

## THE BUDGETING PROCESS IN THE UNITED STATES

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The Budget of the United States is its plan for governmental activity. It reflects the values and choices of its people through their elected president and chosen representatives. It is also a major instrument in stabilizing and developing its economy. It is an instrument of control over its vast bureaucracy.

According to the method selected for calculation the proposed budget for the United States for Fiscal Year 1968 including trust funds, is between \$169 and 195 billion. In addition, state and local authorities will spend an amount of approximately \$80 billion. The national debt is approximately \$335 billion. The expenditure for the national government alone is about 21% of the estimated gross national product; (in billions of dollars) for all units of government this amounts to almost 1/3. This total is greater than the entire gross national product of every other nation of the world, save only the Soviet Union.

For the national government by sources of revenue, the receipts (in billions of dollars) are as follows: Individual Income Taxes, 73.2; Corporation Income Taxes, 33.9; Employment Taxes (social security) 28.4; Excise, 13.7; Unemployment Insurance, 3.0; Estate and Gift, 3.1; Customs, 2.1; Misc., 10.6.

By functions the expenditures are as follows: National Defense 76.8; International Affairs 5.0; outer Space 5.3; Agriculture 4.1; Natural Resources 3.5; Commerce and Transportation 6.9; Housing and Community Development 1.8; Health, Labor and Welfare 46.6; Education 2.7; Veterans 6.7; Interest 10.2;;\* Other 2.5.

\* Excluding the publicly held portion.

## (II)

In a paper as short as this, it is not possible to trace the history in detail of the budget and accounting processes. The principal Act was the Budget and Accounting Act of 1921. This transferred to the President the initial responsibility for preparing and submitting the budget through a Bureau of the Budget. It established a General Accounting Office responsible to the Congress for auditing and prescribing accounting procedures. In performing this function, both the Treasury and the Bureau of the Budget were to be consulted. Over the years an increasing amount of initiative in this regard was developed upon the Treasury and the operating agencies themselves. This was especially clear in the Act of 1950. This Act provided for an annual «budget message», clarified the G.A.O. authority to set standards of accounting for government corporations, gave the Treasury more clearly defined responsibilities in centralized accounting and procedures in reporting, and centralized the power over the agency budgets in the B.O.B., while decentralizing responsibility to the heads of agencies for their preparation. The 1950 Act also took significant steps in the direction of full disclosure, the linking of unit cost and work loads, and B.O.B. controls over statistical information. In 1956 provisions were added toward simplifying allotments and toward installing accrual accounting programs. In 1958 further incentives toward accrual accounting were added as a tool of management. By 1967 the linking of planning, programming, and budgeting was a major theme, but of this, more later. Surveying the history of the last 50 years, we may generalize trends by saying that they have aimed at strengthening budgeting and accounting as tools of management, making both more intelligible, decentralizing responsibility to the agencies while retaining centralized oversight, and (important in recent years) by executive action using the budget as one of the major instruments in a managed or «Keynesian» economy.

## (III)

The principal institutions concerned are (1) the President, acting largely through the Bureau of the Budget directly responsible to him; (2) the heads of the various departments and agencies

acting through their budget officers; (3) the General Accounting Office, the head of which, the Comptroller General, is appointed by the President with the approval of the Senate, for a fixed 12-year term; (4) the Appropriations Committees of the two Houses of Congress; (5) the Ways and Means Committee of the House and Finance Committee of the Senate. Important roles are also played by the Treasury, the Committees (of Congress) on Government Operations, and certain other Committees of Congress.

All tax legislation requires the consent of both Houses' of Congress. Proposals are often made by the President, but the key role lies with the ways and Means Committee of the House of Representatives.

All expenditures must be preceded by authorizing legislation. Such authorizing bills are substantive in character; and, with rare exceptions, emerge from the standing Committees of Congress; are debated on the floors of the two Houses, passed, and signed by the President. He may or may not have recommended their provisions originally. Such authorizations may be for a fixed period of time, or until repealed. They may set an upper limit or they may authorize «sums necessary» to carry out the purpose of the legislation. For many years the primary emphasis of the G.A.O. in its audits concerned the «legality» of expenditures - that is, had they been «authorized» and formally appropriated?

Subject to such authorization, proposals for expenditure follow a course with the following major steps:

1 — Estimates prepared in the departments and agencies and submitted to the B.O.B. (by October 1).

2 — Defense of these estimates before the B.O.B., negotiations, reexamination, and (at times) appeals to the President in case of dispute.

3 — Determination of the Budget by the B.O.B. and transmission to the President.

4 — Adoption, with or without alterations, by President.

5 — Submission to Congress in the Budget Message (mid-January).

6 — Hearings before the two Appropriations Committees, the House acting first in «marking up» and reporting out the various appropriation bills (February-August).

7 — Passages of Appropriations Bills by the two Houses, after reporting out by the two Committees, and floor amendments. (Note that *separate* bills are considered for each major agency or groups of agencies.)

8 — Reconciliation of differences between House and Senate versions in conferences, with final passage by both Houses.

9 — Signature by the President (June-September). (deficiency or supplemental Bills usually follow early in the next Session (Jan.-May).

10 — Continuous subsequent audit by the G.A.O., with reports to the Government Operations Committees of Congress as to illegalities, or ways to improve procedures and controls.

#### (IV)

In the broader fiscal aspects of the budget, including the management of the debt, the President relies heavily on the counsel of such officials as the Secretary of the Treasury, his Council of Economic Advisers, the Chairman of the Federal Reserve Board, as well as the Director of the Budget. Goals which are not always simultaneously attainable are: full employment, stable prices, adequate revenues, low interest on the national debt, ready availability of funds for capital investment, maintenance of an adequate gold supply, cooperation in international monetary policy, and international economic growth. Budgetary instruments in orchestrating such economic planning include selection of taxes for reduction or increase; subsidies to lagging sectors of industry; size of deficit or surplus in current accounts; decisions as to capital expenditure; sales of governmental assets; debt management. Economic developments (both regional and national), levels of employment, returns on capital, and relations between wages and prices, all are affected.

Relating the budget to the economy of the nation as a whole is the most spectacular of all the recent developments. Keynesian

economics have been the most influential single factor, but greater and greater degrees of sophistication are annually revealed. Perhaps the best evidence of this lies in the fact that the nation has had no serious economic recession for almost thirty years. There have been variations in the speed with which the gross national product has increased, but rarely has there been even a minor setback.

For example, it was recently apparent (1966) that an expansion in physical plant was taking place beyond the capacity of the existing labor force to staff it, with inflationary results. The temporary suspension of an investment tax credit of 7% was accordingly authorized, a credit originally instituted to stimulate modernization. By 1967 it was apparent that the economy had somewhat over-reacted. The pace of growth and price increases slackened, interest rates fell, and (most important in this connection) the construction industry was in danger of a serious setback. Consequently President Johnson has recommended a restoration of the 7% tax credit, and already (May 1967) there are clear signs of the anticipated effectiveness of such a move. A small deficit in current accounts is now usually budgeted so as to continue the economic growth stimulated by consumer demand. Other illustrations might be given to indicate that a far more sophisticated approach than the single objective of a «balanced budget» is now firmly established in the executive branch.

(V)

At this point certain descriptive comments on the budget as a whole are in order.

A substantial part of expenditure under the budget is not subject to any real control. For example, interest on the national debt is now about \$ 14 billion, including the publicly held portion. Other considerable items are grants to states and localities which are in accordance with formulas fixed by law. Only a change in the laws themselves would bring a reduction. So also are many pension rates (veterans, the aged, and others) fixed by law. Agricultural subsidies follow a legal formula, which depends to some extent on world as well as domestic prices. In all, perhaps \$ 30 billion is relatively uncontrollable, because it is subject to forces outside the

government or requires legislation to alter the amount. In addition to this, \$ 75.5 billion comes under the heading of national defense and introduces serious non-budgetary considerations. Perhaps \$ 15 - 20 billion under other headings may be classified as relatively controllable.

About 50 billion dollars annually is in the so-called «trust funds». \$ 37 billion of this is received and for the most part paid out in the various social insurances—old age, unemployment, medical care for the aged. Almost \$ 4 billion is received from gasoline taxes and paid out for highway construction. Over \$ 1 billion each involve agriculture, military assistance, housing and community development. These, too, fall almost entirely outside normal budgetary control.

Government corporations are more or less autonomus, largely self-supporting, and subject to accounting practices less rigid than other governmental agencies. In general, the corporation device does not differ materially from that used in other nations desiring a more flexible and adaptable instrument than the usual government department or ministry affords. However, the G.A.O. retains power of audit and approval of the accounting practices.

## (VI)

Attention should be called to the extent that separation of powers (especially the independent position of Congress) introduces additional and often complicating steps in the budgetary process. There is no way of determining the extent to which the detailed review by Congress in fact results in greater economies than would be provided by internal controls in the bureaucracy itself. Customarily Congress does make some substantial cuts, some of which may fade when the time comes for the supplemental appropriation bills. Others are delays in the timing of expenditure. On the side of taxation and revenue, Congress is often determinative, and its estimates of receipts have often been more accurate than those of the Treasury. In any event, the American President normally must work harder to convince the legislature of the correctness of budget estimates than the prime minister of any parliamentary government.

The role of Congress is probably unique among national legislative bodies, especially as regards expenditure. Its role thus deserves close examination. For appropriation purposes, the Appropriations Committee of each House is divided into a number of subcommittees, each entrusted with scrutiny of the estimates of certain related agencies and departments. It is in these subcommittees that most of the real work is done. Members and staff spend many hours and days in preliminary examination. This is followed by «hearings» in which representatives of the agencies present their estimates and defend them under close cross-questioning by subcommittee members. There is continuity from year to year in that the members and staffs know in which agency officials they can have confidence, and which functions are effectively administered. Also chief attention is paid to new items or changes from the preceding year. «Leaks» from within agencies, questions, tips, or grudges from outside or within, often lie behind particular questions. There is a constant probing to determine the agency's own views as to priorities, especially if there are unusual considerations calling for civilian economy.

How much is really cut from the estimates? The more cynical would claim that the agencies customarily ask for more than they expect, so as to give Congress the opportunity it seeks to make a show of economy. In connection with construction projects, some of the economy is a «slowing down» of the rate of expenditure, on the assumption, perhaps valid, that this will delay requests for new projects. Some economy is in the nature of registering disfavor with a particular policy or its administration. It should be borne in mind that the alternative of a change in the authorizing legislation is subject to a presidential veto, whereas appropriation cuts, for practical purposes, can be imposed by a majority vote in each of the Houses. Some ostensible reductions are made in the fixed obligations of the government noted above, with the stipulation that, if the appropriation proves inadequate, the agency may request supplemental funds. Some economies are real and highly intelligent. For example, Marshall Plan aid for construction was once cut over \$100,000,000, on the basis of a decline of 7% in construction costs in Western Europe. The House will often cut a doubtful item quite deeply, and allow the Senate to act as a kind of board of review. The full Committee of the House will often set an over-

all target, and also from time to time direct each of its subcommittees to scrutinize the same year some aspect (e.g., personnel, office costs, transportation) common to most or all agencies.

The «performance budget» (noted later) is freely utilized for year by year comparisons.

The Committees are at heart non-partisan. The localities of the individual members are occasionally favored unduly, but this is not too serious.

Perhaps the best generalization one could make is to say that in a given year genuine and lasting economies in the over-all budget amount to between 1% and 2% of the total. In the portion of the budget which is realistically the subject of annual discretion, this percentage is perhaps doubled.

Once the subcommittees and committees have «marked up» the bills, they are then subject to floor amendment. Occasionally amendments these pass one House, less frequently both Houses. In the former instances, they may or may not survive the joint conference committees.

In general, the Congressional approach is piecemeal. Attempts at an over-all legislative budget, or simultaneous consideration of total revenues and expenditures have proved abortive, and are probably not practicable without some basic changes in the budgetary timetables and precedures.

## (VII)

In a national budget which not only finances the program of the government, but involves sums money such that it affects the whole economy, major problems are bound to arise.

In the first place, how shall expenditures be presented? Considerations that make for detailed control of a budget may not be the best for its understanding. Of the various ways in which the budget might reasonably be presented, each has certain merits. In the end, the President has chosen to include all important ways in his budget message.



From the standpoint of law, the important objective is to appropriate and allocate amounts of money for unit and/ or function. However, substantial amounts so appropriated necessarily carry over into or more of the years that follow. About \$ 25 billion in the 1968 budget it is expected will be spent later than the year in which appropriated. Correspondingly substantial funds are available in this so-called «administrative» budget from earlier years. The administrative budget does not include the trust funds.

A budget presented in terms of total cash flow has certain advantages - notably that of reflecting all the anticipated financial transactions in the given year.

For the first time, the Budget of 1968 has given chief emphasis to a presentation in terms of «national income». This is most useful in analyzing the impact on the economy as a whole. Unlike the «cash flow» budget it excludes loans and repayments, and sales to participants of federal assets. It includes federal retirement programs. It records receipts as at the time of liability.

Basing fiscal policy on the administrative budget is likely to be too restrictive and unlikely to conform to Keynesian theory. Moreover, the other two methods lend themselves better to accrual accounting.

The fourth and fifth types are directed toward popular understanding.

The fourth method is by function - health, national defense, agriculture, transportation, etc., - without reference to the specific agency performing the function. Several special groupings are added, to the basic classifications. For example, there is also a table indicating all the expenditures benefitting primarily the poor.

The fifth type is a sophisticated form of distinguishing between capital and current expenditures. Without going in to all the detailed headings it separates the following amounts from current expenditure: (1967 Appendix; 1968 not yet available)

Net additions to assets:	Civil	approx.	\$ 8 billion
	Defense	approx.	\$18 billion
Development expenditures (e.g. health, education)	Civil	approx.	\$12 1/2 billion
	Defense	approx.	\$ 8 billion

Clearly there are values in each of the five foregoing systemes, and something would be lost if any one were omitted.

However, in no sense does this require that all five be reflected in the details of an accounting system. In selecting such a system other problems arise. Clearly accounting must reflect legality, and in this sense it should correspond to the administrative budget. Clearly also it should serve as an instrument of control. The best thought in the profession is that «accrual» accounting coupled with annual limitations on expenditures serves best this objective. It must naturally include the authority to contract for one or more years in advance. Accrual accounting results in the assignment of resources used in a given period. It recognizes the receipt of goods and services and consumption or use of resources, and can reflect assets and liabilities. It can be integrated with both controls and obligations, and consequently can enforce legality as well as prudence.

As yet the Appropriations Committee of the House of Representatives has been unwilling to accept limitations on annual expenditure as a substitution for authorized fixed sums appropriated. Hence accrual accounting, while spreading throughout the Federal government, has not yet reached its full possibilities. As a matter of fact, both the General Accounting Office, the Treasury, and the Bureau of the Budget have encouraged the individual agencies to work out systems best suited to their respective needs, subject only to controls as to legality of the individual items and to the need for conformity to certain general principles. Any system must ultimately be approved by the G.A.O.

Commencing in 1950 the agencies under B.O.B. pressure introduced what has come to be known as the «performance budget». Estimates were submitted wherever possible which would indicate work load and unit costs. More recently a much more sophisticated development has taken place - the so-called «planning - programming - budgeting» process. The original emphasis in the «performance budget» was to make possible year to year, and agency with agency, comparisons. The new emphasis, in its three stages of planning, programming, and budgeting, forces a much more thoughtful consideration, for example, of alternative methods of performing a function as well as careful thought to each step

in the operation. This is producing - or requiring - a new type of budget officer or senior accountant, one who has a disciplined imagination.

More and more, computers and data processing are utilized in the budgetary process, linked with program and performance. Their most spectacular use has been in the Department of Defense, where various «weapons systems» are analyzed as to «cost effectiveness» both prior to adoption and (later) in the light of alternatives. The technology of management is thus a tool for budgeting as well as for operations.

We may summarize these trends in budgeting and accounting as trends in the direction of better controls, but even more as instruments of creative planning and management. At the same time there is a flexibility which permits a large measure of decentralization and adaptability. For Congress and the general public there is a conscious effort to make the budget estimates more understandable. Moreover, planning and management include not only the specific agency but also the economy as a whole.

Two final problems must be mentioned - as yet relatively unsolved. These are the problem of forcing economy when circumstances change within the duration of the appropriation cycle; and, secondly, the alteration of tax rates to meet an unexpected change in the economy as a whole.

For the first, it has been suggested that the President be given an «item veto». In other words he would be allowed to veto certain items in a Bill without vetoing the entire bill. Several state governors have this power, and have used it in instances in which in their opinion the legislatures have been either extravagant or unwise. Congress has been unwilling to grant this power to the President on the ground that it would weaken its responsibility under the Constitution. However, it has refused to force a President subsequently to spend all appropriated funds; though presumably, if the latter made too great use of this discretion, Congress would not be so tolerant. Here the matter stands at present.

A similar reluctance on the part of Congress has attended attempts to give legislative authority to Presidents to alter tax rates even temporarily and within carefully prescribed limits

and subject to conditions defined in the Law. While not yet granted, such authority is the logical outcome of the Keynesian economics presently in vogue in the United fiscal policy.

In conclusion, budgeting and accounting are clearly becoming increasingly effective tools in the management of big government and big economy. We may expect further progress in the light of experience.

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