New Directions for the Federal Budget?

The Federal budget reflects much of the history of the nation. Changes both on the revenue side and the spending side highlight 200 years of conflicts and compromises about the economic, political, and social priorities of the country. Within the past half century, moreover, the Federal Government has become one of the major influences on the nation's life. Much of the time, the changes have been evolutionary and gradual. Sometimes, however, as during the depression of the thirties, a compass change is clearly evident. Is the nation now on the threshold of another significant budget shift?

The recent Presidential campaign indicated that both candidates favored a curb on the expansion of the Federal Government and an improvement in its effectiveness. These objectives seemed to reflect the sentiments of a substantial portion of the electorate. The Congress, for its part, has instituted new budget procedures to assert control over spending. Altogether, forces to hold down the size of the budget seem to be at work.

Despite these auguries, the prospects for significant restraints on spending are uncertain. Developments since World War II point the other way: Federal spending has increased more than twelvefold since fiscal 1947. Even after adjusting for inflation, Federal spending is almost three times higher than in 1947. Moreover, the current state of public opinion suggests that there is considerable ambiguity about how conflicting pressures on budget making will be reconciled. While the citizenry seems to favor less government, the national government is increasingly asked to tackle problems that used to be the responsibility of the private sector, or of state and local governments, or that had previously not been viewed as problems. The growth of the economy, which often helped to solve problems in the past, is a less certain solution today for two reasons. One is the question of whether satisfactory levels of economic growth can now be attained as easily as before. The other is the difficulty of making growth compatible with improved practices in regard to the environment.

Whenever the economy operates below capacity, there is bound to be pressure to use stimulative fiscal policy in order to promote greater economic activity and to reduce unemployment. However, spending measures and temporary tax cuts for countercyclical purposes tend to undercut the prospects for curtailing outlays and for permanent tax reductions. At present, the spending problem is accentuated because there are strong pressures to do more about newer concerns with respect to energy, pollution, and health. At the same time, some older concerns, such as the structural problems of high unemployment among teenagers, Vietnam veterans, and workers in urban areas as well as the pressure to relieve poverty, give little sign of abating.

The wish to reduce taxes clearly collides with the demand for new or expanded programs. It is not very likely that this conflict can be resolved by the new Congressional budget techniques and by proposed new procedures, such as sunset laws and zero-base budgeting. Sunset laws automatically terminate existing programs at specified dates; zero-base budgeting requires that spending for existing programs be justified each time an additional appropriation is under consideration. Techniques can only lead to efficient decision making after a consensus on priorities has been reached. Consensus is elusive because well-organized special interest groups can often mount heavy pressures to continue or to expand particular programs. What the new budget procedures *can* do is to pose for the Congress in unavoidable form the central question of economics: how to allocate scarce means—in this case Government revenues—among alternative uses—in this case Government outlays.

Budget processes old and new

As the size of the budget grew, a general dissatisfaction with the Congressional budget process became increasingly evident by the late sixties and seemed to pick up momentum in the seventies when inflation accelerated. In 1969, a *New York Times* story carried the headline "Treasury Secretary Warns of Taxpayers Revolt". A recent Brookings Institution study reported that "Ten years ago, government was widely viewed as an instrument to solve problems; today government itself is widely viewed as the problem".[1] Solutions for the varied fiscal maladies were many, but there was one that cut across political, economic, and social differences—the Congress should get the budget under control. In hearings held on proposals for improving Congressional control over revenues and spending, support for such legislation was widespread and included members of the Congress, business leaders, university professors, and public interest groups. Congressman Al Ullman, chairman of the House Ways and Means Committee, testifying in 1973, said:

> . the clear intent of the Constitution is that the Congress does have the power of the purse, that Congress does levy the tax and determine the expenditures . . . Yet, under the procedures we follow today [1973] we have virtually handed all of this over to the Office of Management and Budget—something not intended by the Constitution

At the same hearing, Roy L. Ash, the incumbent Director of the Office of Management and Budget (OMB), said:

> Congressional actions that affect the budget are taken piecemeal and are uncoordinated for the most part

Until the passage of the Congressional Budget and Impoundment Control Act on July 12, 1974, the budget process in the Congress was fragmented; indeed, there was virtually no satisfactory Congressional control over total Federal spending. In addition, the Congress had no committees charged with consolidating the various pieces of budget legislation into a meaningful whole as they entered the legislative hopper. Nor did it have a staff that could have provided it with such an overview. The new budget control act established a Budget Committee in the House and in the Senate to coordinate budget policy. It also established a Congressional Budget Office (CBO) to provide information and analysis comparable to that which the OMB provides the executive branch. The new structure operated on a preliminary, nonbinding basis during fiscal 1976. The new arrangements became mandatory beginning with the fiscal year 1977 that started on October 1, 1976 and that will run through September 30, 1977.[2]

The 1974 budget act sets up a timetable for the Congressional budget process. This timetable is designed to insure that all appropriation bills for a new fiscal year are completed before a current fiscal year ends. In recent years, it was common for some appropriations to be passed after a new fiscal year had begun—occasionally as long as six months after. The act also requires the Congress to set an appropriate level of Federal receipts and outlays, determine budget priorities, and review any decisions by the President to impound any funds for programs already under way.

The new budget timetable is summarized in the accompanying box. In addition to setting new requirements, the act integrates previously existing executive and Congressional schedules. This integration should enable the Congress to exercise better control over spending and taxation and to assess the impact of the emerging budget on the economy. Under the new procedures, the President still submits his budget at approximately the same time in January as in the past; the present schedule specifies it be done by the fifteenth day after the Congress convenes. The actual budget process, of course, begins well before the President submits his budget, for that document represents the culmination of budget making within the executive branch. A new part of the whole budget process is the requirement laid down by the Congress that the President submit to it a "current services budget" much earlier—by November 10.

The current services budget

The current services budget is meant to provide a bench mark or baseline against which any changes later proposed by the President or by the Congress can be measured. A current services budget is one that estimates Federal tax and spending programs on the assumption that they are continued without any change in policies. These estimates are presented for the current fiscal year and also for the fiscal year ahead. This budget must also take into account the effects of expected changes in economic activity or

[1] H Owen and C C Schultze, eds , *Setting National Priorities, the Next Ten Years* (Washington, D C Brookings Institution, 1976), page 7

[2] Starting with the current fiscal year, fiscal years will run from October 1 through September 30 of the succeeding year Fiscal years are identified by the year in which they end From 1921 through fiscal 1976, the fiscal year of the Federal Government began on July 1 and ended on the following June 30 The shift from fiscal 1976 to the current fiscal year, 1977, left the July 1-September 30, 1976 quarter unattached to any fiscal year, and the period is officially known as "the transition quarter"

of other trends. Examples of such changes are higher or lower levels of unemployment or inflation, variation in the number of social insurance beneficiaries, or variation in the number of recipients under programs that are mandated by existing legislation, such as those for veterans.

In the document submitted to the Congress last November, the Ford administration chose to submit four alternative current services budgets based on four alternative sets of economic assumptions or paths. These alternatives for calendar 1977 projected a gross national product (GNP) ranging from $1,874 billion to $1,905 billion, an unemployment rate ranging from 6.4 percent to 6.9 percent, and an increase in the GNP deflator (a measure of the general inflation rate) ranging from 5 percent to 6.5 percent. Total budget revenues under the four paths varied by almost $20 billion, but total spending varied by only about $6 billion. Under the new budget procedures, the Joint Economic Committee of the Congress (JEC) must evaluate whether the President's current services budget is reasonable. The range of estimates submitted for the fiscal 1977 and 1978 current services budgets was judged to be reasonable by the JEC.

Timetable for budget action

On or before	Action to be completed
November 10	President submits current services budget
Fifteen days after the Congress convenes	President submits official budget
March 15	Committees and joint committees submit reports to budget committees in House and Senate
April 1	CBO submits report to budget committees
April 15	Budget committees report first concurrent resolution on the budget to their respective houses
May 15	Legislative committees report bills and resolutions authorizing new budget authority
May 15	Congress completes action on first concurrent resolution on the budget
Seventh day after Labor Day	Congress completes action on bills and resolutions providing new budget authority and new spending authority
September 15	Congress completes action on second required concurrent resolution on the budget
September 25	If necessary, the Congress completes action on reconciliation bill or resolution, or both, implementing second required concurrent resolution
October 1	New fiscal year begins

The standard appropriation process

Following the usual practice, President Ford presented a budget message in January accompanied by documents that gave a detailed and comprehensive view of Federal spending and receipts. It contained revisions for the current 1977 fiscal year and a proposed budget for the next year, fiscal 1978. The fiscal 1978 document also contained budget projections through fiscal 1982. The revenue and spending estimates for fiscal 1978 and subsequent years, of course, combined the continuance of existing programs, the phasing-out or elimination of other existing programs, and proposed programs for which new legislation would have to be enacted.

The standard procedure has been and continues to be that each new activity of the Federal Government—or the expansion of an old activity—must be authorized by a bill which has been passed by both houses of the Congress and has been signed by the President.[3] Such bills are considered first by the appropriate legislative committee (in both the House of Representatives and the Senate) responsible for the subject the bill addresses. If necessary, the bill includes an *authorization* to appropriate up to a specified amount of money for the program. If the committees approve, the bill is brought to a vote before the full membership of each branch of the Congress. If the bills passed by the two houses differ in any respect, these differences must be resolved by a conference committee composed of members of the two houses. If there is an acceptable resolution, then identical bills are resubmitted for passage in each house and transmitted to the President for signature.

Actual authority to spend funds typically involves a further step—the passage of the *appropriation* bill, again by both houses of the Congress. (The stated amount on the appropriation bill may be no more, but may be less than, the amount in the authorization bill.) The appropriation bill must also be signed by the President. An appropriation specifically permits a Federal agency to order goods and services and to draw funds from the Treasury to pay for these goods and services as well as to meet payrolls up to some stated amount. Other spending may take the form of transfers of funds to state and local governments, to individuals, or to governments abroad and inter-

[3] Some bills, of course, are passed over a Presidential veto, and a few bills have become law without Presidential signature under the Constitutional provision that, if the President does not sign or veto a bill, it becomes law after ten days provided that the Congress is then in session

national agencies.[4]

Spending in any single fiscal year is always made up of a combination of spending from some appropriations carried over from previous years as well as from appropriations newly legislated. For example, the Ford administration's January budget document estimated that $129.2 billion would be spent in fiscal 1978 from the pool of previously authorized appropriations and that an additional $310.7 billion would come from new appropriations for new programs or to continue existing programs.

Since World War II, a practice has developed whereby the President may instruct the Bureau of the Budget (now the OMB) to hold spending for a particular activity below the amounts the Congress had appropriated The Congress has increasingly viewed this practice as an infringement on its Constitutional prerogative to determine the appropriate amount of spending by the Federal Government, and the Congress has now passed legislation to assert its control. If a President wishes to withhold or postpone funding for an existing program, under the new Congressional control system he must send a special message to the Congress. The House and the Senate must approve such a rescission bill within forty-five days if the rescission is to become effective. In contrast, if the President wishes to defer spending temporarily, Congressional approval is not required, but the deferral can be denied if one house passes a resolution against the proposal.

Steps to the first concurrent resolution

Under the new timetable for Congressional action on a proposed budget, the various committees with responsibilities for particular segments of budget legislation must report to the budget committee of their house by March 15. These reports give dollar estimates for the programs in their jurisdictions, for instance, social security, transportation, taxes. At the same time, the CBO and the budget staff in each of the houses are busy analyzing the President's proposals, drafting preliminary budget resolutions, and preparing reports that answer questions on the budget that are posed by various Congressional committees. By April 1, the CBO is required to present to each budget committee a report on alternative budget possibilities with respect to total revenues and expenditures and their major categories, as well as a discussion of national budget priorities. At the same time, each budget committee is preparing a similar budget package By April 15, the budget committee in each house must submit its suggested first concurrent resolution on the budget for the next fiscal year. The committees, of course, take into account the material sent to them by the CBO on April 1.

After April 15, within the guidelines of the proposed first concurrent resolutions—they are really preliminary budgets—the contours of the Congressional budget begin to take on more specific form. Between April 15 and May 15, the first concurrent resolution must be debated and passed by both houses. Any differences between the two must be resolved in conference, and the final conference report must be passed by both houses before May 15 In addition, by May 15 the legislative committees in both houses are required to have reported out all programs requiring authorizations. The first concurrent resolution establishes the target for total receipts and outlays and for the deficit or surplus that the Congress aims to achieve. Moreover, the spending total must be broken down into seventeen major categories

Steps to the second concurrent resolution

After May 15, all the Congressional committees continue to work on the proposals within their jurisdictions. They keep in mind the dollar limits set in the first concurrent resolution and aim to complete action on the necessary individual bills by the seventh day after Labor Day. During this period, a committee might seek to raise its tentative target, which would then create adjustment problems for the total budget. These problems can be resolved in a variety of ways, including the cutting of other spending programs or even by increasing revenues.

Action on the second concurrent resolution must be taken by September 15. This resolution sets final totals on the major categories of revenue and spending. Given the spending total and the revenue total, there should then exist a specific deficit or surplus that the Congress is deliberately identifying as its goal for that budget. This is most noteworthy, since until last year there had been no requirement for such an explicit decision by the Congress The second concurrent resolution changes the spending targets of the first resolution to spending ceilings and the revenue targets to revenue floors.

If the Congress cannot reach agreement by September 15, the legislation provides only a ten-day period for it to iron out its differences. However accomplished, joint agreement on a second concurrent resolution must be achieved no later than September 25. Consequently, when the coming fiscal year begins on October 1, the budget totals for that year are already set. There can still be changes made if the Congress decides that

[4] For ongoing programs, many of which represent long-term national commitments, the appropriations process is somewhat different from the one described above A prominent example is the funding of the social security programs

there is a need for new initiatives or for modification of existing programs after the fiscal year begins. Such changes would require further concurrent resolutions.

Among the more important reforms of the budget act is a built-in antifilibuster device To prevent delays by filibuster in the Congressional budget process, the reform legislation not only sets deadlines for each step, but also sets specific time limits for debate. In the case of the Senate, for example, the law states that "Debate in the Senate on any concurrent resolution on the budget . . . shall be limited to not more than 50 hours. . . ."

Experience with the new process

The effectiveness of the new procedures was illustrated by the way the timetable operated to shape the budget for the current fiscal year. Last May, the first concurrent resolution for fiscal 1977 placed total expenditures at $413.3 billion, some $20 billion higher than the proposed spending total for fiscal 1977 in the budget President Ford presented in January 1976. The larger expenditures proposed by the Congress, according to an analysis by the staff of the House budget committee last spring, would have increased employment by about one million persons more than was implicit in the President's budget. The $413.3 billion total itself represented a compromise between differences that had existed earlier between the House and Senate over the size of the proposed jobs programs. The House had proposed higher outlays, including more spending on public works.

As with the first resolution, the proposed second concurrent resolutions passed by each house were not identical. But the differences this time were relatively minor and easily reconciled A few weeks earlier, however, there had been considerable concern over the substantial divergences between the Senate and the House on the proposed tax legislation. The Senate wanted tax cuts much larger than the House did, not only for fiscal 1977 but also for succeeding years. Eventually, the reconciliation kept revenues, and therefore the deficit, close to the totals that had been set in the first resolution.

The disappointing course of the economy after passage of the second concurrent resolution last fall convinced President Carter by the time he took office that it was prudent to try to stimulate the economy further. He therefore proposed a $31 billion package of tax cuts and job creation programs, mostly for fiscal 1977 and 1978. Consequently, the Congress had to work on a third concurrent resolution incorporating these changes. Once again the versions passed by the House and the Senate differed, for the two bodies augmented President Carter's proposals by different amounts Passage of the third concurrent resolution was achieved on March 3. It added $4.4 billion to spending and reduced expected revenues by $14.8 billion. The estimated deficit for fiscal 1977 was thereby raised to $69.8 billion, $19.3 billion above that of the second concurrent resolution, although the stimulus package itself had not been passed.

Assessment of the new budget controls

Any assessment of the new budget controls must take into account a loophole in the coverage of the budget. Some Governmental agencies, such as the Postal Service and some of the lending agencies, are not included in the budget. Outlays by these agencies were $7.2 billion in fiscal 1976, and the estimate for fiscal 1977 is $10.8 billion [5]

If Congressional control over Federal Government activities is to be comprehensive, these off-budget organizations should be put into the budget. Under current arrangements, the financing of existing off-budget agencies is exempt from the provisions of the Congressional Budget and Impoundment Control Act of 1974, but there is no bar to prevent the Congress from putting them into the budget. Until the off-budget agencies are brought explicitly under budget control procedures, a significant and perhaps widening gap in spending control will remain.[6]

When the new budget control system was adopted, it was viewed with considerable skepticism. Previous attempts to control spending had little impact. The spending ceilings in effect for a few years contained too many exceptions The ceiling on outstanding Treasury debt that is still in existence has proved to be ineffective More significantly perhaps, the new system interposed another layer within the existing Congressional structures. The new budget committees, with their responsibilities to set and to monitor binding ceilings on spending and to implement desired goals for revenues, encroach on the domains of existing committees Political observers wondered whether these

[5] These agencies finance some of their operations from funds obtained by borrowing, chiefly from the Federal Financing Bank (FFB), which in turn obtains its funds from the Treasury Consequently, Treasury borrowing from the public is higher than the amount required to finance the recorded budget deficit

[6] As defined in the budget document, "off-budget entities are federally owned and controlled, but their transactions have been excluded from the budget totals under provision of law" Some agencies are completely off-budget, such as the Pension Benefit Guaranty Corporation Only a portion of the activities of some agencies are off-budget, such as the programs for the housing of the elderly and of the handicapped in the Department of Housing and Urban Development (HUD) Off-budget agencies must be differentiated from Government-sponsored agencies, such as the Federal Home Loan Banks (FHLB) and the Federal National Mortgage Association (FNMA), which are privately owned and operated and therefore completely excluded from the budget These agencies borrow in the capital market by issuing their own debt instruments

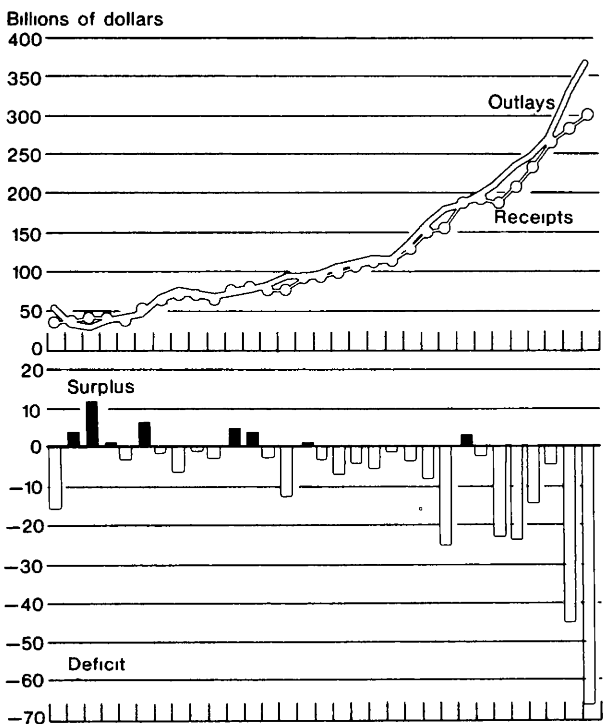
committees would allow their strongly entrenched powers to be eroded. After the first year of operation, however, the consensus was that the new system had been successfully launched Continuing success, nevertheless, is far from a foregone conclusion. A tradition of solid achievement in Congressional budget control must be built to help safeguard the integrity of the new procedures. They should not become empty rituals.

Perspectives on the budget

The bulk of spending under any new budget is based on legislative programs that have been in existence for years, even though in many cases new appropriations are required annually. Any new initiatives on spending and taxation are just the tip of the total budget iceberg. New initiatives, however, are likely to affect future budgets significantly. To understand any new budget, it is therefore helpful to review how it has evolved in size and in composition. Such a perspective can be gained by examining data from two related, though different views of the Federal Government—the view provided by the unified budget and the view provided by the Federal sector of the national income accounts (NIA) [7]

Chart 1

Federal Budget



Source The Budget of the United States Government, 1978

Taking the span of years since World War II, total unified budget Federal receipts and expenditures broadly trace a similar growth trend, although revenues move more erratically. After 1946, revenues typically fell short of spending, there have been only eight years of surpluses. For many years the deficits were generally small—under $5 billion (Chart 1). But beginning with fiscal 1971, deficits in the unified budget—with the exception of two years—were larger than $23 billion, and they reached a historic peak of $66.5 billion in the last fiscal year.

The cumulative deficit for the fiscal years 1947 to 1976 is more than $238 billion, which raised outstanding Federal debt on June 30, 1976 to $620 billion. A sizable portion of this debt, $150 billion, was held by the Government itself. Another sizable portion, $95 billion, was owned by the Federal Reserve System. Privately held net Federal debt has increased from $230 billion in calendar 1946 to $446 billion in 1975. The share of this debt in relation to all outstanding debt in the economy, nevertheless, has dropped from about 50 percent in the late forties to about 15 percent.[8]

Trends in spending

It is convenient to look at Federal spending by the categories used in the NIA. Total NIA Federal spending has increased from $29 5 billion in fiscal 1947 to $373 0 billion in fiscal 1976 All of the broad categories of spending identified in the NIA have grown almost steadily Much of this increase simply reflects the growth of population and the economy, as well as the effects of rising prices. In addition, however, Federal expenditures have been pushed ever higher by the adoption of newly developed programs plus the addition of new functions to previously existing programs

[7] For the purposes of this article, it proved most helpful to discuss Federal Government *spending* using the NIA categories and Federal Government *receipts* using the unified budget categories

The unified budget is the official budget of the United States Government The Federal sector in the NIA is a statistical estimate of Federal Government activities recalculated from budget data to provide a picture of the Federal Government consistent with the accounting system used to estimate total output of the economy—GNP The estimate of total GNP is based on a comprehensive set of data—the NIA—made up of a number of subsectors, such as government, business, and consumers While broadly similar, the unified budget of the Federal Government and the NIA Federal sector differ in agencies covered, in accounting techniques, and in the various descriptive categories into which programs are combined

[8] These debt data, compiled to cover in a consistent accounting framework all debt in the nation by major sector, are available only on a calendar-year basis The latest data are for 1975

Since World War II the Federal Government has grown larger not only in absolute terms but also in relation to other sectors of the economy. The typical test of relative size is to calculate how the Federal Government sector has grown by comparing it with the growth of GNP, the measure of total output of goods and services in the economy. On this basis, the Government sector has grown from 14 percent of GNP in fiscal 1947 to 23 percent in fiscal 1976 This growth has been somewhat erratic: a large upward thrust was associated with the Korean war, another not quite so large was associated with the Vietnam war, and a third was associated with the recent recession (Chart 2).

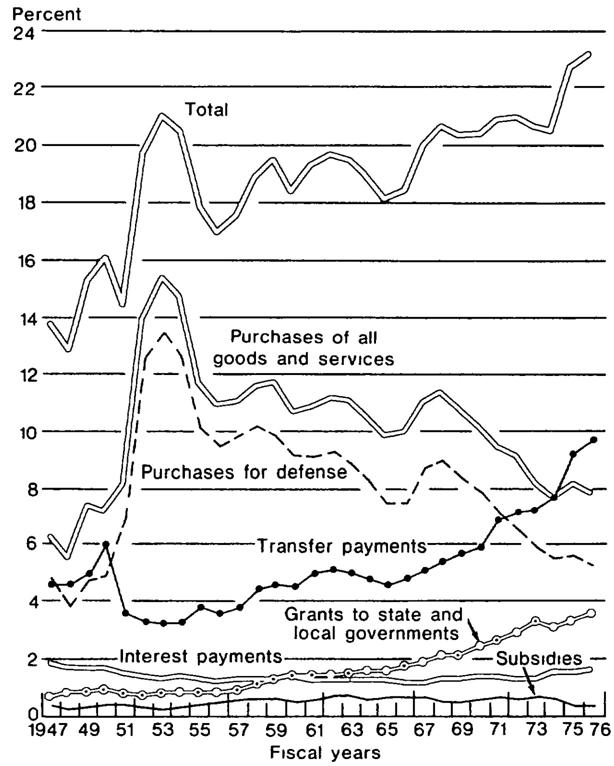
Outlays by sector

Although they have exhibited very different patterns over the years, two components of Federal outlays, spending for goods and services and spending for transfer payments, account for the bulk of outlays. Federal purchases of goods and services increased from $13 billion in fiscal 1947 to $127.2 billion in fiscal 1976. Nevertheless, as a share of GNP these purchases are now only 2 percentage points higher than in 1947. They peaked at more than 15 percent during the Korean war and are currently down in the neighborhood of 8 percent. Defense spending is responsible for this relative decline and now accounts for about two thirds of all Federal purchases, compared with a peak of 87 percent during the Korean war.

Transfer payments, which consist of the various social insurance and the other general welfare and assistance programs, have expanded almost continuously. These payments have increased from $10 billion in fiscal 1947 to $156.7 billion in fiscal 1976, a more than fifteenfold growth. As a percentage of GNP, they have about doubled—from less than 5 percent to almost 10 percent. By fiscal 1975, transfers exceeded total Federal purchases of goods and services and became the largest component among all the NIA Federal spending categories.

There has, of course, been substantial growth of other spending as well. The increase in Federal grants-in-aid to state and local governments, which include revenue-sharing payments, has been important. Grants to state and local governments have climbed from 0 7 percent of GNP in fiscal 1947 to 3.6 percent in fiscal 1976. They now provide more than 20 percent of state and local revenues. Interest payments on Federal debt have registered a sixfold rise in absolute dollar terms, and Federal subsidies have advanced eight fold from the end of fiscal 1946 through fiscal 1976. Still, both have remained relatively small in percentage terms, and together amount to only 2 percent of GNP.

Chart 2
Federal Government Expenditures as a Share of Gross National Product



Federal Government expenditures are based on national income accounts

Sources Economic Report of the President, 1977; The Budget of the United States Government, 1978

Trends in receipts

Despite frequent deficits, Federal receipts tended to increase at almost the same pace as spending until 1970. Most recently, due to the very deep 1973-75 recession, receipts have lagged behind spending by much wider margins than before. Consequently, deficits have widened substantially. Viewed over the long term, all categories of receipts in the unified budget have grown greatly, though some have risen faster than others. There were only temporary interruptions—due sometimes to slowdowns in economic activity, sometimes to changes in tax laws.

The individual income tax has been, and remains, the backbone of Federal Government revenues, accounting for about 45 percent of total receipts every year. Apart from the steady share from the income tax, the composition of Federal revenues has changed markedly since 1946 (Table 1) Starting with a share of less than 8 percent of the total in 1946, employer taxes and individual contributions to social security and related programs now account for almost 31 percent. The jump reflects increases in contribution rates and the tax bases on which contributions are figured, broadened coverage, and the introduction of new types of coverage, such as for hospital bills and disability pay. In all, almost 75 percent of total Federal revenues is now collected from the individual income tax and the social insurance taxes. By contrast, the corporation income tax, which in 1946 constituted more than 31 percent of total revenues, has dropped to about 14 percent, even though its dollar contribution has been growing (Table 2). All other revenue sources now contribute only about 12 percent of the total, compared with 20 percent in 1946, because excise taxes have been reduced or eliminated.

Table 1

Federal Budget Receipts: Distribution by Source

In percent

Description	Fiscal 1946	Fiscal 1968	Fiscal 1972	Fiscal 1976
Individual income taxes	41 0	44 7	45 4	43.9
Corporation income taxes . .	31 1	18 7	15 4	13 8
Social insurance taxes and contributions	7 8	22 5	25 8	30 9
Excise taxes	16 9	9 2	7 4	5.7
Estate and gift taxes	1 7	2 0	2 6	1 7
Customs duties	0 9	1 3	1 6	1.4
Miscellaneous receipts ..	0 5	1 6	1 7	2 7
Total receipts	100 0	100 0	100 0	100 0

Table 2

Federal Government Budget Receipts by Source

In billions of dollars

Description	Fiscal 1946	Fiscal 1968	Fiscal 1972	Fiscal 1976
Individual income taxes	16.1	68.7	94.7	131 6
Corporation income taxes ...	12 2	28 7	32 2	41 4
Social insurance taxes and contributions	3 1	34.6	53 9	92 7
Excise taxes	6.6	14 1	15.5	17 0
Estate and gift taxes	0 7	3 1	5 4	5 2
Customs duties	0 4	2 0	3 3	4 1
Miscellaneous receipts	0 2	2 5	3 6	8 0
Total receipts	39 3	153.7	208 6	300 0

Source The Budget of the United States Government

The government sector in the economy

There is no simple way to assess the impact of the Federal Government sector—or the budget—on the nation's economic system. Federal Government spending as a percentage of GNP provides only the roughest measure of the importance of the Government in the economy. From one point of view, saying that Federal Government spending amounts to 23 percent of GNP overstates its importance. The amount of the total output of goods and services that the Government purchases is down to about 8 percent of GNP As Government purchases as a percentage of GNP have been declining, Government transfer payments to individuals and state and local governments have been rising relative to GNP. Since Federal Government transfer payments do not involve actual Federal purchases of goods and services, it has been said that their inclusion in an evaluation of the Federal sector leads to overstating the Federal Government's role. However, these transfers inevitably alter private spending. Had the Federal Government not received taxes from some people and transferred them to others, a different pattern and level of private spending would have prevailed.

Other budget practices suggest that the budget may well substantially understate the role played by the Federal Government in the economy and in the nation's noneconomic affairs. One understatement of the extent of Government influence results from the size of "tax expenditures". Tax expenditures—or tax subsidies—represent revenue losses arising from special provisions of the Internal Revenue Code (some of them are the "loopholes" about which there is a great deal of popular discussion). These special provisions make the tax liability of an individual or a business firm smaller than it otherwise would have been. Tax expenditures are simply another way by which public policy can attempt to promote particular types of economic activities or moderate undue tax burdens on persons or firms who are seen as facing special circumstances. Estimates of tax expenditures now must be included in the budget by law. The official estimate is that tax expenditures amounted to $95.4 billion in fiscal 1976.[9] Identification of the cost of specific tax expenditures should facilitate the evaluation of whether the benefits to the nation are worth the revenues lost.

Another form of Government influence which is often not recognized is the effect of the Government's credit programs. In fiscal 1976, direct loans outstanding had risen by $14 4 billion to $64.2 billion, and guaranteed

[9] Any estimates of tax expenditures are subject to a wide range of uncertainty because of the technical issues and ambiguities involved in calculating them

or insured loans outstanding rose by $11 3 billion to $169.8 billion. Of course, loans that are guaranteed by the Government do not add to budget outlays unless borrowers default; consequently, these loans represent only a contingent, though large, liability of the Federal Government. In addition, about $10 billion of loans made by off-budget agencies also are excluded from budget spending totals, even though these disbursements increase the amount of Treasury borrowing.

Understatements about the budget also arise from accounting practices The unified budget records certain kinds of receipts not as such, but as offsets to spending. This practice does not affect the size of the surplus or deficit, but it does lower the level of total receipts and total expenditures Offsetting receipts from the public in fiscal 1976 amounted to $13.9 billion, thus reducing outlays from a gross level of $380 4 billion to $366.5 billion and reducing receipts to $300 0 billion, the figures that are cited in the total budget for fiscal 1976.

Finally, in recent years there has been a large increase in the number and in the scope of the regulatory functions of Government. They require relatively small numbers of governmental personnel and relatively small amounts of Federal spending. Nevertheless, these regulatory functions affect a wide range of activities. It sometimes seems as if more discontent with Government is generated from the regulatory and standard-setting functions than is generated from dissatisfaction with the levels of taxation or spending While there are efforts to reduce Government regulation, reasons to introduce new ones seem constantly to arise—right now there is a good deal of pressure to introduce more regulations to protect consumers

Questions of budget policy

Fundamental conflicts with respect to budget policy can be expected to continue for years to come. The charge that Government is too big is commonplace. At the same time there is a strong pressure to raise spending for defense and for health and social needs. There is a similar dichotomy about Government regulation. It is said to be stifling private competition, initiative, or prerogative, but recent calls to reduce regulation have met a mixed response from the industries involved.

Fiscal policy has become more controversial of late For much of the postwar period, the fiscal prescription to combat a recession was simple: cut taxes and increase spending In recent years, however, the persistence of inflation even during recessions has complicated the application of this standard policy prescription Moreover, structural problems of the economy now seem to require policy measures to deal with specific concerns, such as teenage unemployment or the plight of the inner city In brief, reliance on broad fiscal policy to solve national difficulties is being questioned. At the same time, the economy has seemingly become harder to manage This is the context in which the principal budget issues that are likely to be concerning the President, the Congress, and the citizenry at large must be viewed

(1) Tax policy. Federal Government taxes are a perennial center of controversy, with income taxes—individual and corporate—bearing the brunt of the criticism. Broadly viewed, there are three types of complaints rates are too high, the tax structure is too complex, the structure is shot through with too many inequities. While almost everyone favors reform and rate reductions, there is difficulty in reaching a consensus on specific proposals Nevertheless, the time for a fundamental reconstruction of the income tax seems to be coming Former President Ford proposed some revisions in his January budget presentation, and the Carter administration announced that it will send to the Congress this fall recommendations covering both individual and corporate income taxes.

The basic problem underlying any attempted revision of the individual and corporate income taxes is the need to ensure that tax treatment of all forms of income is as uniform and equitable as possible. To do so properly requires a comprehensive approach, since piecemeal reform can give rise to new loopholes or to new forms of unequal treatment.

The merits of a tax reform are generally examined solely on the basis of tax considerations Because government spending ultimately must be paid for by tax collections, a formidable constraint is placed on reforms that would reduce revenues in any major way. Another constraint is that broad-ranging changes in taxes and spending inevitably have important consequences on the overall operation of the economy. Finally, some tax arrangements are specifically designed to implement desired social policies. This results in tax complexity rather than simplicity, as well as favored treatment for selected categories of taxpayers Consequently, the task of actually achieving the general objective of a simple and equitable income tax system has proved elusive—yet in a democracy this objective must continue to be pursued.

(2) Energy shortages and environmental protection. New complexities in budget making have arisen because of the increasing role that the Federal Government is playing in connection with energy and the protection of the environment Legislation to cope with these issues will be a continuing concern of President Carter and his successors and of the Congress. Such legislation can be expected to be a combination of

spending programs, tax changes, special incentives or subsidies, and new regulations. They are likely to have an enduring effect on the budget, and over the long run could materially affect the existing composition of spending and revenues. Even more important, they may well bring marked changes in the structure of the whole economy

The nation's economy, both on the production and the consumption sides, developed on a foundation of cheap energy. The Organization of Petroleum Exporting Countries (OPEC) ended that era, and the resulting higher energy prices have been working their way into the entire price structure. Moreover, the persistent efforts by OPEC to maintain the price relationships between oil and other products that were set immediately after petroleum prices were quadrupled late in 1973, if successful, will tend to exert upward price pressures Standard fiscal measures cannot deal adequately with inflation arising from such unusual developments.

The resolution of the nation's energy problems inevitably involves environmental considerations Damage to the environment from all sources has already been responsible for the adoption of a variety of regulations. These clearly involve money costs Yet lack of environmental regulation can involve social costs that are not so easily perceived. It is now obvious that environmental pollution can no longer be treated with benign neglect In fact, abuse of the environment itself has become a major contributing factor to price and supply pressures, as illustrated by the increasingly expensive search for clean water There is little question that the present generation faces difficult decisions about how the bountiful natural heritage bequeathed to them should be handed on to their successors.

(3) Is government too big? With so many major problems facing the nation, will it continue its practice of shifting problems onto the lap of the Federal Government when all else fails? This results in Government taking on social and economic tasks that might more properly be taken care of by states and localities or by the private sector. Any such misdirection of efforts and resources cannot be fully corrected until the nation's priorities are more thoroughly reassessed and a new consensus forged.

Whatever is done about major priorities, there is at least a potential for better control over Federal spending. The budget control act and its procedures are already in place. And two proposals for further improvements are now being discussed: sunset legislation and zero-base budgeting (ZBB). A bill has already been introduced into the last Congress, the Government Economy and Spending Reform Act of 1976, which combines the sunset and ZBB concepts.

The sunset principle states that all programs must contain a specific and automatic termination date. After that date, it is necessary to reauthorize the program, presumably after searching reexamination. ZBB requires spending programs to be grouped according to objective and then arranged by priority in order to allocate available budget resources among them. Strict application of ZBB requires that spending for each program must be justified each time an appropriation for it is under consideration A fully effective ZBB process should eliminate any need for the sunset principle. Given the relative newness of both concepts and the likelihood of the less than perfect implementation of any set of procedures, sunset laws are probably useful adjuncts to ZBB.

The sunset and ZBB procedures have been used in some state governments, and similar procedures have been in use by business. Stated as general principles, the goals are laudatory; implementation, however, runs the danger of greatly proliferating paper work Expectations for each of these proposals should be tempered by government experience with cost-benefit analysis, a system that was adopted during the Johnson administration but one that was later abandoned in most Federal agencies because of very limited success

Whatever techniques may be used to control Government spending, they cannot solve the basic dilemma of what the proper role and the proper size of the government sector should be in a free democratic society. The question of size does not merely involve the possibility of overwhelming the individual or his initiative. It may also bear on the problem of controlling inflation There is a belief, held particularly widely in Europe, that big government itself can be a major contributor to inflation

In the end, it is the citizenry that will have to come to grips with the issue of what tasks should be allocated to government and what tasks should be allocated to the private sector—business, families, foundations, or voluntary associations. To a substantial extent, the shift to the Government of duties that once were the responsibility of other organizations or the family stems from a perception that certain necessary tasks were not adequately being carried out. To prevent a further diminution of the responsibilities allotted to the private sector, as well as to recapture some that it has lost, will undoubtedly require new private initiatives and innovations. Simply railing at "big government" will not do the trick.

Joseph Scherer