects were set by statute, typically below the government's cost of borrowing at that time. Those favorable financing terms and the low cost of generating electricity from hydropower mean that the PMAs can charge their customers much lower rates than other utilities do. Current law also requires the PMAs to offer their power first to rural electric cooperatives, municipal utilities, and other publicly owned utilities.

This option would require the three PMAs to sell electricity at market rates to any wholesale buyer. The higher rates would provide the federal government with about \$810 million in additional offsetting receipts (which are credited against direct spending) over the 2010–2014 period.

There are several arguments for discontinuing the subsidy for federal electricity sales. First, subsidies are not needed to counter the market power of private utilities because those utilities are kept in check by federal and state regulation of the electricity supply, by federal antitrust laws, and increasingly by competition from independent producers. Second, in many cases, the communities that receive federal power are similar to neighboring communities that do not. Third, federal sales of electricity meet only a small share of the total power needs of households in the regions served by the three PMAs; thus, raising federal rates would have only a modest effect on those regions' economies. Fourth, the PMAs face the prospect of significant future costs to perform long deferred maintenance and upgrades—costs that could be budgeted for by increasing power rates now. Fifth, when water levels are too low to generate sufficient hydropower, PMAs must purchase electricity from other wholesalers to fulfill the terms of their contracts with customers, even though purchased power is generally more expensive than hydropower. Finally, selling electricity at below-market rates can encourage the inefficient use of energy. A potential drawback of this option is that changing the pricing structure of the three PMAs could greatly increase electricity rates for some of the small and rural communities they serve. Although the PMAs account for only a small share of power in the regions they serve, some communities within those regions rely on PMA-provided electricity. Other arguments against this change are that the federal government should continue to provide low-cost power to counter the uncompetitive practices of investor-owned utilities and to bolster the economies of certain parts of the country.

Transfer the Tennessee Valley Authority's electric utility functions and associated assets and liabilities

Identical or similar proposal endorsed by: FC

Savings: \$4 billion

CBO Description

In 1933, the Tennessee Valley Authority (TVA) was established as a federal agency to control flooding, improve navigation, and develop the hydroelectric resources of the Tennessee River for the benefit of a seven-state region in the southeastern United States. Since then, TVA has developed an extensive network of transmission facilities and nuclear- and fossil-fuel

powered electricity-generating plants. As one of the largest electric utilities in the nation, TVA accounted for 5 percent of national electricity generation in 2010. To maintain sufficient capacity, TVA anticipates that it will need to make large capital expenditures in the next decade and beyond. TVA funds its investments primarily by issuing debt, and it services those debt obligations from revenues earned through electricity sales to customers over several decades.

This option would transfer most of TVA's electric utility functions and associated assets and liabilities to a nonfederal owner and operator—a private firm, for example, or to an entity owned by its distributors. That entity could be similar to the newly formed Seven States Power Corporation, a nonprofit electricity generation and transmission cooperative in the Tennessee Valley. The hydropower assets and liabilities would be retained by the government because they serve several other purposes, such as flood control and recreation. This option assumes that the transfer of TVA's electric utility functions and associated assets and liabilities would be completed by the end of 2013. Such a transfer could be accomplished in different ways: TVA's assets and liabilities could be conveyed free of charge, for example, or they could be sold in a competitive auction to a nonfederal entity. Proceeds from such an auction would depend on the terms and conditions of the sale. As a result, potential proceeds are not included in this estimate.

Even in the absence of auction proceeds, the Congressional Budget Office estimates that implementing this option will reduce net outlays by about \$1 billion over the 2012–2016 period and by nearly \$4 billion over the 2012–2021 period. Those savings reflect the estimated net outlays that TVA otherwise would have incurred to build new electric power facilities over the next 10 years. CBO's estimate assumes that the current \$30 billion ceiling on TVA's borrowing would be maintained; if that ceiling was raised, the budgetary savings from this option would probably be greater over the 2012–2021 period.

The 10-year budgetary impact of such a capital transfer does not fully capture its long-term impact on the government. For example, although the government would avoid new capital outlays, it would also forgo a stream of future income that would accrue from those outlays. That income would not fully compensate for the upfront capital costs, however, because of the implicit subsidies conveyed to ratepayers in the region. By law, TVA's rates are set to recover its costs and maintain an operating reserve. But the capital charge included in those rates is artificially low because, unlike private utilities, TVA does not have to provide a return to equity holders—in this case, the taxpayers, who are exposed to the risk of having to make up for future revenue shortfalls. In addition, TVA's borrowing costs are relatively low because its status as a federal agency leads many creditors to assume that TVA's obligations would be paid off in the event of default, even though existing law explicitly states that TVA's debts are not guaranteed by the federal government.

One rationale for this option is that transferring ownership could give state regulatory agencies and TVA's customers more control over future costs. TVA is exempt from most state regulatory review because of its status as a federal agency. Its operations are sheltered

from competition, moreover, because federal law requires customers in its service area to purchase virtually all of their electricity from TVA. Increased competition, proponents would argue, could produce greater efficiency and improve cost control. In addition, many would argue that the generation and transmission of electricity are fundamentally private-sector activities. A final rationale is that it would eliminate the implicit subsidies that the government now provides to the region's ratepayers.

An argument against this option is that TVA's contribution to the economic development of its seven-state region could be diminished if TVA was under nonfederal ownership. For example, a new owner might reduce expenditures on efforts to attract new businesses to the communities in TVA's service area. Furthermore, a reduction in public subsidies would probably cause an increase in electricity prices. Finally, regulatory and other constraints on the new owner and operator of TVA's system could limit the potential benefits of a transfer.

Gradually lower the conforming loan limits for Fannie/Freddie

Identical or similar proposal endorsed by: Coburn

Savings: \$4 billion

CBO Description

The Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) are government-sponsored enterprises (GSEs) that were federally chartered to help ensure a stable supply of financing for residential mortgages, including those for low- and moderate-income borrowers. Over the past 40 years, Fannie Mae and Freddie Mac have carried out that mission in two main ways: by issuing and guaranteeing mortgage-backed securities (MBSs) and by buying mortgages and MBSs to hold in their portfolios. Under current law, the entities are temporarily able to purchase and guarantee mortgages in amounts up to \$729,750 in areas with high housing costs, although that limit will fall to \$625,500 after September 30, 2011. The limit outside of high-cost areas currently is \$417,000, and regulators can raise that limit if house prices rise. The two GSEs provided credit guarantees for over 60 percent of home mortgages originated in 2010, and they also purchased and retained mortgages.

In September 2008, the federal government took control of Fannie Mae and Freddie Mac in a conservatorship process after falling housing prices and rising mortgage delinquencies threatened the GSEs' solvency, impairing their ability to ensure a steady supply of financing to the secondary mortgage market. With that shift in control, the Congressional Budget Office concluded that the institutions had effectively become government entities whose operations should be reflected in the federal budget.

This option would set a maximum loan limit of \$417,000 nationally beginning in 2013 and freeze that limit going forward. The option would retain the scheduled reduction—to \$625,500 starting October 1, 2011—in the loan limit for high-cost areas; thus, no savings would be realized in 2012. Lower loan limits would reduce federal subsidies for the GSEs by roughly \$1 billion over the 2012–2016 period and by almost \$4 billion from 2012 to 2021. For consistency, similar changes could be made to the Federal Housing Administration’s (FHA’s) loan limits. Lower limits for FHA loans would affect discretionary spending subject to appropriations, but the effects of such changes are not included in these estimates.

The major advantages of this option are that it could provide a transition path from conservatorship and restore a role for the private sector in the secondary mortgage market while reducing taxpayers’ exposure to the risk of defaults. Current loan limits, which are high compared with the median price of about \$170,000 for an existing single-family residence in 2010, leave little scope for a private secondary market, which had been significant before the financial crisis. The option would also lower subsidies to affluent borrowers, for whom home ownership is already subsidized through the tax code. Another advantage of the option is that it would probably reduce the amount of capital allocated to housing and shift it toward other investments that would be more productive.

One disadvantage of this option is that housing markets remain fragile and any reduction of federal support might further weaken those markets. The effects would be greatest in high-cost areas, although some of the negative effects might be mitigated through increased reliance on FHA loans. Another disadvantage is that mortgage markets might become more prone to disruptions in the supply of credit during periods of acute financial stress. Reducing the subsidies would also mean that some borrowers would pay more for mortgages; in particular, once markets stabilized, borrowers seeking mortgages in amounts between \$417,000 and \$625,500 would pay interest rates that would probably be about a quarter of a percentage point higher than under current law.

Increase guarantee fees charged by Fannie/Freddie

Identical or similar proposal endorsed by: BC, Coburn, Obama

Savings: \$27 billion

CBO Description

The Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) are government-sponsored enterprises (GSEs) that were federally chartered to help ensure a stable supply of financing for residential mortgages, including those for low- and moderate-income borrowers. Over the past 40 years, Fannie Mae and Freddie Mac have carried out that mission in two main ways: by issuing and guaranteeing mortgage-backed securities (MBSs) and by buying mortgages and MBSs to hold in their portfolios. The two GSEs provided credit guarantees for more than 60 percent of home mortgages originated in 2010, and they also purchased and retained mortgages.

In September 2008, the federal government took control of Fannie Mae and Freddie Mac in a conservatorship process after falling housing prices and rising mortgage delinquencies threatened the GSEs' solvency, impairing their ability to ensure a steady supply of financing to the secondary mortgage market. With that shift in control, the Congressional Budget Office concluded that the institutions had effectively become government entities whose operations should be reflected in the federal budget.

This option would require Fannie Mae and Freddie Mac to raise the average guarantee fee they assess on loans in the MBSs they issue by 5 basis points (100 basis points are equivalent to 1 percentage point) and to raise the effective guarantee fee on loans acquired for their portfolios by the same amount. Those increases, constituting roughly a 20 percent rise in fees, would reduce federal costs for the GSEs by \$11 billion over the 2012–2016 period and by about \$27 billion from 2012 to 2021.

The main advantage of raising guarantee fees would be to reduce the projected costs of conservatorship. CBO estimates that the mortgage guarantees the GSEs issue over the 2012–2021 period will cost the federal government nearly \$50 billion on a fair-value basis with fees at their current levels. (That amount reflects the estimated federal subsidies inherent in the guarantees at the time they are made that is, the up-front payment that a private entity in an orderly market would require to assume the federal responsibility for the GSEs' obligations.) Increased fees on the guarantees would reduce those costs. The higher fees would probably flow through to borrowers in the form of higher mortgage rates; however, rates on 30-year fixed-rate mortgage loans eligible for purchase by Fannie Mae and Freddie Mac are relatively low, about 5 percent, in early 2011. This option would provide the GSEs with flexibility in setting fees for particular borrowers, so the potential would exist to minimize the adverse effects of the higher fees on low- and moderate-income borrowers. Coordination with the GSEs' regulator, the Federal Housing Finance Agency, would be necessary to ensure that the increase in average fee income represented an increase in the rates charged to borrowers with particular risk characteristics and not a shift toward lending to riskier borrowers, who already pay higher-than-average rates. Another advantage of this option is that it would help address the current underpricing of risk, which could shift the allocation of capital too far toward housing and away from more productive activities.

The main disadvantage of raising guarantee fees would be the consequent increase in the cost of borrowing, which could somewhat reduce demand for housing. Another drawback would be more limited refinancing opportunities, which might constrain spending by consumers. Both of those concerns would be particularly salient as long as housing markets and the economy remain weak.

Provide Postal Service Financial Relief and Undertake Reform

Identical or similar proposal endorsed by: FC, Obama

Savings: \$19 billion

The Administration recognizes the enormous value of the U.S. Postal Service (USPS) to the Nation's commerce and communications, as well as the urgent need for reform to ensure its future viability. USPS faces a long-term, structural operating deficit that has been exacerbated by the precipitous drop in mail volume in the last few years due to the economic crisis and the continuing shift toward electronic communication. Absent legislative intervention, USPS will be insolvent by the end of September 2011 when it will be unable to make the statutory \$5.5 billion Retiree Health Benefit prefunding payment to the Office of Personnel Management, will have exhausted its cash reserves, and will have hit its cumulative statutory Treasury borrowing ceiling of \$15 billion. Bold action is needed to ensure that USPS can continue to operate in the short-run and achieve viability in the long-run. To that end, the President is proposing a comprehensive reform package that would: 1) restructure Retiree Health Benefit pre-funding in order to accelerate moving these Postal payments to an accruing cost basis and reduce near-year Postal payments; 2) provide USPS with a refund over two years of the \$6.9 billion surplus in Postal contributions to the FERS program; 3) reduce USPS operating costs by giving USPS authority, which it has said it will exercise, to reduce mail delivery from six days to five days; 4) allow USPS to offer non-postal products and increase collaboration with State and local governments; and 5) give USPS the ability to better align the costs of postage with the costs of mail delivery while still operating within the current price cap, and permit USPS to seek the modest one-time increase in postage rates it proposed a year ago. These reforms would provide USPS with over \$20 billion in cash relief over the next several years and in total would reduce the

Improve Collection of Pension Information from States and Localities

Identical or similar proposal endorsed by: BPC, Obama

Savings: \$3 billion

The Social Security Windfall Elimination Provision (WEP) and Government Pension Offset (GPO) provisions are adjustments to the Social Security formula which ensure that non-covered workers do not receive a higher proportional benefit than workers with similar earnings who worked their entire careers in covered employment. Currently, WEP and GPO adjustments are only applied when an individual worker attests that he or she has a pension in non-covered employment or the Social Security Administration (SSA) discovers that an individual is receiving a non-covered pension. While SSA is able to conduct data matches with the Office of Personnel Management to identify Federal workers who have been employed in non-covered employment, there is currently no similar data system to obtain information on State or local pensioners. This proposal provides up to \$50 million to State and local governments to develop such a system for more timely and accurate data collection and direct pension information reporting to SSA. This proposal would improve enforcement of the current law WEP and GPO provisions, resulting in improved payment accuracy for the Old-Age and Survivor, and Disability Insurance Programs, and is projected to save approximately \$3.1 billion

Get rid of unneeded Federal real property

Identical or similar proposal endorsed by: Coburn, Obama

Savings: \$4 billion

The Administration proposes to create an independent real property board to recommend disposal and consolidation opportunities to the Congress. The Government Accountability Office (GAO) has recognized longstanding inefficiencies in the Federal real estate portfolio, identifying it as a prime candidate for reform in its recent March 2011 report on proposals to reduce the cost of Government operations. Within the 1.1 million buildings, structures, and land parcels that the Federal Government owns or operates are significant opportunities to sell unneeded property, consolidate agency leases, co-locate agency operations, and improve the sustainability of the Government's operations. The Civilian Property Realignment Act (CPRA) would establish an independent board of experts to expedite the disposal of unneeded properties and the consolidation of properties across and within agencies. Modeled after the successful Base Realignment and Closure (BRAC) Commission, the board would achieve this disposal and consolidation of Federal real property through a process that forwards bundled recommendations to the Congress for a direct vote.

Continue unemployment benefits next year

Identical or similar proposal endorsed by: Obama

Cost: \$30 billion

To support unemployed people as they work their way back to a job, we need to make sure that benefits do not run out next year. Extended Unemployment Compensation will prevent six million Americans from losing benefits in 2012.

Revenue/Tax Expenditure Savings

Switch to the chained CPI measure of inflation

Identical or similar proposal endorsed by: BPC, FC, and Coburn

Savings: \$72 billion

CBO Description

Several parameters of the tax code change every year with the price of goods and services, as measured by the consumer price index for all urban consumers (CPI-U). Among the tax parameters that change are the amounts of personal and dependent exemptions; the size of the standard deductions; the income thresholds that divide the rate brackets for the individual income tax; the amount of annual gifts exempt from the gift tax; and the thresholds and phase-out boundaries for the earned income tax credit, the child tax credit, and several other credits. Indexing is intended to keep those amounts relatively stable in real (inflation-adjusted) terms.

Indexing is accomplished by adjusting each parameter from its value in a base year by the percentage change in the CPI-U between that base year and the most recent year for which information is available. The period used for the calculation is not a calendar year but the 12 months that elapse from September to August. The value of the CPI-U in August becomes available in September, which allows enough time to index the tax parameters and prepare the necessary forms for the coming year. Adjustments in parameters of the tax code are calculated as follows: In the base year of 1987, for example, the standard deduction for a single tax filer was \$3,000. Between 1987 and 2010, the CPI-U increased by 93.9 percent; correspondingly, the standard deduction (rounded to the lowest \$50 increment) increased to \$5,800 for 2011.

The standard CPI-U, however, overstates changes in the cost of living by not fully accounting for the extent to which households substitute one product for another when the relative prices of products change. The Bureau of Labor Statistics created the chained CPI-U to explicitly address that “substitution bias” in the standard CPI-U. Whereas the standard CPI-U uses a basket of products reflecting consumption patterns that are as much as two years old, the chained CPI-U incorporates adjustments that people make in the types of products they buy from one month to the next. Although the chained CPI-U corrects for the substitution bias in the standard CPI-U, neither the chained nor the standard CPI-U perfectly captures changes in the cost of living because neither fully accounts for increases in the quality of existing products or the value of new products.

This option would use the chained CPI-U instead of the standard CPI-U to adjust various parameters of the tax code. The Congressional Budget Office estimates that the chained CPI-U is likely to grow at an average annual rate that is 0.25 percentage points less than the standard CPI-U over the next decade. Therefore, using the chained CPI-U to index tax parameters would increase the amount of income subject to taxation and result in higher tax revenues. Furthermore, the effects of instituting such a policy would grow over time. The net revenue increase would be about \$700 million in 2012 but would reach \$14 billion in 2021. Net additional revenues would total \$17 billion over the 2012–2016 period and would sum to \$72 billion from 2012 through 2021. An argument in favor of using the chained CPI-U to index tax parameters is that this approach would more accurately adjust people’s tax liability to reflect changes in the cost of living than the standard CPI-U. The chained CPI-U provides a better measure of changes in the cost of living by more quickly capturing the extent to which households adjust their consumption in response to changes in relative prices.

Eliminate Ethanol Subsidies

Identical or similar proposal endorsed by: BPC, FC, Coburn

Savings: \$19 billion

In the 1970s, Congress began providing federal assistance for the domestic production of ethanol, which included the establishment of the Renewable Fuels Standard (RFS) that created a permanent market for the industry. Since that time federal assistance has grown to include multiple tax incentives and federal grant programs. Most recently, EPA issued a decision to increase the current fuel blend wall from ten percent to fifteen percent (E15), effectively creating an even larger market for ethanol producers.

While born of good intentions, federal subsidies for ethanol now face sizeable roadblocks as consumers have protested the required use of ethanol in their fuel. Ethanol-blended fuel is nearly a third less efficient than gasoline (ethanol burns at 68 percent the energy content of gasoline), has contributed to the increased price of corn (as well as land, feed, and other input costs), and can cause engine damage.

Overall, ethanol subsidies are outdated and have failed to achieve their goals of helping our nation to achieve energy independence. The Congressional Budget Office recently found consumers incur a cost of \$1.78 per gallon as a result of federal subsidies before they even pay at the pump. Meanwhile, U.S. biofuels consumption remains a small share (4.3 percent) of national transportation fuel use.

The original federal ethanol mandates stemmed from several events, foremost of which was the global energy crisis of the 1970s and a desire to achieve energy independence. Over four decades later, our nation seeks this goal more than ever, but ethanol has not helped achieve this target. It is time to give taxpayers a break and allow the ethanol industry a chance to stand on its own or fail.

Volumetric Ethanol Excise Tax Credit (VEETC)

While various forms of federal assistance continue to sustain the ethanol industry, foremost among them is the Volumetric Ethanol Excise Tax Credit (VEETC), which provides 45 cents per gallon to blenders of ethanol. This subsidy alone accounts for \$6 billion in federal spending. It is available in unlimited quantities to blenders, including companies such as Exxon, Valero, BP, and Chevron, which has drawn the ire of some environmentalists. While it was intended to encourage the use of ethanol, the Congressional Research Service determined the VEETC only duplicates what the Renewable Fuels Standard already requires. Now the VEETC only functions to incentivize the consumption of fuel.²⁹⁹⁷

The U.S. Senate recently voted overwhelmingly on a bipartisan basis to repeal the VEETC by a margin of 73-27, clearly demonstrating that taxpayers are ready to end costly and redundant ethanol subsidies. When VEETC is eliminated, the import duty should be eliminated as well. The cost for this provision is \$4.8 billion in 2011. Ending this provision would save \$2.4 billion for the rest of this year.

Small Ethanol Producer Credit

The Small Ethanol Producer Tax Credit provides 10 cents per gallon for the first 15 million gallons of ethanol produced for any producer with capacity below 60 million gallons and has been valued at \$440 million annually. It is estimated to cost nearly \$500 million. It is scheduled to expire at the end of 2011. This tax credit is intended to target small businesses and farmer cooperatives.

The *Los Angeles Times* recently interviewed an ethanol producer about the efforts in Congress to end ethanol subsidies. When asked what impact ending this tax credit would have, one CEO of a longtime small ethanol production company expressed a widely held view, noting, "I don't see a fatal effect." The tax credit is valued at \$1.5 million annually for his company.

While ethanol fuel has yet to capitalize on the ample opportunity given it by taxpayers to achieve economic viability on its own merit, eliminating this tax credit would likely have minimal impacts, considering the Renewable Fuels Standard continues to mandate ethanol be blended with gasoline. Eliminating this provision would save \$4 billion over the next decade.

Biodiesel Tax Credit

Biofuels such as ethanol and biodiesel are renewable fuels made from organic sources such as crop wastes and animal fat. This biodiesel tax credit provides \$1 per gallon, available in unlimited amount to all qualifying biodiesel producers. The credit was created in 2004 and briefly expired two different times and later extended retroactively. It is now scheduled to expire at the end of 2011. U.S. biodiesel production is much smaller than its ethanol counterpart but has also shown strong growth, rising from 0.5 million gallons in 1999 to an estimated 776 million gallons in 2008. Without the tax credit, biodiesel is more expensive than gasoline, demonstrating the fuel is not economical to produce without federal assistance. According to the Congressional Research Service, demand for biofuels [both ethanol and biodiesel] to fulfill a mandate is not based on price, but rather on government fiat. As long as the consumption of biofuels is less than the mandated volume, its use is obligatory. The cost for this provision was \$500 million in 2010. Ending this tax subsidy would save \$5 billion over ten years.

Cellulosic Ethanol Production Tax Credit

The Cellulosic Ethanol Production Tax Credit provides \$1.01 per gallon and expires at the end of 2012. While not yet being produced commercially, cellulosic ethanol holds great promise, and is included as a component of the Renewable Fuels Standard (RFS). The Environmental Protection Agency's recent draft of the RFS for 2012 projects a reduced production from the previous estimate of 500 million down to 3.45 to 12.9 million of cellulosic ethanol.

Still, industry stakeholders still claim this goal is too high. While this should not be taken as a sign cellulosic has no future, it should give strong caution to policymakers not to artificially enhance the capital environment of cellulosic projects. Although the fuel appears to hold great promise, Congress would be wise to avoid another situation similar to its experience with corn-based ethanol and, instead, allow markets to direct the capital as the technology merits it. Already, venture capital, oil and natural gas companies, banks, and agricultural research and technology companies have teamed with industry experts to invest in cellulosic biofuels, and this will likely continue so long as the technology merits additional funding.

This plan calls for the elimination of this tax credit. Currently, the costs associated with this giveaway are minimal under current conditions. However, if production increases to meet RFS requirements, its costs would be substantial. In fact, some estimates project it could cost \$10 billion by 2015 and \$20 billion by 2020 if cellulosic biofuels fulfill their expectations.

Eliminate subsidies for employee parking expenses

Identical or similar proposal endorsed by: BPC, FC, Coburn, **Quigley**

Savings: \$38 billion

Another federal subsidy for environmentally destructive behavior is the tax exemption for qualified parking expenses. While fringe benefits are generally taxable as employee compensation, parking expense benefits have been exempted from taxation. According to a joint report from the Brookings Institution and the World Resources Institute, this exemption “encourages commuting by vehicles and contributes more to fossil fuel use, global warming, and more pollution and congestion.” This begs the question: why should taxpayers continue to subsidize an activity that is harmful to the environment?

We can’t find a good reason, and so we believe that this federal subsidy for employee parking expenses should be cut. This would not stop anyone from driving to work, but it would remove the extra incentive to do so. Not only would this remove a federal subsidy for environmentally harmful behavior, but it would also “improve fairness in the relative tax treatment of employees who receive compensation in different forms.”

Eliminate Mortgage Deduction for 2nd Homes / Yachts

Identical or similar proposal endorsed by: BPC, FC, **Coburn**

Savings: \$15 billion

One of the most popular provisions in the tax code is the home mortgage interest deduction, even though it is claimed by only about a quarter of all tax filers. For the millions of Americans who claim the deduction every year, though, it helps offset the cost of owning a home. Under current law, homeowners can deduct the interest paid on home mortgages for primary residences and vacation homes loans of up to \$1 million, and also on an additional \$100,000 home equity line of credit. This is one of the most expensive tax breaks in current law, resulting in lost federal revenue of nearly \$88 billion in fiscal year 2011.

While most assume the mortgage interest deduction largely benefits middle and lower income earners, economist Martin Sullivan points out this is actually not the case. Sullivan asserts, “The tax benefit provided by the mortgage interest deduction flows overwhelmingly to rich families like those portrayed in the hit television series *Beverly Hills, 90210*.” Data from the Internal Revenue Service further emphasizes this discrepancy. In 2008 alone, millionaires across the country took advantage of more than \$7 billion in mortgage interest deduction tax breaks. Sullivan explains the disparity, “First, the rich have larger houses and

larger mortgages than the poor. Second, the deduction is available only to itemizers. While almost all high-income taxpayers itemize deductions on their returns, very few of the poor do. Finally, the rich have much higher marginal income tax rates than the poor.”

The provision of the mortgage interest deduction relating to second homes further highlights that those benefitting from this tax break are among the most well off. Even a yacht can be considered a second residence — as long as the luxury boat has a “sleeping, cooking, and toilet facility” and an individual lives in it for at least two weeks a year.

The *Seattle Post-Intelligencer* exposed numerous examples of vacationers wrongly taking advantage of this deduction, also noting the IRS does little to verify boat-owners actually meet the requirements to consider these floating vacation getaways a second home. In one case, the newspaper found a Seattle businessman who was able to “declare his yacht a second home for tax purposes ... allowing him to reduce his income by \$19,200, the amount he pays in interest on the loan.” According to the paper, “he also deducted the annual \$3,600 state registration fee, and between the two tax breaks, was able to lower his tax bracket from 36 to 32 percent, greatly reducing his annual tax bill.”

Reforms are needed to ensure this deduction is not abused to provide tax breaks for vacation homes, yachts, and mansions.

Tax Carried Interest as Ordinary Income

Identical or similar proposal endorsed by: BPC, FC, Obama

Savings: \$21 billion

CBO Description

Investment funds—such as private equity, real estate, and hedge funds—are typically organized as partnerships consisting of one or more general partners, who manage the fund. The partners determine investment strategy; solicit capital contributions; acquire, manage, and sell assets; arrange loans; and support all of those activities. Partnerships also can consist of limited partners, who contribute capital to the partnership but do not participate in management. General partners can invest their own financial capital in the partnership, but such investments usually represent a small share of the total funds invested.

General partners typically receive two types of compensation for managing the fund: a fee tied to some percentage of the fund’s assets under management and a profit share, or “carried interest,” tied to some percentage of the profits generated by the fund. A common

compensation agreement gives general partners a 2 percent fee and 20 percent in carried interest. The fee, less expenses of the fund, is taxed as ordinary income (all income except that from capital gains). The taxation of the carried interest is deferred until profits are realized on the fund's underlying assets, and any resulting profits to the general partners are taxed at the capital gains tax rate to the extent that the firm's profits reflect capital gains.

This option would treat the net income partners receive for performing investment management services as ordinary income. Income the same partners receive on the basis of their capital contribution would not be affected. The change would produce \$2 billion in revenues in 2010 and \$13 billion between 2010 and 2014. The President's budget for 2010 proposes a similar change.

Many economists view at least part of carried interest, if not all of it, as performance-based compensation for management services rather than as a return on financial capital invested by that partner. Therefore, at least some component of the carried interest could be considered, and taxed, as ordinary income. And the treatment thus would match that for many other forms of performance based compensation, such as bonuses.

Taxing carried interest at the same rate as ordinary income also would equalize the tax treatment of income that partners earn for performing investment management services with the treatment of income that executives earn for doing similar work. The managers of publicly traded mutual funds also invest in a variety of assets; executives of many corporations direct investment, arrange financing, purchase other companies, or spin off components of their enterprises.

One drawback of taxing all carried interest at ordinary rates is that it would treat the income of partners who provide investment management services differently from that earned by entrepreneurs who start new businesses and contribute labor services and capital. To the extent that the operation of a business generates income for its owners, that income is taxed at ordinary rates. When owners sell a business, however, profits from the sale generally are taxed as capital gains, even though some of those profits are a direct return on the specific labor services of the owners.

Another drawback of the option is that it would reduce the incentive for general partners to undertake risky investments that can lead to new products, innovations, and more efficient markets and businesses. It is not clear, however, how much a lower rate on capital gains contributes to such outcomes, or even whether promoting risky investment offers more economic advantages than disadvantages. Furthermore, the application of that broader motivation to carried interest in investment funds is not clear, because the financial capital that is gathered and invested in such funds is provided almost entirely by limited partners, not by general partners.

Cut subsidies for private-purpose state and local bonds

Identical or similar proposal endorsed by: BPC, FC

Savings: \$23 billion

CBO Description

Federal tax law permits state and local governments to issue bonds whose interest income is exempt from federal taxation. As a result, those bonds bear lower rates of interest than they would if the interest income were taxable. (The bondholder is compensated for the lower interest rate by not having to pay federal tax on the interest income.) For the most part, proceeds from those tax-exempt bonds finance public projects, such as schools, highways, and water and sewer systems. But state and local governments also issue tax-exempt securities— known as private-activity bonds—whose proceeds are used by nongovernmental entities to finance various quasi-public facilities and private-sector projects: mortgages for rental housing and single-family homes; infrastructure facilities such as airports, docks, wharves, mass transit, and solid-waste disposal plants; small manufacturing plants and agricultural land and property for first time farmers; student loans; and facilities for nonprofit institutions, such as hospitals and universities. The American Recovery and Reinvestment Act of 2009 (Public Law 111-5) established a new type of qualified tax-exempt private-activity bond for 2009 and 2010 that is to be used to finance projects in “recovery zones,” areas with significant poverty, unemployment, or home foreclosures.

The act also made the interest on all tax-exempt private activity bonds issued in 2009 and 2010 deductible under the alternative minimum tax. The Tax Reform Act of 1986 limits the annual volume of new bonds that state and local governments can issue for eligible facilities, small manufacturing plants, student loans, and housing and redevelopment projects. Some private-activity bonds are exempt from the cap, including those for airports, ports, and solid-waste disposal facilities that meet requirements for government ownership, and certain bonds for nonprofit organizations (primarily hospitals and educational institutions). Initially, the cap was not indexed for inflation, so the volume of private-activity bonds issued each year would decline over time and eventually disappear. However, the volume cap has since been raised periodically, and beginning in 2002 it was indexed for inflation. (At that time, the annual volume of new bonds allowed was \$225 million per state or \$75 per state resident, whichever was greater.) This option would, beginning in 2011, curtail the issuance of private-activity bonds either by eliminating the tax exemption for all new issues or by allowing tax exemption but no longer indexing the volume cap for inflation. The first approach would have an immediate effect on the volume of such bonds and would increase

revenues by a total of \$4 billion over the period from 2010 to 2014. The second approach would work more slowly, boosting revenues by only \$0.1 billion over those five years. (Lawmakers also could limit the outstanding stock of private-activity bonds for some uses, such as nonprofit organizations' facilities. That change is discussed in Revenue Option 39.)

One rationale for this option is that limiting or eliminating the tax exemption for new private-activity bonds could improve economic efficiency. Investments that can be financed at below-market interest rates require a lower cash return and thus may contribute less to national income than do investments that are not preferentially taxed. Altering those projects' financing by removing the tax exemption or curbing the volume cap would redirect savings to investments that earn a higher cash return and therefore may contribute more to national income and welfare.

A disadvantage of this option is that some of the projects that cannot earn the market rate of return and therefore do not get built may have sufficient public benefits beyond their cash return to compensate for the interest rate subsidy. (If the federal government wished to help such projects, however, it could do so more efficiently through a direct subsidy. Unlike tax-exempt financing, such a subsidy would not reduce federal revenues by more than the drop in borrowers' interest costs. In addition, access to a direct subsidy would not be open-ended, and the subsidy amount could receive regular scrutiny from policymakers in the annual budget process.)

Eliminate Hollywood tax breaks

Identical or similar proposal endorsed by: BPC, FC, Coburn

Savings: \$1 billion

Designed as an incentive to encourage Hollywood to produce feature films and television programs in the United States, entertainment companies may currently elect to deduct up to \$15 million in certain costs associated with the production of television episodes and movies where at least 75 percent of the compensation costs are for work performed on U.S. soil. Allowing Hollywood to benefit from this accelerated cost recovery results in federal revenue losses of at least \$30 million a year.

While benefitting from special tax treatment, the entertainment industry is not lacking in privately generated revenue. The year's top grossing film, *Hangover Part II*, brought in more than \$232 million less than one month after hitting theaters. With a production budget of \$80 million, the film netted a profit in its first weekend, as moviegoers spent more than \$85 million to catch the latest installment of this series. Likewise setting new records was *Harry Potter and the Deathly Hallows, Part 2*, which set an opening day record of \$92.1 million and

\$168.6 in its first weekend. Despite a tough economy, taxpayers are still choosing to spend their own money at the box office. They should not be forced to pay for Hollywood flicks twice – once at the box office and once with a federal subsidy program for a multi-billion dollar a year industry.

Hollywood film production is also being subsidized through state tax incentives in nearly 40 states—to the tune of \$1.5 billion in 2010, according to the Center on Budget and Policy Priorities (CBPP), which suggests states consider scaling back their Hollywood tax breaks. According to the Motion Picture Association, only 11 states do not provide –significant tax incentive for [entertainment] production. However, in light of chronic budget shortfalls, many states are now considering eliminating these tax subsidies altogether.

It is unclear if these incentives, whether at the state or federal level, actually pay for themselves by bringing in enough revenue during production to offset the cost of the multi-million dollar write offs and tax breaks. An independent commission in the state of Missouri recommended eliminating the credit in 2011, stating –This tax credit serves too narrow of an industry and fails to provide a positive return on investment to the state. There is currently no long term opportunity for the location of production facilities for films in Missouri. CBPP echoes this sentiment, saying, –The revenue generated by economic activity induced by film subsidies falls far short of the subsidies’ direct costs to the state. To balance its budget, the state must therefore cut spending or raise revenues elsewhere, dampening the subsidies’ positive economic impact.

Unlike Washington, many states are forced to live within their means and cannot run large deficits to fund low-priority spending during an economic downturn. Congress should follow their lead and eliminate this tax break for a highly profitable industry in little need of taxpayer support—other than their purchase of popcorn and movie tickets on a Friday night. Eliminating this provision could save more than \$1 billion over ten years.

Eliminate Timber Subsidies

Identical or similar proposal endorsed by: BPC, FC, Coburn

Savings: \$5 billion

The federal tax code has several breaks for tree planting in the timber industry, including annual expensing and deductions that can provide significant benefits to the industry.

While taxes are deferred until a company harvests its timber, deductions for timber growing expenses can be made at the time of expenditure. Maintenance costs, such as thinning, disease and pest management, and fire costs can be deducted as they occur.

Up to \$10,000 in reforestation expenses may also be deducted per taxpayer per unit of property, with amounts over that being amortized over seven years. This allows multiple

individuals to claim the same benefit for the same unit of property, which by regulation, only has to be one acre or more in size.

Reforestation expenditures include costs associated with forestation or reforestation by planting, artificial seeding, or natural seeding.

The current expensing provision allows for immediate expensing (especially in light of deferred tax assessment) while other industries may be required to capitalize these costs and amortize them over a longer periods of time or, alternatively, only recover them upon a future disposition.

Remove Many Energy Subsidies

Identical or similar proposal endorsed by: Some by Coburn, Obama

Savings: \$61 billion

Eliminating many energy subsidies in the tax code will provide savings. Both alternative energy, solar and wind, and fossil fuels, oil, gas and coal, will have subsidies removed.

Include All Income Earned Abroad by U.S. Citizens in Taxable Income

Identical or similar proposal endorsed by: BPC, FC, Coburn

Savings: \$71 billion

United States citizens who live and earn income abroad must file tax returns each year. For calendar year 2009, current law allows those citizens to exclude from taxation up to \$91,400 of the income they earn in other countries. (That exclusion is indexed for inflation.) Because of that exclusion and others for foreign housing and the usual personal exemptions and deductions, U.S. citizens who reside abroad and earn close to \$100,000 may not incur any U.S. tax liability, even if they pay no taxes to their resident countries. If they do pay taxes to their resident countries, those citizens receive a credit, which also could eliminate their U.S. tax liability on the income. (The Tax Increase Prevention and Reconciliation Act of 2005, however, included several technical changes that made the tax exemption less generous overall.)

This option would retain the credit for taxes paid to foreign governments but would require U.S. citizens living overseas to include all of the income they earned abroad in their adjusted

gross income. U.S. citizens who paid taxes to countries where tax rates are higher than in the United States generally would not owe U.S. taxes on their earned income; those living in countries with lower tax rates might have some U.S. tax liability. That change would increase revenues by \$1 billion in 2010 and by \$28 billion from 2010 to 2014.

One rationale for eliminating the exclusion for foreign earnings is that U.S. citizens with similar income should incur similar tax liabilities, regardless of where they live or what services they receive from the government. That principle is violated if people can move to low-tax foreign countries and escape U.S. taxation while retaining their U.S. citizenship. In addition, the existing exclusion represents an implicit subsidy to corporations that employ U.S. citizens abroad, because those companies can pay their employees less than they would if the income were fully subject to U.S. taxes. Moreover, ending the exclusion for foreign-earned income would lessen some of the complexity of the tax code.

Opponents of this option argue that U.S. citizens who live in other countries should not face the same tax treatment as U.S. residents because they do not receive the same services from the U.S. government. Opponents also maintain that excluding foreign-earned income promotes exports by U.S. multinational firms by making it less expensive for those companies to hire U.S. employees to live and work abroad.

Exclusion of Certain Allowances for Federal Employees Abroad

Identical or similar proposal endorsed by: BPC, FC, and Coburn

Savings: \$18 billion

Federal government civilian employees who work abroad and pay federal income taxes, but no taxes to a foreign government, are allowed to exclude from income taxes certain cost-of-living special allowances such as housing, travel, and food. The rationale is that costs of living, such as food, fuel, and living expenses for those living abroad are generally higher. However, incomes for federal civilian workers overseas are generally higher than average incomes in the United States, in part because of this discrepancy. As a result, this tax expenditure is not addressing a true need and largely benefits higher-income earners.

There is no similar tax exclusion for federal workers employed in high cost-of-living areas in the United States such as metropolitan areas or other high-cost areas like Hawaii and Alaska. In addition, some federal workers, such as Department of State employees, even earn Washington, D.C. "locality" pay while serving overseas to compensate for the higher cost of living. It is unclear why federal employees receive both additional salary for a higher cost of living and tax-free benefits for the same reason.

As a result of the hidden costs of this tax provision, federal agencies may not make the most prudent decisions on where to base their personnel. Agency budgets do not include the amount of money lost to the Treasury through these allowances and exemptions. As such, what may appear to be a better deal to taxpayers may actually cost more than another option when the cost of this tax benefit is taken into consideration.

Part of the underlying assumption for this special tax break is that federal employees are driven primarily by financial considerations when looking at overseas employment. But foreign federal jobs also provide the opportunity to live and work in a foreign country with a steady paycheck and benefits. With a nine percent unemployment rate in the United States, it is unlikely federal workers will leave the federal workforce if this tax provision were repealed. However, it is also clear should any federal employees choose to leave such a desirable overseas post, there would likely be plenty of qualified applicants for any such job openings.

Repealing the exclusion from income taxes certain cost-of-living special allowances such as housing, travel, and food for federal employees is also part of a bipartisan proposal and is included in tax reform legislation sponsored by Senators Ron Wyden (D-Oregon) and Dan Coats (R-Indiana).

Repeal the “LIFO” and “Lower of Cost or Market” Inventory Accounting Methods

Identical or similar proposal endorsed by: BPC, FC, Obama

Savings: \$100 billion

CBO Description

To compute its taxable income, a business must first deduct from its receipts the cost of purchasing or producing the goods it sold during the year. Determining those costs requires that the business identify and attach a value to its inventory. Most companies calculate the cost of the goods they sell in a year using the accrual method of accounting, adding the value of the inventory at the beginning of the year to the cost of goods purchased or produced during the year and then subtracting from that total the value of the inventory at the end of the year.

The tax code allows firms to choose among several approaches for identifying and determining the value of the goods included in their inventory. For itemizing and valuing goods in stock, firms can use the “specific identification” method. That approach, however, requires a very detailed physical accounting in which each item in inventory is matched to

its actual cost. An alternative approach—“last in, first out” (LIFO)—also allows firms to value their inventory at cost but, in addition, permits them to assume that the last goods added to inventory were the first ones sold. Under that assumption, the cost of those more recently produced goods should approximate current market value (that is, the cost of replacing the inventory).

Yet another alternative approach—“first in, first out” (FIFO)—is based on the assumption that the first goods sold from a business’s inventory have been in that inventory the longest. Like firms that adopt the LIFO method, firms using the FIFO approach can also value their goods at cost. But firms that use the FIFO approach have still another choice—the “lower of cost or market” (LCM) method. Instead of assessing their existing inventory at cost, they can assess that inventory on the basis of its market value and then choose whichever valuation is lower. In addition, if a business’s goods cannot be sold at market prices because they are damaged or flawed, firms that use the FIFO approach can qualify for the “subnormal goods” method of inventory valuation.

This option would eliminate the LIFO method of identifying inventory, as well as the LCM and subnormal goods methods of inventory valuation. Businesses would be required to use the specific-identification or FIFO methods to account for goods in their inventory and to set the value of that inventory on the basis of cost. Those changes—which would be phased in over a period of four years—would increase revenues by \$72 billion from 2012 through 2016 and by a total of \$98 billion over the 2012–2021 period.

The main rationale for this option is to align the tax accounting rules with how businesses probably sell their goods. Under many circumstances, firms probably prefer to sell their oldest inventory first—among other reasons, to minimize the risk that the product becomes obsolete or damaged during storage. Under those circumstances, allowing firms to use alternative methods to identify and to value their inventories for tax purposes allows them to reduce their tax liabilities without any change in their economic behavior.

An argument for eliminating the LIFO method is that it allows companies to defer taxes on real (inflationadjusted) gains when the prices of their goods are rising relative to general prices. Firms that use LIFO can assume that the goods that are sold are from newer—and costlier—inventory when, in fact, the items may have been in inventory for some time and were produced when costs were lower. By deducting those higher costs as the price of production, firms are able to defer taxes on the amount by which the value of their goods has appreciated, until those goods are sold.

An argument against disallowing the LIFO accounting method is that such a policy change could also result in the taxation of income that arises from inflation. The gains that would be taxed if the LIFO method was terminated could be attributable to inflation and, therefore, would not represent real changes in a firm’s resources and its ability to pay taxes. However,

other elements of the corporate income tax do not correct for inflation and therefore gains attributable to inflation are taxed.

An argument for eliminating the LCM method of inventory valuation under FIFO is that, when prices are falling, it provides a tax advantage for goods that have not been sold. The LCM method allows a business to compare the market value of each item in its inventory with the item's cost and then set the lower of the two as the item's value. The year-end inventory will have a lower total value under LCM than under the cost method if the market value of any item in the inventory is less than its cost. Using the LCM method when prices are falling allows the firm to claim a larger deduction for the costs of goods sold, causing the firm's taxable income to fall as a result. In effect, that method allows a firm to deduct from its taxable income the losses it incurred from the decline in the value of its inventory. (That deduction is allowed even though the firm has not sold the goods.) A firm, however, is not required to recognize gains in the value of its inventory when prices are rising, which means that gains and losses are taxed differently. Similarly, firms that use the subnormal goods method of inventory valuation can immediately deduct the loss, even if the company later sells the good at a profit.

End Certain Economic Development Tax Breaks

Identical or similar proposal endorsed by: BPC, FC, Coburn

Savings: \$15 billion

New Markets Tax Credit

Individuals investing in businesses that provide capital to low-income residents in low-income communities can apply for the New Markets Tax Credit. New Market Tax Credits reduce an individual's taxes by a portion of their investment over several years, creating an incentive for investment. Rather than working this way, the program rewards past behavior, but does little to incentivize new development.

In addition, some of the —community development entities|| benefiting from this special tax break are actually multi-million dollar companies. Recipients of the tax break are often subsidiaries of major banks, like two divisions of Chase Bank, which were awarded \$204 million worth of tax credits through this program in only three years (2007-2009); or the Merrill Lynch Community Development Company, which received \$174 million in the same period; or Wachovia Community Development Enterprises, which received \$521 million in awards from 2004-2009.

These credits have been used to subsidize expensive construction projects like the \$116 million renovation of the landmark Blackstone Hotel in downtown Chicago, a Marriott hotel. This project's main beneficiary was Prudential Financial Inc., the second-largest U.S. life insurer, which received \$15.6 million in New Market Tax Credits.

In 2009 alone, over \$3.5 billion in federal funding was directed via this tax break for projects not seemingly intended to benefit low-income regions:

- \$19.9 million for a multiplex movie cinema and retail development;
- \$8 million for a hockey arena;
- \$5 million for 3D digital products and software application sales;
- \$1.1 million for a cable television station;
- \$15.7 million for a performing arts venue and school;
- \$2.2 million for the —development of enhanced streetscapes;||
- \$4.9 million for an 86 Room Fairfield Inn & Suites;
- \$3.75 million for the historic rehabilitation of a —vacant hotel;||
- \$9.8 million for a movie studio and entertainment venue;
- \$4.5 million for architecture studios;
- \$10.7 million for a historic rehabilitation of the headquarters of a global entertainment and convention venue management company; and
- \$31 million for two —historic theater rehabilitations.

These credits are disbursed to a recipient for at least eight years. The Congressional Research Service estimates roughly \$705 million will be spent on these credits in fiscal year 2011.

Empowerment Zone, Renewal Community, and District of Columbia Tax Incentives

Similarly, Empowerment Zones (EZs) and Renewal Communities (RCs) are federally designated geographic areas characterized by high levels of poverty and economic distress, where businesses and local governments are often eligible to receive federal grants and tax incentives.

Since 1993, Congress has authorized three rounds of EZs and one round of RCs with the objective of revitalizing federally selected economically distressed communities. These designations unlock a combination of federal tax incentives and grants.

Nearly \$1.8 billion in grant incentives provided to EZs and ECs have been allocated since 1993 and have mostly been expended. The Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010 enacted on December 17, 2010 extended EZ tax benefits, but not RCs, until the end of 2011.

There are several Empowerment Zone (EZ) tax incentives intended to help —economic development|| in areas that are struggling economically. One of these provisions allows

businesses to receive a credit equal to 20 percent of the first \$15,000 in wages paid to an employee who is a resident of the empowerment zone and who performs most of their work within the empowerment zone. The idea is to make it easier for companies to hire individuals in these poor areas. RC tax incentives, which have not been extended since they expired in 2009, are similarly allowed for businesses to collect an employment tax credit equal to 15 percent of the first \$10,000 in wages paid to an employee who is a resident of the renewal community and who performs most of their work within the renewal community.

Other investment incentives apply to both the EZ and RC programs with the goal of fostering economic development through an increase in the capital stock within the designated geographic areas. Firms may expense up to \$35,000 of the cost of new and used qualified property/assets they acquire when the assets are placed in service, for a total of \$285,000 if they are located in an EZ. Empowerment zone tax-exempt bonds can be issued for economic development projects in EZs. Capital gain deferral options are also available for investments within EZs and 50-75 percent of the gain from the sale of EZ small business stock held for more than five years is excluded from gross income.

There is also a special carve out for the District of Columbia (DC) Enterprise Zone, which includes census tracts in the District of Columbia with a poverty rate of at least 20 percent. Businesses in the DC Zone are eligible for the following tax benefits: (1) a wage credit equal to 20 percent of the first \$15,000 in annual wages paid to qualified employees who resided within the District of Columbia; (2) \$35,000 in increased Section 179 expensing; and (3) tax-exempt bond financing. Additionally, a capital gains exclusion is allowed for certain investments in small business stock held more than five years and made within the affected areas. These incentives were extended through 2011 after expiring in 2009.

Since federal grant programs also exist to assist these economic development zones/communities, it is unclear why these tax incentives should be extended. For entities applying for government funding, additional points are awarded on grant applications for the Department of Housing and Urban Development, Treasury, and Health and Human Services, and Department of Education programs.

Government-sponsored studies by the Government Accountability Office (GAO) and the Department of Housing and Urban Development (HUD) have failed to demonstrate EZ designation generating improvement in community outcomes.

In 2001, HUD published a progress report examining the first five years of the Empowerment Zone and Enterprise Communities programs. HUD investigators found little evidence that the EZ program resulted in community improvement. The small growth that did occur within these communities, given the low take-up rate of the tax incentives, may have been attributable to activities not related to EZ activities.

In 2006, GAO also released a report on the EZ program. This study found —none of the federal agencies that were responsible for program oversight—including HHS and the

Departments of Housing and Urban Development (HUD) and Agriculture (USDA)—collected data on the amount of program grant funds used to implement specific program activities. This lack of data limited both federal oversight and GAO’s ability to assess the effect of the program.

Despite a previous request by GAO as part of a 2004 study for these federal agencies to address this deficiency, GAO found this issue had not been addressed two years later. Based on the limited data GAO had, it could not determine that the EZ program was effective.

Tribal Economic Development Bond Program

Established in the 2009 stimulus legislation, the Tribal Economic Development Bonds (TEDB) program authorizes tribes to issue up to \$2 billion in bonds for economic development purposes, with each tribe selected for participation eligible to issue as much as \$30 million.

Unlike previous tribal bonds, this provision does not require bonded projects to fulfill an —essential government function,|| and thus can be used for a wide variety of initiatives including tourism development, convention facilities, golf course, and marinas. Tribes contend the provision brings them into parity with state and local government bond provisions.

The bonds are not always put to the best use. Thanks in part to the new tax free bond provision, the Salt River Pima-Maricopa Indian Community in Arizona constructed the new spring training facility for Major League Baseball’s Colorado Rockies and the Arizona Diamondbacks. With twelve baseball fields, including an 11,000 seat central stadium, two soccer fields, clubhouses, separate workout facilities for both teams, and a theater, the Salt River Fields complex is conveniently located near the tribes’ Talking Stick Resort, casino, and golf course.

The New York Times describes the new facility this way: —Simply put, it’s the nicest spring training facility in the majors.|| Legendary former Yankees manager Joe Torre gushed, —This is amazing. I’ve never seen anything like this in a major league place, much less a spring training facility. It’s incredible. It’s enormously impressive, it really is.||

Also, these bonds are provided for the development of certain facilities associated with casinos. Although Congress in the Recovery Act excluded gaming as a permitted use of TED Bonds, the IRS opened a very large loophole, as the prohibition does not explicitly extend to ancillary facilities, such as a hotel, if they are structurally independent. As such, a hotel built on top of the casino would be ineligible, but a hotel built next to the casino would qualify – even though they serve exactly the same function.

This proposal would prohibit the further issuance of any new bonds under the program. Eliminating this provision could save \$400 million over the next ten years.