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Sequestration Is Now in Effect: What It Could Mean to California

In August 2011, Congress passed, and President Obama signed, the Budget Control Act of 2011 to reduce projected budget deficits.[1] This law specifies across-the-board spending cuts to many federal programs and would have taken effect in January 2013, but legislation delayed the start date. These automatic federal spending cuts—known as sequestration—are intended to ensure a $1.2 trillion deficit reduction in federal government spending over a 10-year period. These cuts went into effect on March 1, 2013.

In addition to delaying the start of sequestration by two months, the American Taxpayer Relief Act of 2012 (ATRA)[2] lowered the overall deficit reduction from $109 billion to $85 billion for federal fiscal year 2013. These across-the-board spending cuts impact many federal discretionary programs and mandatory programs.[3]

Which Federal Government Programs Are Impacted?

According to Congressional Budget Office estimates, the $85 billion reduction is composed of $71 billion in discretionary spending cuts and $14 billion in mandatory spending cuts for federal fiscal year 2013; these reductions are, in general, equally divided between defense and non-defense spending. The federal Office of Management and Budget says, for federal fiscal year 2013, resources subject to sequestration for defense will be cut by nearly 8 percent, and by about 5 percent for non-defense funding.

While many federal programs are subject to automatic cuts by a fixed percentage, the

Sequestration (Automatic Federal Budget Cuts) Was Triggered on March 1, 2013
Many big-ticket budget items—such as basic elementary and secondary education funding—are subject to sequestration. California relies on billions of dollars in federal funding every year, and cuts to these funds due to the sequester will be felt by numerous programs.

Budget Control Act (BCA) explicitly exempts some programs (particularly entitlements and programs that aid low-income Americans). The process for determining the cuts is specified in the BCA, and in part depends on spending levels in a continuing resolution signed into law in September 2012. The federal sequestration table below outlines which programs would receive cuts of about 5 percent to 8 percent,[4] and which would be protected.

Sequestration (Automatic Federal Budget Cuts)

THE FEDERAL PROGRAMS AFFECTED AND EXCLUDED

Major federal programs currently slated to receive automatic cuts of 5 percent to 8 percent	Major federal programs currently protected from sequestration
> Defense programs (many affect defense contractors) > Head Start and Child Care and Development Block Grant > Health and Human Services programs (for example, Medicare;* National Institutes of Health grants; Women, Infants, and Children Supplemental Feeding Program; and Substance Abuse and Mental Health Services Administration grants) > Housing programs (for example, Section 8 vouchers, homeless assistance grants, and the Low-Income Home Energy Assistance Program) > Job training programs (Workforce Investment Act programs) > K–12 education programs (for example, Title I and special education) > Public safety (for example, State Criminal Alien Assistance Program)	> Child nutrition (for example, school lunches) > Federal-aid highway programs > Medicaid (Medi-Cal)** and Children's Health Insurance Program (Healthy Families) > Military salaries > Pell grants > Social Security benefits > Supplemental Nutrition Assistance Program (CalFresh, formerly known as food stamps) > Supplemental Security Income > Temporary Assistance for Needy Families (CalWORKs) > Veterans' benefits and health care

* Medicare will receive a 2 percent cut.

** Although Medicaid grants to states are exempt from the sequester, Medicaid's state Grants and Demonstrations account is not exempt. Several programs are under this account, although only the Money Follows the Person Demonstration and the Medicaid Integrity programs would be impacted, as they are the only two programs that received funding in federal fiscal year 2012 and under the current continuing resolution.

How Is California Affected?

California receives large amounts of funding from the federal government: approximately $86 billion in federal funds will be funneled through the state budget in 2012–13. Even more federal funds flow directly to localities and entities outside of the state budget, such as Medicare payments to providers, and Head Start payments to locally based organizations.

As a result of the sequester, California could lose several hundreds of millions of federal dollars in federal fiscal year 2013 alone.[5] For example, National Institutes of Health grants to the state could be reduced by nearly $200 million.[6] And according to the U.S. Department of Education, K–12 schools in California could lose more than $200 million in federal funds.

The federal sequestration, along with two other federal fiscal issues—the budget and the debt ceiling—could have significant impacts on California's budget and economy (see "Other Looming Federal Fiscal Issues" below). Lawmakers likely will look at components of various alternative policies proposed over the past few years (such as the president's budgets) for solutions to these fiscal challenges. This means *all* programs—including those now exempt from sequestration—could be reconsidered as potential deficit reduction sources as lawmakers continue with their negotiations. And that means proposals to reduce state entitlement funding (such as for Medicaid) could result in a significant fiscal burden to California during a time of precarious economic recovery.

Other Looming Federal Fiscal Issues

In addition to sequestration, two major fiscal issues Congress and President Obama must address in the coming months are: the expiration of the federal continuing resolution on March 27, 2013, and the end of the debt limit suspension on May 19, 2013.

The Federal Budget

Federal agencies are operating under a continuing resolution until March 27, 2013,[7] because Congress has not yet passed the necessary federal appropriations bills for federal fiscal year 2013. To keep the federal government funded after March 27, Congress must either pass final fiscal year 2013 appropriations bills or a continuing resolution that will fund the federal government for the last six months of the fiscal year—from March 27, 2013, through September 30, 2013.[8]

The Debt Ceiling

To avoid defaulting on federal obligations, which could lead to a partial government shutdown, Congress took action in early February 2013 and suspended the limit on borrowing through May 18, 2013. On May 19, the existing debt ceiling will be increased by the amount of borrowing that took place while the limit was suspended (from early February to May 18). If no further action takes place before May 19, the U.S. Treasury will need to use extraordinary measures[9] to ensure the government can continue to pay its bills and operate normally for the rest of the year.

Endnotes

1 Public Law 112–25.

2 Public Law 112–240.

3 Discretionary programs are funded through federal appropriations bills; Congress sets the funding level for each program through the annual federal budget process. Mandatory programs generally are funded through legislation other than federal appropriations bills, and include entitlements, such as Social Security and Medicare. Congress controls spending for these programs indirectly—that is, outside the budget process—by setting benefit rules and eligibility levels.

4 Medicare will receive a 2 percent cut.

5 This estimate is based on a potential extension of the current continuing resolution (and therefore annualized funding).

6 "BCA Sequester: Impact of Two-Month Delay," Special Analysis 13–01, Federal Funds Information for States (FFIS), January 15, 2013.

7 Continuing Appropriations Resolution, 2013, Public Law 112–175.

8 The Budget Control Act (BCA) also includes spending caps for discretionary spending. If current funding levels are extended for the remainder of federal fiscal year 2013, these spending caps will be exceeded, and the extended funding levels will have to be adjusted downward to conform to the BCA.

9 Congress may use so-called extraordinary measures to prevent exceeding the debt limit. These steps may include, for example, suspending investments in federal retiree pension funds.

Written by Meredith Wurden and Meg Svoboda. Federal Update is a series of occasional briefs researched and written by the California Senate Office of Research (SOR) to highlight federal issues and their potential impact on California. SOR is a nonpartisan office charged with serving the research needs of the California State Senate and assisting Senate members and committees with the development of effective public policy. It was established by the Senate Rules Committee in 1969. For more information and copies of this report, please visit **www.sen.ca.gov/sor** or call **(916) 651-1500.**