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Three Aspects of Federal Budget Making

THE ANNUAL TRANSMITTAL to Congress of the Budget Message always raises the question of which type of budget best serves the purposes of fiscal decision-making.

The administrative or traditional budget contains estimates, for the ensuing and current fiscal years, of receipts and disbursements of Federally-owned funds. By various means of authorization, Congress is asked to grant an amount of *new obligational authority,* which does not coincide with expenditures for a particular year.

To estimate the impact of fiscal operations on the economy, it is necessary to combine budget and trust fund transactions in a consolidated cash statement. The "cash" budget yields information on money flows between the Federal Government and the public and furnishes the basis for short-run estimates of the effect of fiscal operations on bank reserves.

A "capital" budget, not used by the Federal Government, would distinguish between "capital" and "current" outlays. Opponents of such a budget consider it a way of concealing chronically unbalanced budgets; proponents advance it as a means to public acceptance of large and necessary outlays by the Federal Government on durable goods.

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Federal Reserve Bank of St. Louis

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IN THE MIDST OF HIS ANNUAL BOUT with the Federal taxgatherer, a citizen may be forgiven for putting aside the broader aspects of Federal fiscal problems. Yet current discussions of such matters intrude themselves upon his consciousness. The Federal Budget for 1956, after nearly a year in process of formulation, was sent by the President to Congress on January 17 of this year. Since then the general press and the financial journals have treated at length such subject as the effects of the proposed expenditures on different Government programs, the effect of a continuing budget deficit on the performance of the economy, and the prospects for a balanced budget in ensuing years.

Another, perhaps more fundamental, question has elicited a flurry of journalistic comment. Economists, Government officials, and economic research organizations have argued that a "cash-consolidated" budget gives a more accurate picture of the impact of fiscal operations on the economy than does the "administrative" budget in present use. Others have suggested that a system of "capital" accounting be incorporated in a cash budget to permit separation of items of current expense from asset acquisitions. The average citizen finds it difficult enough to make his way through the present administrative budget, which is presented to him in a volume about the size of the St. Louis telephone directory. When he contemplates the complexities suggested by other types of budgets he is likely to despair of comprehending his Government's financial operations. A solution to his intellectual difficulties lies in the realization that different types of budgets yield information useful for different purposes of decision-making.

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To understand the various proposals for presenting budgetary information it is first necessary to become familiar with the elements of the conventional or administrative budget. By the Budget and Accounting Act of 1921, as amended, the President is required to present to Congress in January of each year an estimate of government revenues and expenditures for the ensuing fiscal year, a revised estimate for the current fiscal year, and an accounting of receipts and expenditures for the fiscal year which ended on the preceding June 30.

On the receipts side of the budget are included funds owned directly by the Government and paid into the Treasury to the credit of the general and special funds. Excluded from budget receipts are money obtained by borrowing, money paid into revolving funds such as those of Government corporations and the Post Office, and money earmarked for one of the

trust funds. In general, then, budget receipts consist of the income taxes, excise taxes, and custom duties which people and businesses pay into the United States Treasury.

TABLE I

SUMMARY OF THE BUDGET
(Fiscal years. In billions)

	1953 actual	1954 actual	1955 estimate	1956 estimate
New obligational authority:				
Under existing legislation	$ 80.3	$ 62.8	$ 57.2	$ 53.1
Under proposed legislation			.1	5.5
Total new obligational authority	80.3	62.8	57.3	58.6
Budget receipts:				
Under existing legislation	64.8	64.7	58.8	57.7
Under proposed legislation			.2	2.3
Total budget receipts	64.8	64.7	59.0	60.0
Net budget expenditures:				
Under existing legislation	74.3	67.8	63.5	60.5
Under proposed legislation				1.9
Net budget expenditures	74.3	67.8	63.5	62.4
Budget deficit	9.4	3.1	4.5	2.4
Public debt at end of year	266.1	271.3	274.3	276.0
Balances of appropriations carried forward at end of year	78.4	68.0	53.9	49.6

Budget expenditures are outlays of Federally-owned funds on the national security program, interest on the public debt, Federal services and benefits, agriculture and agricultural resources, and so on. Expenditures of the general fund are stated on a *gross basis,* receipts not ordinarily being deducted from expenditures. Expenditures of the so-called "public-enterprise" revolving funds are reported on both a *gross* and a *net* basis, but in the main budget statement receipts are deducted from expenditures to get a net figure. For example, it is estimated that gross expenditures for agriculture and agricultural resources in the fiscal year 1956 will be $7.6 billion. But receipts, consisting mostly of collections on loans and sales of commodities, will amount to about $5.4 billion. Thus, the net estimated expenditures for the programs will be about $2.2 billion.[1] Net budget expenditures are estimated on a "checks issued" basis—i.e., the date of a check or cash payment determines the fiscal year in which the expenditure falls. However, interest on the public debt counts as an expenditure in the year in which it becomes payable even though the coupons (or savings bonds) may not be presented for payment in that year. Retirement of Government debt and investment in United States Government securities by Government corporations are always excluded from expenditures. Certain payments from one Government fund to another are eliminated from both the receipt and expenditure side.

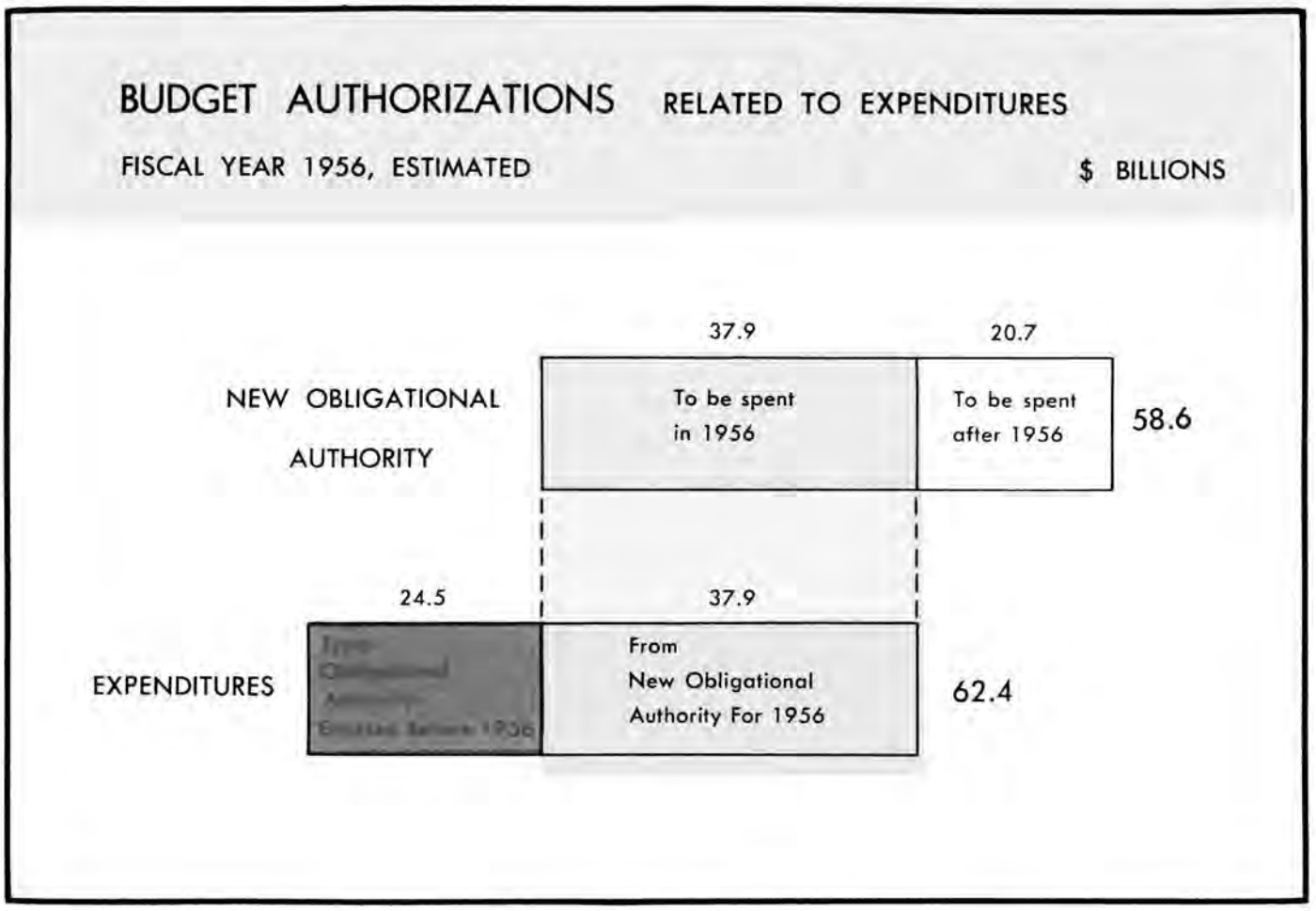
By various means of authorization, Congress is asked to grant an amount . . .

Federal agencies cannot commit themselves to expenditures or pay bills until Congress authorizes them to do so. Usually authorization takes the form of an *appropriation,* which permits an agency to incur obligations and pay bills as they come in. Sometimes, though, Congress will grant a *contract authorization,* which gives authority to incur obligations but not to spend money; such an authorization requires a subsequent *appropriation to liquidate contract authorization* to allow the actual expenditure of funds. Occasionally *reappropriations* and *reauthorizations* are necessary to continue available balances of prior appropriations or authorizations which would otherwise expire, though for a few purposes, such as interest on the public debt, Congress grants permanent authorizations under which sums become available year after year without further legislative action. Finally, *authorizations to expend from debt receipts* may be necessary to make borrowed funds available to an agency or to enable a Government-owned corporation to borrow directly from the public.

. . . of new obligational authority, which does not coincide with expenditures for a particular year.

Whatever form Congress may use, the sum of the various types of authorization, less the part of appropriations which is to liquidate previous contract authorization, constitutes *new obligational authority.* The amount of new obligational authority granted will not be the same as expenditures for a particular year. There will ordinarily be a time lag between authorization and the receipt of goods and services, and in the case of such capital goods as an atomic energy installation or an aircraft carrier the interval between incurring an obligation and making final payment may be several years. Thus it happens that expenditures in any year come partly from new obligational authority granted for that year and partly from authority granted in previous years. For example, in fiscal 1956 about 40 per cent of the estimated expenditures of $62.4 billion will be from obligational authority granted in previous fiscal years, and about 60 per cent of the expenditures are to be from authorizations requested for 1956. Finally, it is anticipated that $20.8 billion, or about one-third, of the

1 On a gross basis budget expenditures for 1956 will be $73.3 billion, but after receipts of Government corporations and the postal service of about $10.9 billion are deducted, net expenditures amount to $62.4 billion.



new obligational authority will not be spent until fiscal 1957 or later. The above chart will help the reader to get these relationships in mind.

In periods when Congress is making huge appropriations for the purpose of building up the military machine, new obligational authority in any year may greatly exceed budget expenditures. Table II shows how the conflict in Korea affected unexpended balances of appropriations in the early 1950's.

In fiscal 1955 and 1956 payments for military equipment authorized in previous years will exceed the dollar value of new equipment ordered, with the result that cumulative unspent balances of appropriations will decline. By July 1, 1956, these balances will be down nearly $30 billion from their peak at the end of fiscal 1953.

The administrative budget thus provides a means for closely estimating receipts and expenditures of Government-owned funds in any year and for keeping track of congressional authorizations over time. The primary function of the traditional budgetary statements is to furnish a system of easy accounting controls to prevent overspending of appropriations.

TABLE II

BUDGET AUTHORIZATIONS, EXPENDITURES, AND UNSPENT APPROPRIATIONS 1950-1956
(In Billions of Dollars)

Fiscal Year	New obligational authority*	Expenditures	Amount brought forward into the year	Cumulative unspent balances of appropriations**
1950	49.3	39.6	11.5	14.1 e
1951	82.9	44.0	14.1	50.3 e
1952	91.4	65.4	50.3	68.8
1953	80.3	74.3	68.8	78.4
1954	62.8	67.8	78.4	68.0
1955 e	57.3	63.5	68.0	53.9
1956 e	58.6	62.4	53.9	49.6

e Estimated

* Included authorizations to contract and to make expenditures from borrowed money, as well as appropriations to make expenditures from the general revenues of the Government.

** Includes reappropriations of spending authority which would lapse if not used in a given fiscal year, as well as continuing and new appropriations. Does not include authorizations to contract or spend from borrowed money.

Source: *The Budget of the United States Government for the Fiscal Year Ending June 30, 1956.*

To estimate the impact of fiscal operations on the economy, it is necessary to combine budget and trust fund transactions in a consolidated cash statement.

The administrative budget does not, however, permit an accurate measurement of the impact of fiscal operations on the economy. In order to have some notion of what that impact may be within a particular year it is essential to have an estimate of the total amount of money which will be collected from people in taxes and the total amount which will be turned back as cash expenditures. The orthodox budget does not accurately describe cash flows to and from the public, for it does not include receipts and expenditures of the trust funds, such as old-age and survivors insurance, unemployment insurance, railroad retirement, and the like. Moreover, the customary budget counts as expenditures certain payments which do not find their way into the hands of the public. Chief items in this category are interest on the Government securities in which the trust funds are invested and accrued interest on savings bonds, which is counted as a budget expenditure at the time of accrual. In Special Analysis A of the budget document is found a summary of Federal Government receipts from and payments to the public, here presented in somewhat simplified form as Table III. The Federal Government includes budget transactions, trust fund transactions, and the transactions of those Government corporations carried on the books of the Treasury. The public includes household units, business firms, the Federal Reserve and Postal Savings Systems, state and municipal governments, and international organizations.

TABLE III

RECEIPTS FROM AND PAYMENTS TO THE PUBLIC

(In Millions of Dollars)

Description	Fiscal Year 1955 Estimated
Budget receipts	$60,000
Trust fund receipts	11,283
Intragovernmental transactions	– 2,455
Seigniorage on silver	– 35
Total receipts from the public	$68,793
Budget expenditures	$62,408
Trust fund expenditures	8,845
Intragovernmental transactions	– 2,455
Net accrued interest and other noncash transactions	– 563
Total payments to the public	$68,235
Excess of receipts over payments	$ 558

Source: *The Budget for the Fiscal Year 1956, p. 1131.*

The "cash" budget yields information on money flows between the Federal Government and the public, . . .

Consolidation of budget receipts and expenditures with trust fund transactions yields helpful information. In fiscal 1956 receipts of the trust funds will be about $2.5 billion more than expenditures from them; the excess cash will be invested in Treasury securities, payment to the public of these trust fund expenditures is postponed, and the excess cash received from the public by the trust accounts is available to the Government. Of the transactions between Government agencies and trust funds, interest paid on United States securities held by trust funds amounted to about $1.7 billion.[2] Of the noncash transactions, accrued interest on savings bonds will amount to more than $500 million in fiscal 1956. This amount plus the $2.5 billion excess of cash receipts in the trust funds changes a $2.4 billion deficit in the administrative budget to a $500 million surplus when only the money flows between the Federal Government and the public are considered.

If present estimates hold, the impact of Federal taxing and spending in fiscal 1956 will be almost neutral. No one would pretend, of course, that the cash deficit or cash surplus is the only thing to be considered in assessing the effect of the budget on the economy. The kinds of taxes levied play a part in determining the level of economic activity, and the debt managers, by tapping alternative sources of borrowed funds, may encourage or discourage business expansion. As the budget document itself points out, ". . . not only cash flows, but also many other Federal financial activities have important economic effects." For example, a large increase in new appropriations will likely stimulate economic activity before the funds themselves are actually paid out. The repeal or modification of a tax law may affect business decisions to invest or disinvest before cash flows between the Federal Government and the public have been influenced.

. . . and furnishes the basis for short-run estimates of the effect of fiscal operations on bank reserves.

Incidentally, familiarity with the consolidated cash statement as presented in the budget document is of help in day-to-day monetary analysis. Treasury operations have an important effect on the reserves of

[2] Presently United States Government securities held by the trust funds amount to about $50 billion, or close to one-fifth of the public debt.

commercial banks as may been seen from an inspection of Table IV. In the first two business days of 1955, for example, changes in Treasury deposits in the Federal Reserve banks added $177 million and $103 million to bank reserves.

TABLE IV

FACTORS AFFECTING MEMBER BANK RESERVES

(Sign indicates effect on member bank reserves)

(In Millions of Dollars)

	January 3, 1955	January 4, 1955
Treasury Federal Reserve Deposits	+177	+103
Currency	— 2	+ 39
Gold and Foreign Federal Reserve Deposits	— 21	— 17
Federal Reserve Bank Credit	+355	+ 4
Other Factors	+ 35	— 7
Change in Member Bank Reserves	+544	+122

Additions to, or subtractions from, bank reserves by the Treasury are the net result of a complex of transactions. The *Daily Statement of the United States Treasury* presents in a table of "Cash Deposits and Withdrawals" a consolidated cash statement of Treasury operating transactions.[3] The Treasury cash statement is a convenient way of grouping Treasury transactions so as to show their effect on member bank reserves (see Table V.)

TABLE V

SOURCES AND USES OF TREASURY FEDERAL RESERVE DEPOSITS

(Signs indicate effect on member bank reserves)

(In Millions of Dollars)

	January 3, 1955	January 4, 1955
Individual income taxes	— 33	— 99
Corporate income taxes	— 2	— 11
Other cash receipts	— 31	— 62
Total deposits	— 66	—172
Defense Department expenditures	+199	+265
Foreign aid programs	+ 14	— 2
Other cash expenditures	— 17	+102
Total withdrawals	+196	+365
Net withdrawals	+130	+193
Net cash borrowing	— 25	— 6
Change in other cash balances	+ 72	— 84
Treasury Federal Reserve Deposits	+177	+103

Cash income of the Treasury reduces commercial bank reserves, for individuals and business firms draw checks on their accounts to make tax remittances or other payments. But the Treasury may deposit funds in its Federal Reserve account, from which nearly all withdrawals are finally made, or it may temporarily leave funds in the Tax and Loan accounts of commercial banks.[4] Insofar as tax receipts are left in Tax and Loan accounts there is no immediate effect on bank reserves, and in Table V an adjustment for Tax and Loan account changes is made under the heading "Change in Other Cash Balances." And, of course, net cash borrowing (or repayment) affects bank reserves. Treasury cash withdrawals from its Federal Reserve deposits normally go into private accounts in commercial banks and thus add to bank reserves.

A "capital" budget, not used by the Federal Government, would distinguish between "capital" and "current" outlays.

Traditionally, Americans have applied one principle of private financial practice to governmental budgets and rejected another. They have felt that the budget should be balanced within the annual accounting period, that outgo should not exceed income. Yet, except in the budgets of certain municipalities, no distinction has been made between "capital" and "current" outlays.[5]

Capital goods, whether those of a business firm or a household, are ordinarily defined as goods which yield their service flows over a period of time longer than the annual accounting period. A manufacturing firm does not charge off the whole cost of a new plant in one year, nor does a family consider the purchase of a house as a drain on a single year's income. But under present Federal practice all expenditures, whether on plant and equipment which may last for decades or on the current pay of soldiers and sailors, are financed in the same way.

For a half century or more writers in public finance have discussed the pros and cons of adapting a capital budget to governmental accounting. Both Denmark and Sweden have adopted budgetary systems which distinguish between the operating budget and the capital, or investment, budget, and other countries, notably Canada, have separated the "ordinary" from the "extraordinary" budget. Under a system of capital accounting, durable goods may be entered in the

[3] Although figures for Treasury cash deposits and withdrawals differ somewhat from Federal receipts from and payments to the public, the differences are small (about 1/10 of 1 per cent) and can for many purposes be neglected. For a reconciliation of the two statements see *The Budget for Fiscal Year 1956*, p. 1132.

[4] In fact, the purpose of Tax and Loan accounts is to cushion the withdrawal of bank reserves as a consequence of tax and other payments. The Treasury closely gears its withdrawals from the Tax and Loan accounts to its expenditures.

[5] Special Analysis D distinguishes between investment and operating expenditures but is not intended to be a capital budget. See *The Budget for the Fiscal Year 1956*, p. 1153-1164.

capital budget whether the expenditures are self-liquidating or non-income-yielding, or the capital budget may contain only remunerative enterprises. Whichever system is adopted, the original cost of the durable goods is met by borrowing, by transfer of amortization or depreciation allowances from the operating to the capital budget, or by receipts from inheritance or gift taxes. It is essential to the notion of a capital budget that losses on income-earning projects, after depreciation and interest charges as well as operating expenses, be carried by the operating budget. Similarly, nonincome earning assets, such as schools, parks, or roads must be a charge against the operating budget to the extent of interest and depreciation charges plus operating expenses.

Continuing international tensions, a rapidly growing population, and increasing urban congestion have brought demands for vast capital outlays which in turn have suggested the separation in the Federal budget of asset purchases from current expenditures. About two-thirds of Federal spending today is for the national security program. The reasons for quickly increasing the rate of school-and-road-building are compelling. The question arises whether in the interest of efficient allocation of resources a new type of budgetary procedure should not be adopted.

Opponents of such a budget consider it a way of concealing chronically unbalanced budgets; . . .

Opposition to a system of capital accounting at the Federal level has historically been based on a number of grounds. Some writers have insisted that the borderline between "capital" and "current" outlays is too fuzzy to permit a useful distinction between the two types. Others have contended that a multiple budget makes, at best, for an "incomplete budget and, at worst, for an evasion of fiscal responsibility by concealing chronically unbalanced budgets. And students of the problem, unconvinced by either of these objections, have remarked that private businesses distinguish capital outlays from others because capital expenditures are ordinarily financed by the issue of securities, whereas government borrowing should largely be determined by current levels of income and employment.

. . . proponents advance it as a means to public acceptance of large and necessary outlays by the Federal Government on durable goods.

Proponents of capital budgets rejoin that a projection of outlays over several years is necessary to intelligent decision-making concerning the allocation of the tax dollar. They point out, moreover, that the pressure for financing by direct borrowing of the responsible agencies will grow.[6] Public acceptance of elaborate schemes for building roads and school buildings may well depend, they insist, upon provision for the amortization of necessary outlays over a carefully estimated period of useful life and the inclusion of interest and depreciation charges in a meaningful operating budget.

The three budget types are not alternative, but rather supplementary, control mechanisms to aid in the management of Governmental affairs.

Presently the three budget types just described should not be viewed as alternative but rather as supplementary tools to aid in the management of big Government. For the purposes of exercising control functions the administrative budget, with its stress on accounting for each period's income and outgo of Federally-owned funds, is not likely to be superseded. There will probably be some shift in emphasis, however, toward analyses which yield more information of economic significance.[7] People who would be informed will come more and more to rely upon the consolidated cash statement, which helps to assess the role of Government in maintaining business stability and influencing the reserves of commercial banks. Finally, the possibility of adopting a capital budget will doubtless receive serious consideration as people increasingly sense the need for greater insight into the related problems of allocating tax monies among Federal activities and balancing the cost of capital outlays against the benefits of resulting service flows.

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[6] The issue of securities which are the obligation of the issuing corporation and not directly guaranteed by the Government enable the corporation to obtain funds without adding to the public debt. Certificates of interest issued by the Commodity Credit Corporation and notes of the Federal National Mortgage Association are examples. The lease-purchase method of obtaining public buildings is another device for obtaining the benefits of a capital good without additions to the public debt.

[7] There have been repeated requests, for example, for changes in the *form* of the budget so that more information will be available concerning whole programs and less concerning details of expenditures by departments.