



U.S. HOUSE OF REPRESENTATIVES

# COMMITTEE ON THE BUDGET

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## Sequestration: An Update for 2013

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# Sequestration: An Update for 2013

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# Sequestration: An Update for 2013

*Sequestration: The cancellation of budgetary resources, or holding back money that would otherwise be spent under current law.*

## Overview of Budget Changes in the Fiscal Cliff Deal

The American Taxpayer Relief Act of 2012 (H.R. 8, now P.L. 112-240) averted the so-called “fiscal cliff” crisis by raising new revenue from upper-income taxpayers, extending middle-class tax relief, and modifying upcoming sequestration of spending.

### Background on Sequestration

The Budget Control Act of 2011 (BCA) contained two different orders for sequestration – automatic spending cuts to all non-exempt programs. The **deficit reduction sequester** required nine annual sequesters of \$109 billion – half from defense and half from non-defense programs – if the work of the Joint Select Committee on Deficit Reduction did not result in enactment of deficit reduction of at least \$1.2 trillion. The first of these annual sequesters was set to take effect on January 2. The BCA also mandated a separate **discretionary sequester** if appropriations for any year exceeded the annual caps set by the law. For 2013, that discretionary sequester will now apply separately to security and non-security categories, so a breach in one cap would trigger a discretionary sequester only to that category. Starting in 2014, those categories change to defense and non-defense spending. (See Question 6 below for further details on the categories.)

### **Budget Process Changes Made by H.R. 8**

#### Deficit Reduction Sequester

- Reduced by \$24 billion for 2013
- Postponed until March 1 (instead of January 2)

#### Discretionary Caps

- Reduced by \$4 billion for 2013 and \$8 billion for 2014
- Discretionary sequester for 2013 postponed until March 27 (instead of 15 days after the end of session)
- Changed categories for 2013 from defense/non-defense to security/non-security

### Changes Made in the Fiscal Cliff Deal

The deficit reduction sequester of approximately \$109 billion had been slated to take place on January 2. The deal moved the date to March 1, and reduced the spending cuts required by \$24 billion.

The measure also postponed the looming discretionary sequester – originally due 15 days after the end of session – until March 27, which is consistent with the expiration of the Continuing Resolution providing 2013 appropriations.

The agreement also reduced the discretionary caps by a total of \$4 billion for 2013 and by \$8 billion for 2014. Because of the delay in the discretionary sequester, the Appropriations Committee has an opportunity to provide funding for 2013 consistent with the new discretionary limits. The 2013 levels for security and non-security categories are reduced by \$2 billion each, for a total discretionary level of \$1,043 billion (down from the \$1,047 billion in the original BCA for 2013 and identical to the 2012 cap). For both the deficit reduction sequester and the 2014 discretionary caps, the categories remain split between defense and non-defense spending, with both the defense and non-defense discretionary cap reduced by \$4 billion for 2014, to a total level of \$1,058 billion.

## Frequently Asked Questions about Sequestration

### 1. How does the deficit reduction sequester work?

The BCA requires spending cuts that will accomplish the deficit reduction that the efforts of the Joint Select Committee on Deficit Reduction did not achieve. The cuts, to be carried out over a nine-year period, are divided evenly between defense and non-defense spending, including both discretionary and mandatory programs. The first round of cuts – which had been set to take effect on January 2, 2013 – have now been reduced by \$24 billion and rescheduled to take effect on March 1, 2013.

### 2. How much spending will the deficit reduction sequester cut?

The deficit reduction sequester was originally designed to enforce savings of \$1.2 trillion through 2021. Based on the calculations in the BCA before the passage of H.R. 8, spending on government programs would have been reduced by \$984 billion, with the remaining savings from reduced debt service costs.

Previously, for 2013 that meant a \$55 billion cut in defense and a \$55 billion cut in non-defense spending. Those 2013 amounts are now reduced by \$24 billion in total.

2013 Deficit Reduction Sequester			
In billions of dollars			
	Defense	Non-Defense	Total
Discretionary	54.6	38.0	92.6
Mandatory	0.1	16.6	16.7
Original Total	54.7	54.7	109.3
<i>Fiscal Cliff Change</i>	<i>-12.0</i>	<i>-12.0</i>	<i>-24.0</i>
<b>New Total Cut</b>	<b>42.7</b>	<b>42.7</b>	<b>85.3</b>

Source for original split: [OMB](#). Table may not add due to rounding.

CBO made [rough calculations](#) last year that the \$984 billion in programmatic reductions would translate into \$888 billion in deficit reduction through 2021. The deficit reduction amount is lower for two reasons. First, for discretionary programs the programmatic reduction applies to budget authority, which sets the level of funding a program is eligible to spend, but not how much actually flows out of the Treasury in that fiscal year. Changes in budget authority result in outlay changes – the actual flows from the Treasury – over a period of years. Some of the outlay changes from the sequester will occur beyond 2021 and are thus not included in the deficit reduction through 2021. Second, reductions in Medicare required under the sequester will not achieve the full reductions because they cause some offsetting effects, such as reducing Medicare premiums since they are calculated based on program costs. These effects offset a portion of the savings in the program.

**3. How much of the sequestration comes from discretionary versus mandatory spending?**

The bulk of the deficit reduction sequestration savings come from discretionary programs (those funded by annual appropriations bills) as opposed to mandatory programs (also known as direct spending, or entitlement spending, where a program’s annual cost is generally determined by eligibility criteria established by law). The required savings are to come half from defense programs and half from non-defense programs. Within each half, the savings are allocated to discretionary and mandatory programs based on the contribution each makes to the total of discretionary budget authority and sequesterable direct spending. Because defense has almost no mandatory funding subject to sequestration, almost all of the defense portion will come from discretionary programs. On the non-defense side of the budget, mandatory programs will account for about one-third of the non-defense savings. Thus, almost all defense savings and about two-thirds of non-defense savings will come from discretionary programs.

**4. What is the total effect on discretionary spending?**

At the time of the BCA’s enactment, [CBO estimated](#) that the initial discretionary spending caps cut spending by \$800 billion over ten years (2012 through 2021) compared with continuing the current levels (which had already been reduced in previous legislation) adjusted for inflation. Those caps will be replaced by even lower caps as part of the deficit reduction sequester and the additional discretionary cut for 2013 and 2014 in the fiscal cliff deal. In its [economic update](#) in August 2012, CBO estimated the deficit reduction sequester will reduce discretionary spending by an additional \$900 billion over ten years below the existing BCA caps. H.R. 8 further reduced discretionary caps by a total of \$12 billion over 2013 and 2014.

## **5. Which programs will be sequestered?**

For 2013, the deficit reduction sequestration will apply individually to discretionary and mandatory programs unless they are specifically exempted. In its September 14 [report](#) to Congress, OMB provided a preliminary list of which accounts are exempt and approximately how much each category of spending will be cut, although the percentage cut will change based on actual appropriations and the changes in H.R. 8.

On the discretionary side of the budget, few accounts are exempted. Pell grants, spending from most transportation trust funds (which support highways, mass transit, and airports), and all programs administered by the Department of Veterans Affairs are exempt. The President also exercised his discretion to exempt military personnel accounts for 2013.

On the mandatory side of the budget, the bulk of spending is either exempt or subject to a special rule. Social Security is exempt, as are many programs that serve low-income beneficiaries, including Medicaid, Supplemental Nutrition Assistance Program (formerly called food stamps), Supplemental Security Income, and Temporary Assistance for Needy Families. Federal retirement and disability accounts and veterans' programs are exempted, as are most refundable tax credits. Other specific exemptions include a variety of government insurance programs and activities funded from private donations or voluntary contributions. Most of Medicare payments to providers are subject to sequestration but limited to a 2 percent reduction. (Some of Medicare is exempt and a small portion is subject to the full sequester.) Farm support programs comprise the largest component of the remaining mandatory spending subject to full sequestration.

For 2014 and beyond, the deficit reduction sequester works a little differently for discretionary programs. In those years, the portion of the sequester that applies to discretionary programs will lower the discretionary caps, not funding for individual programs. It will be up to the Appropriations Committee to determine how the cuts are allocated. If the Appropriations Committee breaches the caps, the separate discretionary sequester would apply at the program level to remove the breach.

## **6. What are the firewalls? What is the "security" category?**

The BCA set different spending caps for different discretionary categories, separated by a "firewall" for enforcement purposes. If a cap is breached in one category, the firewall requires an offsetting discretionary sequester only within that portion of discretionary spending rather than across all discretionary categories.

The BCA includes a security category for discretionary caps that refers to programs within the Departments of Defense, Homeland Security and Veterans Affairs; the National Nuclear

Security Administration; the intelligence community management accounts; and accounts in the International Affairs budget function. H.R. 8 uses the security and non-security categories for purposes of the 2013 discretionary sequester.

For the deficit reduction sequester and discretionary sequester for 2014 through 2021, the BCA uses the categories of non-defense spending and defense, which is the federal budget's national defense function. That includes the Department of Defense, nuclear-energy related activities at the Department of Energy, the national security activities of several other agencies such as the Selective Service System, and portions of the activities of the Coast Guard and Federal Bureau of Investigation.

**7. What percentage of the cut is in “defense” versus “non-defense” programs?**

The deficit reduction sequester requires that half of the savings come from defense programs and half from non-defense programs.

For a discretionary sequester, only the programs in the category violating the cap are subject to sequester. That is, if the security cap is breached, only security spending would be sequestered.

**8. Is funding for Overseas Contingency Operations (OCO) exempt from a deficit reduction sequester?**

No. Classification as OCO does not exempt spending from a sequester. However, to the extent that OCO funding is covered by other exemptions in the law, it will be exempt. The President has exempted military personnel from the sequester. As a result, the military personnel accounts classified as OCO will also be exempt.

**9. Will sequestration cuts be at the program level, or at the budget account level?**

The deficit reduction sequestration occurs at the program-by-program level, with every non-exempt program cut by the percentage required to reach the calculated deficit reduction target for that year. There may be budgetary accounts within agencies that have some programs exempt from sequestration or where the size of the sequestration is limited by statute, whereas other programs are not exempt and are subject to the full cut required.

**10. Who determines the size of the required cut, and when will we know the specifics?**

Under budget law, OMB will manage all aspects of the deficit reduction sequester. The law specifies that OMB estimates are to be used to determine both which programs are exempt from the sequester and the size of the cut on the remaining programs. Neither the CBO nor the Budget Committees plays a role in implementing the sequester. OMB issued a preliminary list of exempt programs and a rough estimate of the size of the cut to each category of spending in its September 14 [report](#), but those cuts would now be smaller

because the 2013 sequester has been reduced by \$24 billion (22 percent). OMB will need to recalculate the precise cut to each program using actual levels enacted for 2013 in the continuing resolution, and an updated estimate of the level of unobligated balances in defense accounts.

**11. How much discretion does the President have in how the sequester is applied?**

Almost none. The President does not have discretion to vary the size of the cut to agency budgets. The President has exercised his authority to exempt military personnel accounts from sequestration, which did not change the total defense sequester – the amount of the sequester on other defense programs will increase. All agencies will continue to have their existing transfer authority with the limitations that are specific to each agency.

**12. How is the sequester in 2013 different from the sequester in following years?**

The deficit reduction sequester for 2013 will reduce spending not only for all non-exempt mandatory programs, but it will also lower the amount already appropriated for all non-exempt discretionary programs. For 2014 through 2021, the effect of the deficit reduction sequester on appropriations will be to lower the total annual discretionary cap. The Appropriations Committee will then allocate funding under that new, lower cap, but funding will not be further cut by a sequester (unless total appropriations exceed the caps set in law, in which case there will be a discretionary sequester). The sequester for mandatory programs for 2014 through 2021 will follow the same process as for 2013.

**13. Is there a waiver?**

There is no waiver of the deficit reduction sequester unless there is a declaration of war. The only option for changing it would be to enact legislation to amend the BCA.



## Sources for information mentioned in this report

“OMB Report Pursuant to the Sequestration Transparency Act of 2012 (P. L. 112–155),”  
September 14, 2012:

[http://www.whitehouse.gov/sites/default/files/omb/assets/legislative\\_reports/stareport.pdf](http://www.whitehouse.gov/sites/default/files/omb/assets/legislative_reports/stareport.pdf)

The Budget Control Act of 2011 (P.L. 112-25): <http://www.gpo.gov/fdsys/pkg/PLAW-112publ25/pdf/PLAW-112publ25.pdf>

CBO’s “Update to the Budget and Economic Outlook: Fiscal Years 2012 to 2022,” August 22, 2012: <http://www.cbo.gov/publication/43539>

Congressional Research Service report on “Budget ‘Sequestration’ and Selected Program Exemptions and Special Rules,” November 23, 2011:

<http://www.crs.gov/pages/Reports.aspx?PRODCODE=R42050&Source=search>

CBO report on the “Estimated Impact of Automatic Budget Enforcement Procedures Specified in the Budget Control Act,” September 12, 2011: <http://cbo.gov/ftpdocs/124xx/doc12414/09-12-BudgetControlAct.pdf>

CBO Analysis of the Budget Control Act, August 1, 2011:

<http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/123xx/doc12357/budgetcontrolactaug1.pdf>

The American Taxpayer Relief Act of 2012 (H.R. 8, P.L. 112-240):

<http://www.gpo.gov/fdsys/pkg/BILLS-112hr8enr/pdf/BILLS-112hr8enr.pdf>