# Fiscal Highlights

**Sequestration Update** - Steven M. Allred

In December 2013, Congress passed the Bipartisan Budget Act of 2013 (BBA), providing states some certainty in federal funding and reducing the threat of federal shutdowns for the next two years.

By way of background, the Budget Control Act of 2011 (BCA) required Congress to reduce the deficit by $1.2 trillion over ten years (FY 2012 to FY 2021). Since Congress failed to come up with deficit reduction legislation, automatic spending cuts called sequestration kicked in. The American Taxpayer Relief Act of 2012 postponed the FY 2013 cuts for two months and reduced that year's sequestration to make up for the shorter amount of time in which to achieve savings. All non-exempt programs received across-the-board cuts of approximately 5 percent.

Beginning in FY 2014, sequestration is handled differently. "Mandatory" programs (those in which the annual cost is determined by statutory eligibility criteria) will continue to experience across-the-board cuts similar to FY 2013. The majority of mandatory funding awarded to states is exempt from sequestration, but some mandatory funding is not exempt, notably grants for rehabilitation, mineral leasing, social services block grants, and payments in lieu of taxes.

Non-exempt "Discretionary" programs (those in which funding is determined by annual appropriations bills) will not undergo across-the-board cuts in FY 2014 - FY 2021. Rather, appropriations must adhere to spending caps, and Congress can choose to cut or spare individual programs through the appropriations process.

The BBA increased the spending caps for FY 2014 and FY 2015 by $63 billion ($45 billion in FY 2014 and $18 billion in FY 2015). It offset the increases with $85 billion in deficit reductions achieved mostly through increased airline passenger fees, decreased federal employee pensions, decreased military retiree COLAs before age 62, and extended sequestration of non-exempt mandatory programs for two years until FY 2023. Federal spending will thus be larger in the next two years but less in subsequent years until FY 2023 (barring future changes to the law).

Federal funds are 27 percent of the state budget in FY 2015. While passage of the BBA provides more certainty to states than we've had in the recent past under the "fiscal cliffs," risks remain. Such risks could include debt ceiling standoffs, geo-political events, loss of federal borrowing capacity, and many others.