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PRESIDENT'S PROPOSED FEDERAL FISCAL YEAR 2014 BUDGET

Budget Overview

President Obama released his proposed $3.77 trillion budget for Federal Fiscal Year (FFY) 2014 on April 10, 2013 - nine weeks after the date (February 4, 2013) required by law and also after both the House and Senate had passed their respective FFY 2014 budget resolutions. According to the Office of Management and Budget (OMB), the President's FFY 2014 Budget would reduce the Federal budget deficit by an estimated $1.8 trillion over the next 10 years of which roughly $580 billion would come from tax revenue increases. It would use much of the estimated savings to repeal $109 billion a year in sequestration spending cuts that, otherwise, would be imposed over eight years under current law.

The President's major deficit reduction proposals include the offer that he made to House Speaker Boehner in "fiscal cliff" negotiations last December. Limiting the value of tax deductions to no more than 28 percent and other high-income tax benefits would raise the estimated $580 billion in added tax revenue. Other budget savings include an estimated $400 billion in mandatory (entitlement) health savings, mainly from Medicare; $200 billion in other mandatory savings, such as from reduced farm subsidies and Federal retirement benefits; and $200 billion in additional discretionary savings. The proposed use of a "chained" measure of the Consumer Price Index (CPI) that, in effect, would reduce cost-of-living adjustments for Social Security and other entitlement benefits and income tax brackets would save an estimated $230 billion. All of these savings, in turn, would reduce net interest payments on the Federal debt by an estimated $210 billion over the next 10 years.

The President's Budget is far closer to the FFY 2014 budget resolution (S. Con. Res. 8) passed by the Senate on a 50 to 49 vote than the version (H. Con. Res. 25) passed by the House on a 221 to 207 party line vote. The Senate version similarly would reduce the Federal budget deficit by an estimated $1.8 trillion over 10 years, repeal the remaining sequestration cuts, and increase tax revenues while the House version would reduce the deficit by $4.6 trillion entirely through spending cuts, and replace defense sequestration cuts with deeper cuts in non-defense spending. The President's Budget differs from the Senate budget resolution by calling for greater mandatory spending cuts and smaller revenue increases. It should be noted that the Administration's budget estimates are not directly comparable to Congressional budget estimates because OMB's budget assumptions and methodologies vary from those used by the Congressional Budget Office (CBO). Small differences in budget assumptions for economic factors, such as inflation, unemployment, income, and interest rates, can make a difference of tens of billions of dollars in estimated Federal spending and revenues per year.

We also caution that the Administration has released limited information on its new budget proposals and that its budget documents do not specify the final FFY 2013 funding levels for individual programs as enacted under H.R. 933, the FFY 2013 Continuing Resolution, signed into law on March 26, 2013, and as affected by 5.0 percent sequestration cut that is applied to non-defense discretionary programs. As reported previously to the Board, the exact FFY 2013 funding level and amount of sequestration cuts for individual programs are subject to interpretation by the Executive Branch, and some Federal departments have limited authority to transfer funds between programs. Therefore, H.R. 933 requires each Federal department to submit an FFY 2013 spending or operating plan by program and activity level, which reflects the impact of sequestration cuts, to Congress by no later than April 25, 2013.

With these caveats in mind, we believe that the net overall fiscal impact on the County of the President's FFY 2014 Budget, if enacted, would be relatively small. This is largely because, similar to last year, the President is proposing a relatively small reduction in overall mandatory spending, such as Medicaid, which accounts for most of the County's total Federal revenue, and is proposing to fund most discretionary programs through which the County currently receives funding at or near FFY 2013 funding levels. The County would benefit over the next eight years if his proposal to repeal sequestration cuts were enacted though the net fiscal impact on the County would depend on how those cuts are replaced by offsetting cuts and/or revenue increases. It also is noteworthy that the President's budget proposals would increase

Federal expenditures in FFY 2014 by nearly $160 billion above the CBO's latest current law baseline estimate with most of his proposed 10-year spending cuts occurring after FFY 2018.

Major Budget Proposals of County Interest

Similar to President Obama's first three proposed budgets, his FFY 2014 Budget includes a package of terminations, major cuts, and/or consolidations of a number of discretionary programs, much of which is similar or identical to proposals included in one or more of his previous three proposed budgets. This includes the following proposals of County interest:

State Criminal Alien Assistance Program (SCAAP): The President proposes to terminate SCAAP, which received an appropriation of $250.2 million in FFY 2013 and $240 million in FFY 2012. The President's first three proposed budgets similarly would have terminated or deeply cut SCAAP. The County's most recent FFY 2012 SCAAP payment was an all-time low of $6.25 million.

Homeland Security Grants: Similar to last year, the President proposes to consolidate programs in the Federal Emergency Management Agency's (FEMA) State and Local Programs account into a new National Preparedness Grant Program (NPGP). The consolidated programs would include the State Homeland Security Grant Program and Urban Area Security Initiative Grant.

Hospital Preparedness Program (HPP): Similar to last year, the President proposes to reduce HPP funding from roughly $375 million to $255 million in FFY 2014. The County, which is one of only four local jurisdictions that receive direct HPP formula grants, received an HHP allocation of $10.6 million in FFY 2012 - a larger allocation than received by all but eight states.

Community Development Block Grant (CDBG): The President proposes to reduce CDBG funding from $2.94 billion to $2.79 billion in FFY 2014.

Community Services Block Grant (CSBG): Similar to last year, the President proposes to reduce CSBG funding from about $677 million to $350 million in FFY 2014. The Administration also proposes to target the $350 million in funding to the highest performing Community Action Agencies through a competitive grant process.

Grants-in-Aid to Airports: The President's Budget would reduce funding for the Grants-in-Aid to Airports program, which currently helps to fund operations and improvements at five County-owned airports, by $450 million to $2.9 billion in FFY 2014.

Other major budget proposals of County interest include:

Medicaid Disproportionate Share Hospital (DSH) Funding: The Affordable Care Act (ACA) reduced DSH funding by a combined total of $18.1 billion in FFYs 2014 through FFYs 2020. The Medicaid DSH cuts subsequently were extended through FFY 2021 under Public Law 112-96 and FFY 2022 under Public Law 112-240. Under current law, beginning in FFY 2023, annual DSH allotments would revert back to the higher levels, including increases for inflation, which would have been in effect without the ACA's cuts. The President's Proposed Budget would delay the start of the ACA's Medicaid DSH cuts for one year to FFY 2015, and be budget neutral by spreading the FFY 2014 DSH reduction of $500 million into FFYs 2016 and 2017. This proposed one-year delay in starting Medicaid DSH cuts makes sense because, less than six months before the start of FFY 2014, the Department of Health and Human Services (HHS) has not yet released proposed regulations for the methodology to be used for distributing the DSH cuts among states.

It also would "rebase" (determine) future DSH allotments beyond FFY 2022 "based on states' actual DSH allotments as reduced by the Affordable Care Act." According to OMB, this estimated rebasing of the Medicaid DSH cuts would save $3.6 billion over a 10-year period, ending in FFY 2023. Similar to last year when the President proposed the rebasing of Medicaid DSH allotments beyond FFY 2020, HHS has not released detailed language for its latest proposal. It is unclear how the future "rebasing" of future Medicaid DSH allotments will vary from how they were rebased in FFYs 2021 and 2022 when CBO estimated the savings to be $4.0 billion in FY 2021 and $4.2 billion in FY 2022, rounded to the nearest 100 million.

Gun Violence Reduction Funding: The President's FFY 2014 Budget includes funding requests that are consistent with his plan to reduce gun violence that was released in January 2013. This includes requests of $150 million for the COPS Comprehensive School Safety Program, $51 million to increase Federal enforcement of existing gun safety laws, $100 million to expand the capacity of the National Instant Criminal Background Check System (NICS), $55 million in grants to states to improve the submission of criminal and mental health records to the NICS, $55 million for a new project to help school districts to detect and refer students with signs of mental illness to service providers, $50 million to train 5,000 additional mental health professionals to serve students and young adults, and $50 million for suicide prevention programs.

Military Base Realignment and Closure (BRAC): The Administration is proposing a new BRAC round in 2015 to help reduce defense spending. During the last BRAC round in 2005, it was speculated that Los Angeles Air Force Base (LAAFB) might be realigned, but the base was determined to have a high military value and kept open. Moreover, since that time, the Air Force approved a land swap at LAAFB, which in effect, will significantly reduce the cost savings that would be achieved from closing it in the future. Congress would have to enact legislation in order to authorize a new BRAC round, but Congress rejected the Administration's similar request for a BRAC proposal last year.

Section 8 Tenant-Based Rental Assistance: The President proposes to increase Section 8 Tenant-Based Rental Assistance from $18.94 billion to $19.98 billion in FFY 2014 to support existing vouchers and provide new vouchers targeted to homeless veterans. It also includes an increase for Administrative Fees from $1.37 billion to $1.68 billion in FFY 2014.

Homeless Assistance Grants: The President proposes to increase Homeless Assistance Grants from $2.03 billion to $2.38 billion in FFY 2014 to help maintain HUD-funded beds that assist the homeless and expand rapid re-housing and permanent supportive housing. The Los Angeles Homeless Services Authority is the primary recipient of Homeless Assistance Grant funding within the County.

Child Care and Development Fund: The President proposes to increase the Child Care and Development Fund by a total of $700 million a year over the next 10 years, including an annual increase of $200 million for the discretionary Child Care and Development Block Grant (CCDBG), which is subject to available annual appropriations, and an annual increase of $500 million for the Child Care entitlement, which would be set by statute. In FFY 2013, CCDBG received roughly $2.3 billion in appropriations while the Child Care Entitlement was funded at roughly $2.9 billion.

Preschool for All Initiative: The President proposes a new initiative to provide all low and moderate income four year-olds with high quality preschool that would be funded by raising the Federal tax on cigarettes and other tobacco products.

Human Trafficking Initiative: The President proposes $10 million in FFY 2014 for a new initiative to prevent and address domestic human trafficking that would provide direct services to domestic victims of trafficking, train service providers, and invest in data collection, research and evaluation.

Budget Outlook

Both houses of Congress already have passed widely divergent FFY 2014 budget resolutions on party line votes, and the President's major deficit reduction proposals previously were offered - and rejected - by the Congressional Republican leadership during the "fiscal cliff" negotiations. To date, neither party has indicated any willingness to compromise on the issue of net tax revenue increases - Democrats want budget savings to include increased revenue while Republicans oppose any net revenue increase. It, therefore, is extremely unlikely that both houses will reach agreement on an FFY 2014 budget resolution, which would include budget reconciliation instructions that importantly would allow changes to entitlement spending and taxes to pass the Senate with a simple majority rather than 60-vote majority.

In the absence of an agreed upon budget resolution, which sets non-binding spending and revenue targets, the Senate and House may prepare their respective FFY 2014 appropriations bills using different discretionary spending ceilings. If so, this would increase the likelihood of Congress enacting few, if any, of the 12 individual FFY 2014 appropriations bills, which means that an omnibus appropriations bill or continuing resolution (CR) again would be needed to fund Federal programs through the end of FFY 2014.

The next key Federal budget deadline will be late July, which is the expected deadline for increasing the Federal debt ceiling to enable the Federal government to borrow funds needed to finance Federal operations and to avoid a default on its debt service. Earlier this year, legislation was enacted to suspend the Federal debt ceiling through May 18, 2013, though it currently is believed that the Treasury Department can take extraordinary measures, such as borrowing from trust funds, to postpone the need to increase the debt ceiling until late July. Debt ceiling increase legislation could be the vehicle for enacting major budget changes, such as a deficit reduction package or repeal of sequestration cuts. If debt ceiling legislation does not include such changes, the risk of major Medicaid and/or other entitlement cuts being enacted this year would be greatly diminished.

We will continue to keep you advised.

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