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Altering Accounting for Federal Credit Programs Would Artificially Inflate Costs, Raise Risk of Cuts

By Richard Kogan

The House Budget Committee will consider a bill tomorrow to change the accounting for federal loan and loan guarantee programs to make them look more expensive to the federal government than they really are. This proposal (The Budget and Accounting Transparency Act, H.R. 1872) would affect all 100-plus loan programs, ranging from veterans' housing loans to agriculture loans to student loans, disadvantaging them relative to other federal programs and exposing them to a greater likelihood of cuts.[1]

Partial List of Programs Affected by Proposal

- Veterans' housing loans
- Small business loan guarantees
- Small business disaster assistance loans
- Small business direct microloans
- Overseas Private Investment Corporation (OPIC) loans and guarantees
- Export-Import Bank (Ex-Im) short-, medium-, and long-term guarantees
- Commodity Credit Corporation (CCC) export guarantee (GSM) loans
- Rural water and waste disposal loans
- Agriculture Credit Insurance Fund (ACIF) operating and capital loans
- Rural electrification loans
- Rural Housing Insurance Fund (RHIF) single- and multi-family housing loans
- Federal Housing Administration (FHA) loans of all types
- Indian housing guarantees
- Student loans, subsidized and "unsubsidized"
- Ford "PLUS" loans
- Title 17 Innovative Technology (alternative energy) loans
- Transportation infrastructure, finance, and innovation (TIFIA) loans
- Railroad rehabilitation and improvement loans

[1] For more thorough discussions of the deficiencies of the proposal, see these two CBPP reports: Paul N. Van de Water and Joan Huffer, "House 'Budget Transparency' Bill Will Make Budget More Opaque," June 18, 2013, http://www.cbpp.org/cms/index.cfm?fa=view&id=3976; Richard Kogan, Paul Van de Water, and James R. Horney, "House Bill Will Artificially Inflate Costs of Federal Credit Programs," revised June 18, 2013, http://www.cbpp.org/cms/index.cfm?fa=view&id=3661 .

The Congressional Budget Office (CBO) estimates that the proposal would raise the official cost of the affected programs by $55 billion per year.[2] This means that it could make ten-year deficits appear half a trillion dollars higher than they really are. As policymakers react to this apparently worsening outlook, this distortion of credit programs' actual cost could put upward pressure on taxes and downward pressure on all programs, not just credit programs.

In addition, CBO estimates that $24 billion of this $55 billion in additional annual cost would occur in discretionary programs, meaning that annual appropriations bills would be scored as $24 billion more costly than they really are, all else being equal.

CBO also reports that 44 of the 100-plus credit programs cost the government *nothing* — or even make money for the government — under existing accounting because they receive origination fees and interest payments that cover (or more than cover) the defaults that occur. But, CBO reports, the proposal would make 33 of those 44 programs *appear to* cost money. That artificial change might change policymakers' perception of those programs, adversely affecting them in the appropriations process or the broader budget process.

Proposal Would Inflate Cost Based on What Private Lenders Would Charge

The federal budget records credit programs, like all other federal programs, based on the amount of money that they actually cost (or generate for) the federal government. Since 1992, a special procedure has been used to show the net costs of those programs up front rather than spread over the many years it takes loans to be repaid in whole or in part. But that procedure produces the same total costs over time as the prior pure-cash accounting.

The proposal before the House Budget Committee would add a *loss-aversion penalty* to the recorded cost of every credit program, largely reflecting the additional amount that private lenders would charge if they, not the federal government, provided the loans. The main reason for the penalty is that the price of capital is higher for the private sector. The penalty may also reflect the fact that private lenders are less able to recoup losses when some loans are not repaid (and, perhaps, would not make the loans at all if they did not expect a sufficient profit).

It is important to note that supporters of the proposal do *not* contend that current estimates of the costs of credit programs misrepresent the cash flows related to loans and guarantees. They merely advocate adding an extra charge to reflect the private sector's loss-aversion, which is built into private-sector lending practices.

But is this really relevant? A program does not cost the federal government more than the government actually spends just because the same program would cost private lenders more. Nor would the proposed accounting change make credit programs more expensive; it would just make them *appear* more expensive.

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[2] This $55 billion estimate and those in succeeding paragraphs are from CBO, *Fair Value Estimates of the Cost of Federal Credit Programs in 2013*, June 27, 2012, at http://www.cbo.gov/publication/43352, and backup data at that source.

That is the fundamental flaw in the proposal. Budgets should record actual costs, and budget proposals should be estimated the same way. This proposal would make increases in credit programs appear to cost more than they really cost — and make cuts appear to save more than they really save. Especially in light of the very tight appropriations caps that the Budget Control Act of 2011 established, this proposal would expose federal credit programs to greater likelihood of cuts.

Advocates of the proposed accounting change call it "fair-value accounting," but in reality, the proposal would put loan programs at an *unfair* disadvantage. Regardless of one's position on whether credit programs are generally worthwhile, the budget should put them on a level playing field with other programs. The proposed accounting change would tilt the playing field against these programs, thereby distorting the process of setting policy priorities.