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# Declining Surplus Renews Debate Over the Budget Outlook

**By RICHARD W. STEVENSON**

WASHINGTON, July 11 — The Bush administration said today that the weakening of the economy might push the federal budget surplus this year down to a level that, Democrats said, would portend a return to fiscal difficulties in the years ahead.

Mitchell E. Daniels Jr., director of the White House Office of Management and Budget, said the government would run a surplus this year big enough to meet the bipartisan commitment to use excess Social Security revenue only for reducing the national debt. And Mr. Daniels said there was no risk "at present" that the economic downturn would force the government to dip into Social Security surpluses in coming years.

But he did not rule out the possibility that the surplus this year would fall short of earlier expectations by enough to breach what Democrats have sought to establish as a standard for fiscal responsibility: reserving excess funds generated by the Medicare system, as well as the entire Social Security surplus, for debt reduction.

The Congressional Budget Office's most recent projections, made two months ago, forecast a surplus in Social Security this year of $156 billion and a surplus in Medicare's hospital insurance trust fund of $28 billion, a total of $184 billion. At the time, the budget office forecast a surplus in the general budget of an additional $16 billion, leaving the government $200 billion in the black for the year.

Since the economy all but stalled this spring, however, private economists and government budget analysts have been marking down their surplus estimates. Today Mr. Daniels said the White House now expected a surplus of at least $160 billion for the fiscal year that ends on Sept. 30.

In a briefing for reporters, Mr. Daniels said the actual figure could be higher, and in any case would be larger than the Social Security surplus. But he said it was too early to know whether it would dip below the level of the combined Medicare and Social Security surpluses.

"The surplus is in great shape," Mr. Daniels said. "It's the economy that's not in the best of shape."

Mr. Daniels said the 10-year, $1.35 trillion tax cut signed into law by President Bush last month would give the economy a big lift in coming months, ensuring that tax receipts rebound in the new fiscal year, starting Oct. 1.

In a $2 trillion federal budget and a $10 trillion national economy, there is little or no

economic significance to whether the surplus is slightly above or slightly below the combined Medicare and Social Security surpluses.

But the political implications of its falling below could be substantial, providing Democrats an opportunity to portray Mr. Bush's tax cut as too expensive and to cast themselves as guardians of fiscal restraint.

The chairman of the Senate Budget Committee, Senator Kent Conrad, Democrat of North Dakota, will hold a hearing on Thursday where he plans to question Mr. Daniels closely on the budget outlook.

In an interview, Mr. Conrad said the possibility that the government would be forced to dip into the Medicare surplus this year was evidence that Congress and the administration were likely to "raid" both the Medicare and Social Security surpluses starting next year.

"It shows we're into the Medicare trust fund already this year," Mr. Conrad said, "and we see serious danger" of using all of the Medicare surplus next year, along with some of the Social Security surplus.

Mr. Conrad maintained that the fiscal outlook was even dimmer than it seemed, saying his own projections did not take account of a variety of tax and spending measures that have strong bipartisan support and are likely to create even more budget pressure in coming years.

Among them, he said, are proposed spending increases for the military and education, the extension of popular tax breaks and reductions in the alternative minimum tax, a complex provision that will push up the tax bills of millions of middle- and upper-income people over the next decade unless revised.

"It suggests to me that we have to go back to the drawing boards with respect to the budget for next year and beyond," Mr. Conrad said.

Mr. Daniels said Mr. Conrad was assuming that government spending would increase at a pace higher than what Mr. Bush will support. In any case, he said, it is meaningless to measure fiscal health relative to the Medicare surplus, which he described as an accounting gimmick.

The Medicare surplus is generated by one part of the Medicare program, its hospital insurance trust fund. The rest of Medicare requires infusions of general tax revenue each year. So there is no Medicare surplus, Mr. Daniels said, when the program is looked at as a whole.

"With respect," he said, "the notion of a Medicare surplus is flawed, it's misleading, and it's dangerous."

He said Mr. Bush's standard for fiscal prudence was the Social Security surplus, which he said the administration would protect at all costs, even if that meant vetoing spending bills passed by Congress. The Social Security surplus is projected to be nearly $2.6 trillion over the next decade, Mr. Daniels said, enough to pay off as much of the $3 trillion publicly held national debt as can be redeemed, as a practical matter, between now and 2011 — about $2.1 trillion, by the administration's estimate.

Any effort to redeem more debt, by offering premiums to holders of Treasury bonds, would apportion the government's resources unduly to bondholders at the expense of initiatives, including tax cuts and spending programs, that would benefit more people, Mr. Daniels said.

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