A CITIZEN'S GUIDE TO THE FEDERAL BUDGET

BUDGET OF THE UNITED STATES GOVERNMENT

Fiscal Year 2000

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A Note to the Reader

Next year, your Federal Government will spend nearly *$1.8 trillion.*

Needless to say, that's a lot of money. And the Government spends it on lots of things—on programs as large and popular as Social Security, and on activities as small and unknown as repairs to the National Zoo. Together, these programs are what make up the Federal budget.

How much do you know about the budget? If your answer is "not much," you're not alone. In fact, hardly anybody knows everything that's in the thousands of pages, and several books, that make up the budget each year.

But we know you care a lot about how the Government spends your money. That's why we created *A Citizen's Guide to the Federal Budget* four years ago, and why we have published this fifth edition. With it, we hope to make the budget more accessible and understandable.

The *Guide* is designed to give you a walking tour of the budget. In these pages, we will outline for you how the Government raises revenues and spends money, how the President and Congress enact the budget, why the budget deficit and Federal debt have been problems, and what the President hopes to accomplish with his 2000 budget.

After you read these pages, we hope that you will think the tour was worth your time.

1. What *Is* the Budget?

The Federal budget is:

- a plan for how the Government spends your money.

  What activities are funded? How much does it spend for defense, national parks, the FBI, Medicare, and meat and fish inspection?

- a plan for how the Government pays for its activities.

  How much revenue does it raise through different kinds of taxes—income taxes, excise taxes, and social insurance payroll taxes?

- a plan for Government borrowing.

  If revenues are greater than spending, the Government runs a surplus. When there is a surplus, the Government can reduce the national debt.

- something that affects the Nation's economy.

  Some types of spending—such as improvements in education and support for science and technology—increase productivity and raise incomes in the future.

  Taxes, on the other hand, reduce incomes, leaving people with less money to spend.

- something that is affected by the Nation's economy.

  When the economy is doing well, people are earning more and unemployment is low. In this atmosphere, revenues increase and the deficit shrinks.

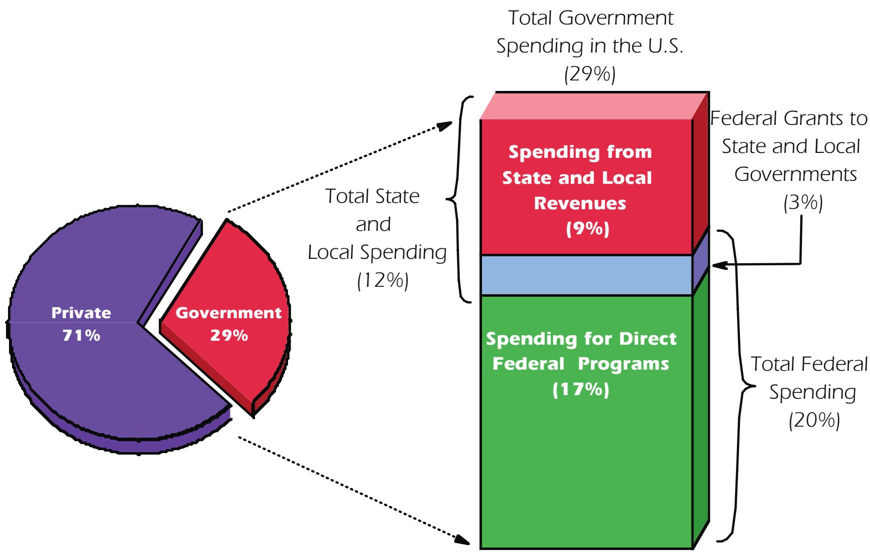
- an historical record.

  The budget reports on how the Government has spent money in the past, and how that spending was financed.

The 2000 Budget is a document that embodies the President's budget proposal to Congress for fiscal 2000, the *fiscal year* that begins on October 1, 1999. It reflects the President's priorities and proposes to protect the budget surplus until Social Security is reformed.

The Federal budget, of course, is not the only budget that affects the economy or the American people. The budgets of State and local

Chart 1–1. Government Spending as a Share of GDP, 1998



Note: Numbers do not add due to rounding.

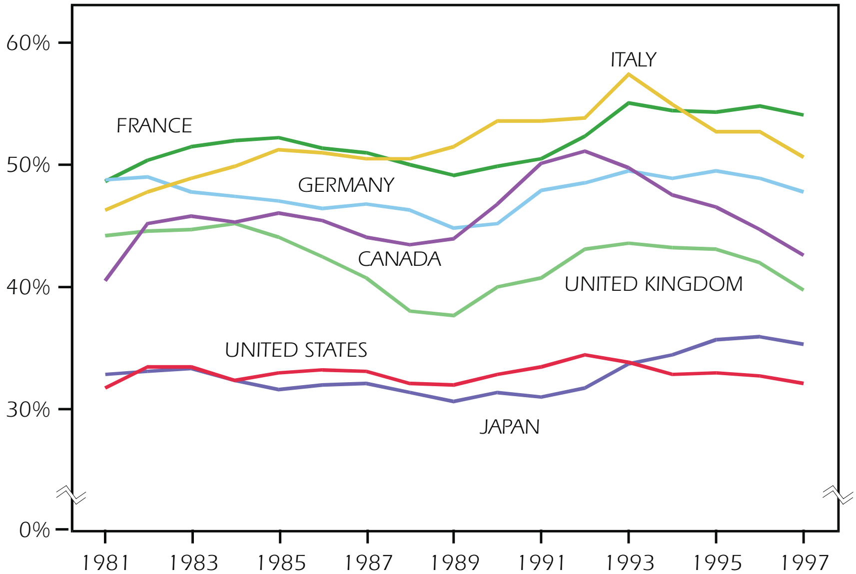
Total Government spending accounts for less than one-third of the national economy. Federal spending is about two-thirds of this amount, or about 20 percent of GDP.

governments have an impact as well. While Federal Government spending was a little less than 20 percent of the Gross Domestic Product (or GDP, which measures the size of the economy) in 1998, State and local governments spending was about another nine percent (see Chart 1–1).

State and local governments are independent of the Federal Government, and they have their own sources of revenue (taxes and borrowing). But the Federal Government supplements State and local revenues by making grants to them. Of the $989 billion that State and local governments spent in 1998, $230 billion came from Federal grants.

As shown in Chart 1–2, compared to six other industrialized nations, the United States allocates the smallest share of its GDP to government spending (Federal, State, and local combined).

Chart 1–2. Total Government Outlays as a Percent of GDP



Source: OECD, calendar year data.

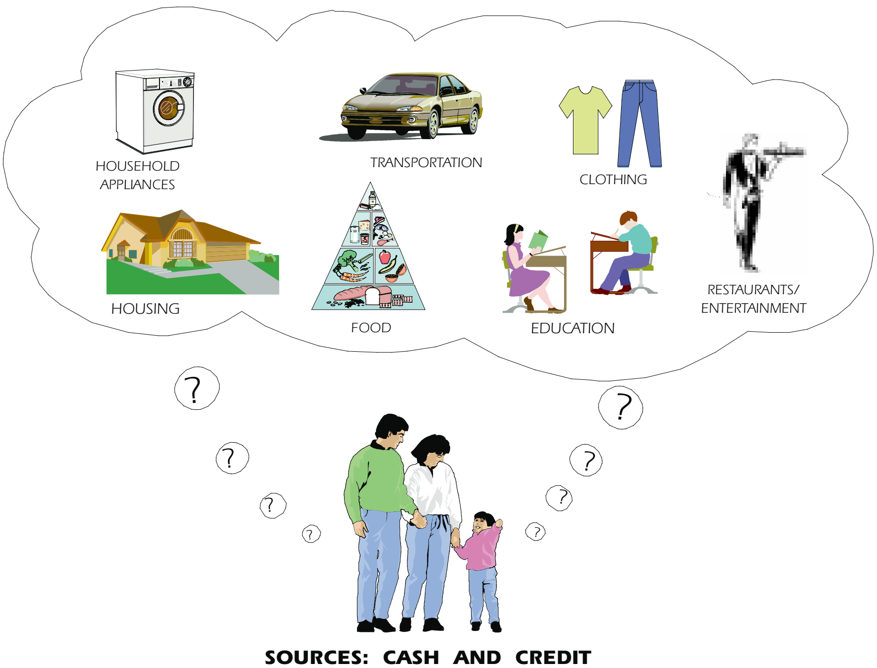
The United States allocates a smaller portion of its GDP to government spending than any other nation shown.

2. Where the Money Comes From—and Where it Goes

In a typical American household, a father and mother might sit around the kitchen table to review the family budget. They might discuss how much they expect to earn each year, how much they can spend on food, shelter, clothing, transportation, and perhaps a vacation, and how much they might be able to save for their future needs.

If they do not have enough money to make ends meet, they might discuss how they can spend less, such as by cutting back on restaurants, movies, or other entertainment. They also might consider whether to try to earn more by working more hours or taking another job. If they expect their shortfall to be temporary, they might try to borrow.

Chart 2–1. Family Budgeting

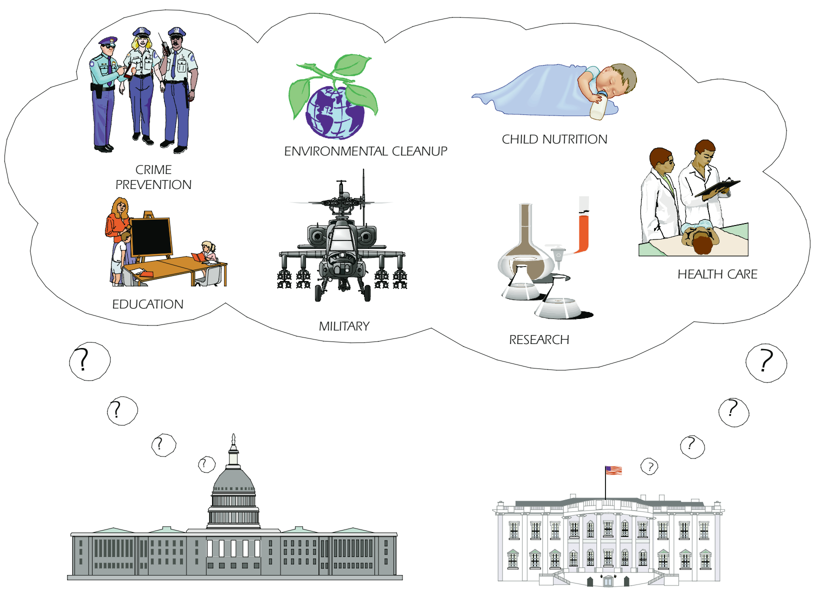


Generally speaking, the Federal Government plans its budget much like families do. The President and Congress determine how much money they expect the Government to receive in each of the next several years, where it will come from, and how much to spend to reach their goals—goals for national defense, foreign affairs, social insurance for the elderly, health insurance for the elderly and poor, law enforcement, education, transportation, science and technology, and others.

They decide how much spending they will finance through taxes and how much through borrowing. They debate how to use the budget to help the economy grow, or to redistribute income. And, especially lately, they debate how to use the budget surplus to address longer-term concerns and invest in the Nation's future.

In this chapter, we will discuss these decisions in some detail—that is, how the Government raises revenues and where it spends money.

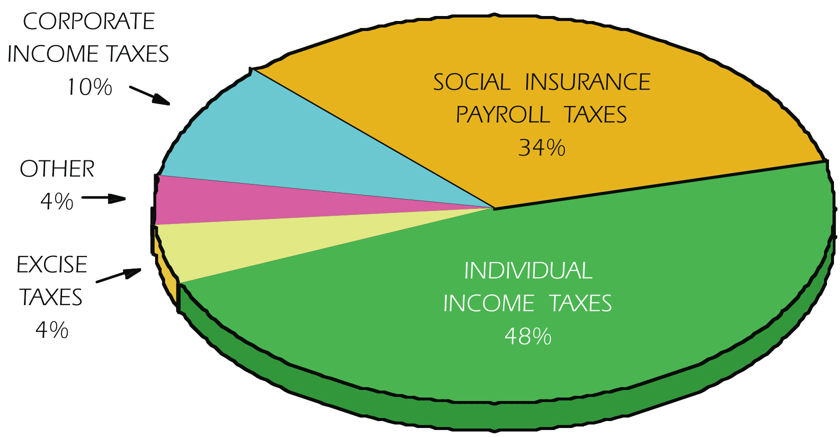
Chart 2–2. National Budgeting



SOURCES: TAXES AND BORROWING

Revenues

Chart 2–3. The Federal Government Dollar—Where It Comes From



The money that the Federal Government uses to pay its bills—its revenues—comes mostly from taxes. In 1998, revenues were greater than spending, and the Government was able to reduce the national debt with the difference between revenues and spending—that is, the surplus.

Revenues come from these sources:

- Individual income taxes will raise an estimated $900 billion in 2000, equal to about 10 percent of GDP.
- Social insurance payroll taxes—the fastest growing category of Federal revenues—include Social Security taxes, Medicare taxes, unemployment insurance taxes, and Federal employee retirement payments. This category has grown from two percent of GDP in 1955 to an estimated seven percent in 2000.
- Corporate income taxes, which will raise an estimated $189 billion, have shrunk steadily as a percent of GDP, from 4.5 percent in 1955 to an estimated 2.1 percent in 2000.

Table 2–1. Revenues By Source—Summary

(In billions of dollars)

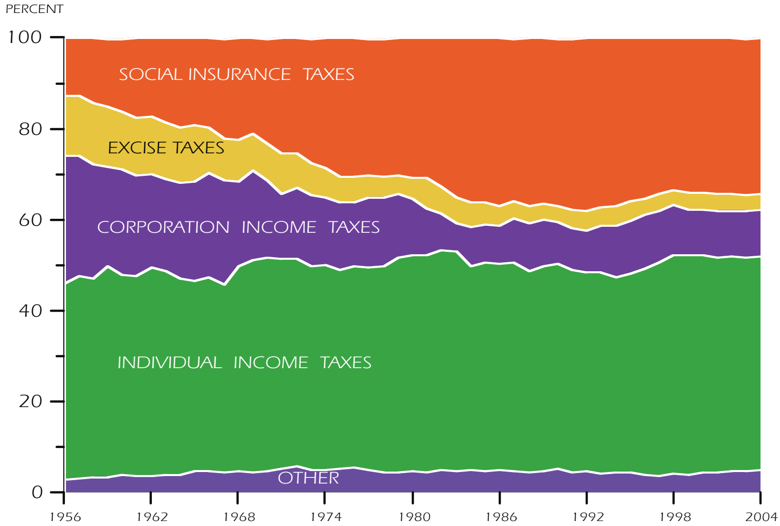
Source	1998 Actual	Estimate 1999	2000	2001	2002	2003	2004
Individual income taxes	829	869	900	912	943	971	1,018
Corporate income taxes	189	182	189	197	203	212	221
Payroll taxes	572	609	637	660	686	712	739
Excise taxes	58	68	70	71	72	74	75
Estate and gift taxes	24	26	27	28	30	32	34
Customs duties	18	18	18	20	21	23	25
Miscellaneous receipts	33	35	42	45	50	52	53
Total receipts	**1,722**	**1,806**	**1,883**	**1,933**	**2,007**	**2,075**	**2,166**

Notes: The revenues listed in this table do not include revenues from the Government's business-like activities—i.e., the sale of electricity and fees at national parks. The Government counts these revenues on the spending side of the budget, deducting them from other spending to calculate its outlays for the year.

Numbers may not add to the totals because of rounding.

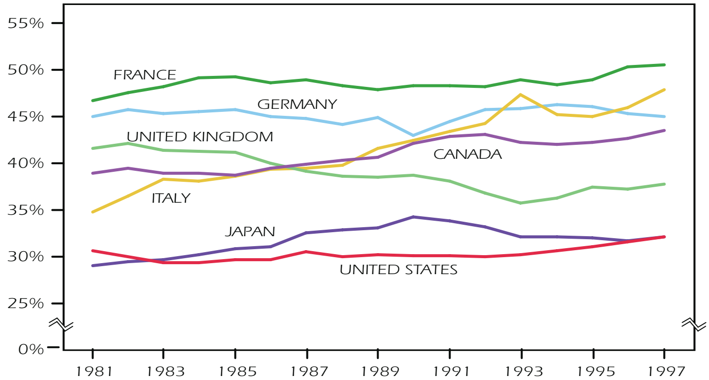
- Excise taxes apply to various products, including alcohol, tobacco, transportation fuels, and telephone services. The Government earmarks some of these taxes to support certain activities—including highways and airports and airways—and deposits others in the general fund.
- The Government also collects miscellaneous revenues—e.g., customs duties, Federal Reserve earnings, fines, penalties, and forfeitures.

Chart 2–4. Composition of Revenues



Between 1960 and 1998, payroll taxes have increased substantially as a percent of total revenues, and corporate income taxes have declined, but individual income taxes have remained roughly constant.

Chart 2–5. Revenues as a Percent of GDP—Comparison With Other Countries



Source: OECD, calendar year data.

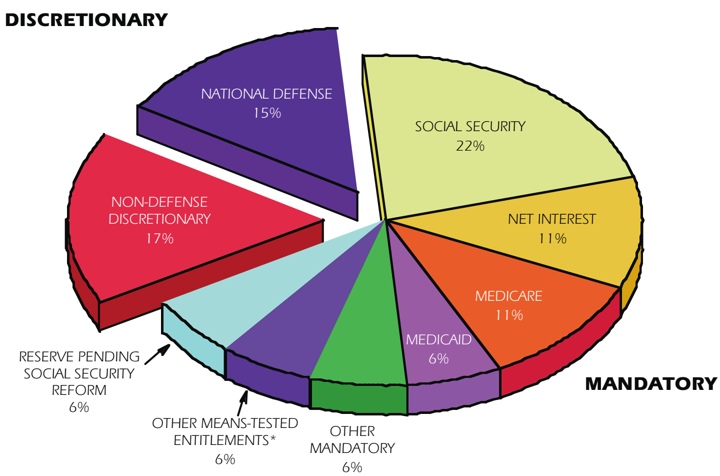
The United States and Japan have the lowest revenues as a percent of GDP of the seven countries shown above.

Spending

As we have said, the Federal Government will spend nearly $1.8 trillion[1,] and have a surplus of over $117 billion in 2000, which we divided into nine large categories as shown in Chart 2–6.

- The largest Federal program is Social Security, which will provide monthly benefits to nearly 45 million retired and disabled workers, their dependents, and survivors. It accounts for 22 percent of your Federal dollar (or 23 percent of all Federal spending).
- Medicare, which will provide health care coverage for over almost 40 million elderly Americans and people with disabilities, consists of Part A (hospital insurance) and Part B (insurance for physician costs and other services). Since its birth in 1965, Medicare has accounted for an ever-

Chart 2–6. The Federal Government Dollar— Where It Goes



** Means-tested entitlements are those for which eligibility is based on income. The Medicaid program is also a means-tested entitlement.*

[1] In calculating Federal spending, the Government deducts collections (revenues) generated by the Government's business-like activities, such as fees to national parks. These collections will total an estimated $216 billion in 2000. Without them, spending would total an estimated $2.0 trillion in 2000, not $1.8 trillion.

growing share of spending. In 2000 it will comprise 11 percent of your Federal dollar (or 12 percent of all Federal spending).

- Medicaid, in 2000, will provide health care services to almost 34 million Americans, including the poor, people with disabilities, and senior citizens in nursing homes. Unlike Medicare, the Federal Government shares the costs of Medicaid with the States, paying between 50 and 83 percent of the total (depending on each State's requirements). Federal and State costs are growing rapidly. Medicaid accounts for six percent of your Federal dollar (also six percent of the budget).

- Other means-tested entitlements provide benefits to people and families with incomes below certain minimum levels that vary from program to program. The major means-tested entitlements are Food Stamps and food aid to Puerto Rico, Supplemental Security Income, Child Nutrition, the Earned Income Tax Credit, and veterans' pensions. This category will account for an estimated six percent of your Federal dollar (also six percent of the budget).

- The remaining mandatory spending, which mainly consists of Federal retirement and insurance programs, unemployment insurance, and payments to farmers, comprises six percent of your Federal dollar (also six percent of the budget).

- National defense discretionary spending will total an estimated $275 billion in 2000, comprising nearly 15 percent of your Federal dollar (and 16 percent of the budget).

- Non-defense discretionary spending—a wide array of programs that include education, training, science, technology, housing, transportation, and foreign aid—has shrunk as a share of the budget from 23 percent in 1966 to an estimated 18 percent in 2000 (or 17 percent of your Federal dollar).

- Interest payments, primarily the result of previous budget deficits, averaged seven percent of Federal spending in the 1960s and 1970s. But, due to the large budget deficits that began in the 1980s that share quickly doubled to 15 percent. Since the budget is now in surplus, interest payments are estimated to drop to 12 percent of the budget in 2000 (11 percent of your Federal dollar).

- Six percent of your Federal dollar (the budget surplus) will not be spent. The President has proposed that any surplus be reserved until a plan to save Social Security has been enacted.

Table 2–2. Spending Summary

(In billions of dollars)

	1998 Actual	Estimate 1999	2000	2001	2002	2003	2004
Budget Policy with Social Security reform:							
Outlays:							
Discretionary:							
Department of Defense	258	265	262	269	279	291	301
Non-DoD discretionary	297	317	330	341	339	338	338
Priority initiatives	......	......	......	2	4	7	10
Subtotal, discretionary	555	581	592	612	623	636	649
Mandatory:							
Programmatic:							
Social Security	376	389	405	424	444	465	487
Medicare and Medicaid	291	311	328	350	363	391	416
Means-tested entitlements (except Medicaid)	99	107	112	118	124	129	134
Deposit insurance	–4	–5	–2	–2	–1	–*	1
Other	92	117	116	118	115	125	131
Subtotal, mandatory	855	919	959	1,007	1,044	1,110	1,170
Net interest	243	227	215	207	197	188	179
Subtotal, mandatory and net interest	1,098	1,146	1,174	1,214	1,241	1,297	1,349
Total, outlays	**1,653**	**1,727**	**1,766**	**1,826**	**1,863**	**1,934**	**1,998**
Receipts	**1,722**	**1,806**	**1,883**	**1,933**	**2,007**	**2,075**	**2,166**
Resources contingent upon Social Security reform:							
Department of Defense	......	......	......	–10	–17	–13	–15
Non-DoD discretionary	......	......	......	–15	–20	–16	–9
Priority initiatives	......	......	......	–2	–4	–7	–10
Related debt service	......	......	......	–1	–2	–4	–6
Total	......	......	......	–27	–43	–41	–40
Reserve pending Social Security reform	**69**	**79**	**117**	**134**	**187**	**182**	**208**
Surplus	**0**	**0**	**0**	**0**	**0**	**0**	**0**
MEMORANDUM:							
Discretionary totals if no Social Security reform is enacted, net of designated offsets	555	581	574	573	568	584	600

* $500 million or less.

Table 2–3. Total Spending by Function

(Outlays, in billions of dollars)

Function	1998 Actual	Estimate 1999	2000	2001	2002	2003	2004
National defense:							
Department of Defense-Military	256	264	261	269	278	290	300
Other	12	13	13	14	14	14	14
Total, national defense	268	277	274	282	292	304	314
International affairs	13	15	16	17	18	18	18
General science, space, and technology	18	19	19	19	19	19	19
Energy	1	*	–2	–1	–1	–1	–1
Natural resources and environment	22	24	24	24	24	24	24
Agriculture	12	21	15	13	11	10	10
Commerce and housing credit	1	*	6	8	9	10	10
Transportation	40	43	46	49	50	52	53
Community and regional development	10	10	10	10	10	9	9
Education, training, employment, and social services	55	60	63	68	67	69	70
Health	131	143	152	163	173	185	197
Medicare	193	205	217	231	235	252	266
Income security	233	243	258	267	275	282	291
Social security	379	393	409	427	447	468	491
Veterans benefits and services	42	44	44	45	46	47	48
Administration of justice	23	24	28	29	28	28	28
General government	13	15	14	15	15	15	15
Net interest	243	227	215	206	195	183	173
Allowances		3	3	–27	–40	–34	–29
Undistributed offsetting receipts	–47	–40	–46	–45	–51	–47	–48
Total	**1,653**	**1,727**	**1,766**	**1,799**	**1,820**	**1,893**	**1,958**

* $500 million or less.

Note: Spending that is shown as a minus means that receipts exceed outlays. Numbers may not add to the totals because of rounding.

Table 2–4. Discretionary Spending by Agency

(Outlays, in billions of dollars)

Agency	1998 Actual	Estimate 1999	2000	2001	2002	2003	2004
Legislative Branch	2	2	3	3	3	3	3
Judicial Branch	3	3	4	4	4	4	4
Agriculture	16	17	16	15	15	15	15
Commerce	4	5	7	5	5	5	5
Defense-Military	258	265	262	269	279	291	301
Education	26	29	32	35	35	35	35
Energy	17	17	18	18	18	18	18
Health and Human Services	35	39	42	43	43	43	43
Housing and Urban Development	33	33	34	34	32	31	30
Interior	7	8	8	9	9	9	9
Justice	15	16	19	20	19	19	19
Labor	10	11	11	11	11	12	12
State	5	6	6	7	7	6	7
Transportation	37	40	43	46	48	49	51
Treasury	11	12	12	13	13	13	13
Veterans Affairs	18	19	19	19	19	19	19
Corps of Engineers	4	4	4	4	4	4	4
Other Defense Civil Programs	*	*	*	*	*	*	*
Environmental Protection Agency	7	7	7	8	7	7	7
Executive Office of the President	*	*	*	*	*	*	*
Federal Emergency Management Agency	3	3	3	3	2	2	2
General Services Administration	1	*	*	*	*	*	*
International Assistance Programs	11	12	12	12	13	12	12
National Aeronautics and Space Administration	14	14	13	13	13	14	14
National Science Foundation	3	3	4	4	4	4	4
Office of Personnel Management	*	*	*	*	*	*	*
Small Business Administration	1	1	1	1	1	1	1
Social Security Administration	5	6	6	6	6	6	6
Other Independent Agencies	6	6	6	6	7	7	7
Allowances	......	3	3	–24	–36	-29	-24
Undistributed offsetting receipts	......	......	–3	1	1	–*	–*
Total	**555**	**581**	**592**	**586**	**582**	**600**	**615**

* $500 million or less.

Note: Discretionary spending is appropriated by the Congress each year, in contrast with mandatory spending, which is automatic under permanent law. For a more complete discussion of discretionary spending, see "Action in Congress" in Chapter 3.

Spending that is shown as a minus means that receipts exceed outlays.

Numbers may not add to the totals because of rounding.

“On” and “Off” Budget

From time to time, you may hear about programs that are “off-budget,” meaning that the Government categorizes them separately from other programs.

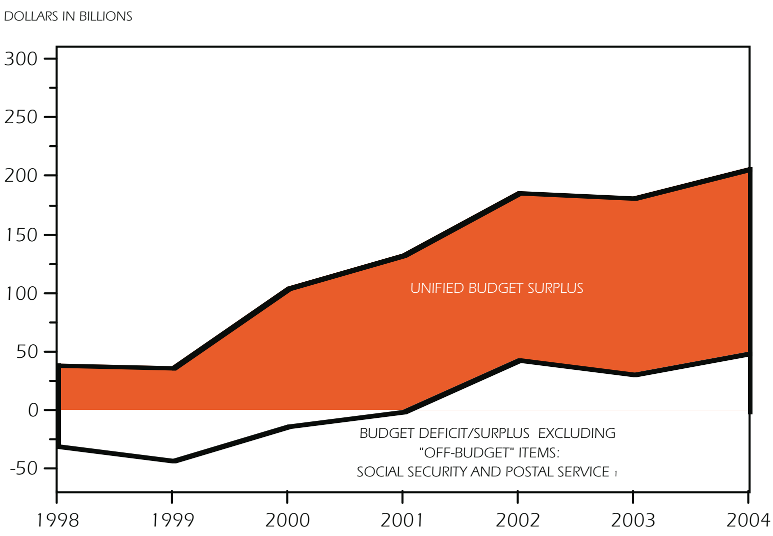
Specifically, the law requires that the spending and revenues of two Federal programs, Social Security and the Postal Service, be excluded from the budget totals—that is, categorized as “off-budget.” Therefore, the budget displays “on-budget,” “off-budget,” and “unified budget” totals to satisfy this legal requirement.

The unified budget is the most useful display of the Government’s finances; it is vital in calculating how much the Government has to borrow.

The “off-budget” category is designed to give special status to certain programs. Over the years, the Government has placed numerous programs “off-budget,” then returned them to the unified budget. But the mere listing of programs as “off-budget” does not, by itself, protect them from the budget process—e.g., Administration and congressional review, possible cuts, and hiring and procurement rules.

Chart 2–7 illustrates the relationship between on- and off-budget items, and the unified budget.

Chart 2–7. On- and Off-Budget Deficit Projections



3. How Does the Government Create a Budget?

The President and Congress both play major roles in developing the Federal budget.

The President's Budget

The law requires that, by the first Monday in February, the President submit to Congress his proposed Federal budget for the next *fiscal year*, which begins October 1.

The White House's Office of Management and Budget (OMB) prepares the budget proposal, after receiving direction from the President and consulting with his senior advisors and officials from Cabinet departments and other agencies.

The President's budget—which typically includes a main book and several accompanying books[1]—covers thousands of pages and provides reams of details.

The Budget Process

Through the budget process, the President and Congress decide how much to spend and tax in any one fiscal year. More specifically, they decide how much to spend on each activity, ensure that the Government spends no more and spends it only for that activity, and report on that spending at the end of each budget cycle.

The President's budget is *his* plan for the next year. But it's just a proposal. After receiving it, Congress has its own budget process to follow. Only after the Congress passes, and the President signs, the required spending bills has the Government created its actual budget.

[1] They are the main budget book, entitled, *Budget of the United States Government: Fiscal Year 2000,* as well as *Analytical Perspectives, Appendix, Historical Tables,* and *A Citizen's Guide to the Federal Budget,* which you are now reading.

For fiscal 2000—that is, October 1, 1999 to September 30, 2000—the major steps in the budget process are outlined in Chart 3–1.

Chart 3–1. Major Steps in the Budget Process

Formulation of the President's budget for fiscal 2000.	Executive Branch agencies develop requests for funds and submit them to the Office of Management and Budget. The President reviews the requests and makes the final decisions on what goes in his budget.	February–December 1998
Budget preparation and transmittal.	The budget documents are prepared and transmitted to Congress.	December 1998–February 1999
Congressional action on the budget.	Congress reviews the President's budget, develops its own budget, and approves spending and revenue bills.	March–September 1999
The fiscal year begins.		October 1, 1999
Agency program managers execute the budget provided in law.		October 1, 1999–September 30, 2000
Data on actual spending and receipts for the completed fiscal year become available.		October–November 2000

Action in Congress

Congress first must pass a "budget resolution"—a framework within which the Members will make their decisions about spending and taxes. It includes targets for total spending, total revenues, and the deficit, and allocations within the spending target for the two types of spending—*discretionary* and *mandatory*—explained below.

- *Discretionary spending,* which accounts for one-third of all Federal spending, is what the President and Congress must decide to spend for the next year through the 13 annual appropriations bills. It includes money for such activities as the FBI and the Coast Guard, for housing and education, for space exploration and highway construction, and for defense and foreign aid.

- *Mandatory spending,* which accounts for two-thirds of all spending, is authorized by permanent laws, not by the 13 annual appropriations bills. It includes entitlements—such as Social Security, Medicare, veterans' benefits, and Food Stamps—through which individuals receive benefits because they are eligible based on their age, income, or other criteria. It also includes interest on the national debt, which the Government pays to individuals and institutions that hold Treasury bonds and other Government securities. The President and Congress can change the law in order to change the spending on entitlements and other mandatory programs—but they don't have to.

Think of it this way: For discretionary programs, Congress and the President *must* act each year to provide spending authority. For mandatory programs, they *may* act in order to change the spending that current laws require.

Currently, the law imposes a limit, or "cap," through 2002 on total annual discretionary spending. Within the cap, however, the President and Congress can, and often do, change the spending levels from year to year for the thousands of individual Federal spending programs.

In addition, the law requires that legislation that would raise mandatory spending or lower revenues—compared to existing law—be offset by spending cuts or revenue increases. This requirement, called "pay-as-you-go," is designed to prevent new legislation from increasing the deficit.

Once Congress passes the budget resolution, it turns its attention to passing the 13 annual appropriations bills and, if it chooses, "authorizing" bills to change the laws governing mandatory spending and revenues.

Congress begins by examining the President's budget in detail. Scores of committees and subcommittees hold hearings on proposals under their jurisdiction. The House and Senate Armed Services Authorizing Committees, and the Defense and Military Construction Subcommittees of the Appropriations Committees, for instance, hold hearings on the President's defense plan. If the President's budget proposed changes in taxes, the House Ways and Means and the Senate Finance Committees would hold hearings. The Budget Director, Cabinet officers, and other Administration officials work with Congress as it accepts some of the President's proposals, rejects others, and changes still others. Congressional rules require that these committees and subcommittees take actions that reflect the budget resolution.

If you read through the President's budget, the budget resolution, or the appropriations or authorizing bills that Congress drafts, you will notice that the Government measures spending in two ways—"budget authority" and "outlays."

Budget authority (or BA) is what the law authorizes the Federal Government to spend for certain programs, projects, or activities. What the Government actually spends in a particular year, however, is an *outlay*. To see the difference, consider what happens when the Government decides to build a space exploration system.

The President and Congress may agree to spend $1 billion for the space system. Congress appropriates $1 billion in BA. But the system may take 10 years to build. Thus, the Government may spend $100 million in outlays in the first year to begin construction and the remaining $900 million over the next nine years as construction continues.

Monitoring the Budget

Once the President and Congress approve spending, the Government monitors the budget through:

- agency program managers and budget officials, including the Inspectors General, or IGs;
- OMB;
- congressional committees; and
- the General Accounting Office, an auditing arm of Congress.

This oversight is designed to:

- ensure that agencies comply with legal limits on spending, and that they use budget authority only for the purposes intended;
- see that programs are operating consistently with legal requirements and existing policy; and, finally,
- ensure that programs are well managed and achieving the intended results.

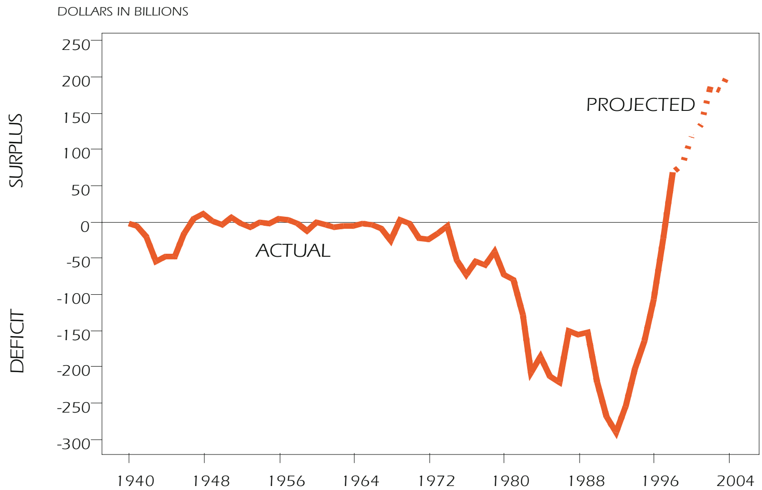
The Government has paid more attention to good management of late, through the work of Vice President Gore's National Partnership for Reinventing Government and implementation of the 1993 Government Performance and Results Act. This law is designed to improve Government programs by using better measurements of their results in order to evaluate their effectiveness.

4. The Budget Surplus and Fiscal Discipline

In 1998 the Federal budget reported a surplus of $69 billion, the first surplus since 1969, and reduced Federal debt held by the public by over $50 billion. With continued prudent fiscal policies, the budget can remain in surplus for many years. The turnaround from deficit to surplus can be attributed to fiscal discipline and strong economic growth. The change from deficit to surplus is an important milestone.

Put simply, a surplus occurs when revenues exceed spending in any year—just as a deficit occurs when spending exceeds revenues. Generally, to finance

Chart 4–1. Past and Future Budget Deficits or Surplus



Deficits began increasing dramatically in the 1980s, but have now been reversed.

past deficits, the Treasury has borrowed money. With certain exceptions, the *debt* is the sum total of our deficits, minus our surplus, over the years.

The Government incurred its first deficit in 1792, and it generated 70 annual deficits between 1900 and 1997.

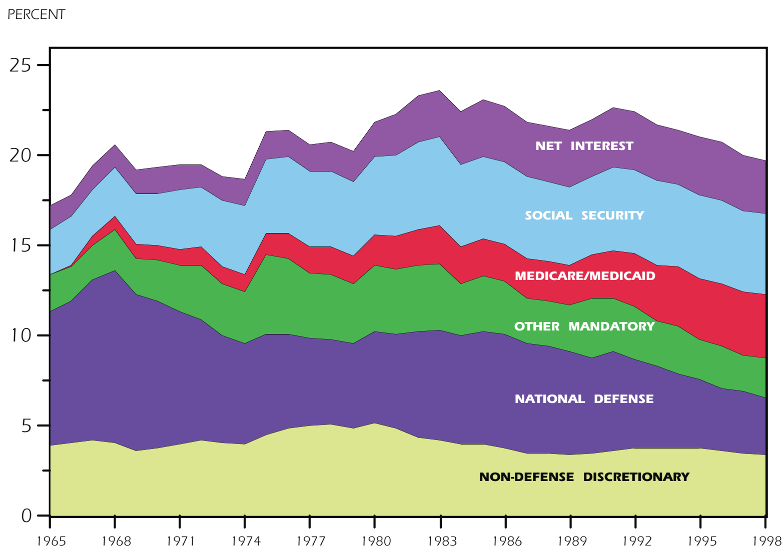
Chart 4–1 provides the history of budget surplus and deficits since 1940.

For most of the Nation's history, deficits were the result of either wars or recessions. Wars necessitated major increases in military spending, while recessions reduced Federal tax revenues from businesses and individuals.

The Government generated deficits during the War of 1812, the recession of 1837, the Civil War, the depression of the 1890s, and World War I. Once the war ended or the economy began to grow, the Government followed its deficits with budget surplus, with which it paid down the debt.

Deficits returned in 1931 and remained for the rest of the decade—due to the Great Depression and the spending associated with President Roosevelt's New Deal. Then, World War II forced the Nation to spend unprecedented amounts on defense and to incur corresponding unprecedented deficits.

Chart 4–2. Outlays as a Percent of GDP



Between 1965 and 1998, spending on Social Security, Medicare and Medicaid, and interest as a percentage of GDP grew, while spending on defense fell.

Since then—with Democratic and Republican Presidents, Democratic and Republican Congresses—the Government has balanced its books only nine times, most recently last year.

Nevertheless, the deficits before 1981 paled in comparison to what followed. That year, the Government cut income tax rates and greatly increased defense spending, but it did not cut non-defense programs enough to make up the difference. Also, the recession of the early 1980s reduced Federal revenues, increased Federal outlays for unemployment insurance and similar programs that are closely tied to economic conditions, and forced the Government to pay interest on more national debt at a time when interest rates were high. As a result, the deficit soared.

Why have we been able to move from deficit to surplus? Because spending growth has been restrained. Outlays are growing slower and revenues are holding steady.

Revenues have stayed relatively constant, at around 17 to 21 percent of GDP, since the 1960s. In that time, however, outlays grew from about 17 percent of GDP in 1965 to nearly 24 percent in 1983 before falling below 20 percent today.

Since 1983, spending had been reduced or held constant as percent of GDP across a wide variety of programs. The most significant reduction has occurred in discretionary spending, which has fallen from 10.3 percent to 6.6 percent of GDP. Combined spending on social security and net interest has remained roughly constant at about 7-1/2 percent of GDP since 1983. A similar path has been followed in the rest of mandatory spending in total, but only because the growth in Medicare and Medicaid has been offset by declines in other mandatory spending (see Chart 4–2).

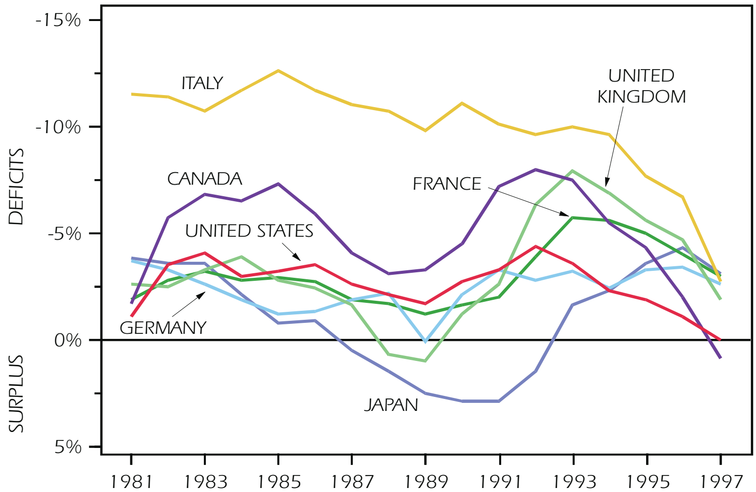
Why a Budget Surplus is Important

As Chart 4–3 illustrates, this Nation has a good record when compared to the recent history of the six other major developed economies. (To make accurate comparisons with the governments of other nations, the U.S. data include the activities of State and local governments.)

Should we worry about the possibility of a return to budget deficits?

The 2000 Budget forecasts surplus for decades to come, if we maintain the policy of fiscal discipline and strategic investments in the American people.

Chart 4–3. Total Government Surplus or Deficit as a Percent of GDP



Source: OECD, calendar year data.

Of the seven nations shown above, only the United States and Canada eliminated their total Government budget deficits in 1997.

We must do all we can to keep the days of deficits in the past. Budget deficits force the Government to borrow money in the private capital markets. That borrowing competes with (1) borrowing by businesses that want to build factories and machines that make workers more productive and raise incomes, and (2) borrowing by families who hope to buy new homes, cars, and other goods. The competition for funds tends to produce higher interest rates.

Deficits increase the Federal debt and, with it, the Government's obligation to pay interest. The more it must pay in interest, the less it has available to spend on education, law enforcement, and other important services, or the more it must collect in taxes—forever after. As recently as 1997, the Government spent over 15 percent of its budget to pay interest, in contrast to a projected 12 percent for 2000. Continuing surplus will reduce these interest payments further in future years.

In the end, the surplus is a decision about our future. We can provide a solid foundation for future generations, just as parents try to do within a family. For a Nation, this means a strong economy and low interest rates and debt. Alternatively, we can generate large deficits and debt for those who come after us.

Surplus and Debt

If the Government incurs a surplus, it generally repays debt held by the public.

Table 4–1 summarizes the relationship between the budget surplus or deficit and the repayment of Federal debt.

Federal borrowing involves the sale, to the public, of notes and bonds of varying sizes and time periods until maturity. The cumulative amount of borrowing from the public—i.e., the debt held by the public—is the most important measure of Federal debt because it is what the Government has borrowed in the private markets over the years, and it determines how much the Government pays in interest to the public.

Debt held by the public was $3.7 trillion at the end of 1998—roughly the net effect of deficits and surplus over the last 200 years. Debt held by the public does not include debt the Government owes itself—the total of all trust fund surplus and deficits over the years, like the Social Security surplus, which the law says must be invested in Federal securities.

Because of the progress in eliminating the budget deficit, the debt held by the public has been reduced for the first time in 29 years.

Table 4–1. Federal Government Financing and Debt

(in billions of dollars)

	1998 Actual	Estimate 1999	2000	2001	2002	2003	2004
Federal Government financing:							
Budget surplus	69	79	117	134	187	182	208
Other means of financing	−18	−29	−19	−17	−17	−16	−15
Repayment of debt held by the public	51	50	98	117	170	166	193
Federal Government debt:							
Debt held by the public	3,720	3,670	3,572	3,455	3,285	3,119	2,926
Debt held by government accounts	1,759	1,945	2,140	2,326	2,530	2,736	2,948
Gross Federal debt	5,479	5,615	5,711	5,781	5,815	5,856	5,874
Debt subject to legal limit	5,439	5,577	5,674	5,745	5,780	5,821	5,842

Note: Numbers may not add to the totals because of rounding.

The sum of debt held by the public and debt the Government owes itself is called Gross Federal Debt. At the end of 1998, it totaled $5.5 trillion.

Another measure of Federal debt is debt subject to legal limit, which is similar to Gross Federal Debt. When the Government reaches the limit, it loses its authority to borrow more to finance its spending; then, the President and Congress must enact a law to increase the limit. Because the budget has returned to surplus and debt is being reduced, there will be no need to increase the statutory limit in 2000.

The Government's ability to finance its debt is tied to the size and strength of the economy, or GDP. Debt held by the public was 44 percent of GDP at the end of 1998. As a percentage of GDP, debt held by the public was highest at the end of World War II, at 109 percent, then fell to 24 percent in 1974 before gradually rising to a peak of 50 percent in the middle 1990s.

That decline, from 109 to 24 percent, occurred because the economy grew faster than the debt accumulated; debt held by the public rose from $242 billion to $344 billion in those years, but the economy grew faster.

Individuals and institutions in the United States hold two-thirds of debt held by the public. The rest is held in foreign countries.

Returning the Budget to Surplus

Ever since the deficit soared in the early 1980s, successive Presidents and Congresses have tried to cut it. Until recently, they met with only limited success.

In the early 1980s, President Reagan and Congress agreed on a large tax cut, but could not agree about cutting spending; the President wanted to cut domestic spending more than Congress, while Congress sought fewer defense funds than the President wanted. They wound up spending more on domestic programs than the President wanted, and more on defense than Congress wanted. At the same time, a recession led to more spending to aid those affected by the recession, and reductions in tax revenues due to lower incomes and corporate profits.

By 1985, both sides were ready for drastic measures. That year, they enacted the Balanced Budget and Emergency Deficit Control Act. It set annual deficit targets for five years, declining to a balanced budget in 1991. If necessary, GRH required across-the-board cuts in programs to comply with the deficit targets.

Faced with the prospect of huge spending cuts in 1987, however, the President and Congress amended the law, postponing a balanced budget until 1993. The President and Congress never achieved those revised targets, in part because of the extraordinary costs of returning the Nation's savings and loan industry to a sound financial footing.

By 1990, President Bush and Congress enacted spending cuts and tax increases that were designed to cut the accumulated deficits by about $500 billion over five years. They also enacted the Budget Enforcement Act (BEA)—rather than set annual deficit targets. The BEA was designed to limit discretionary spending while ensuring that any new entitlement programs or tax cuts did not make the deficit worse.

First, the BEA set annual limits on total discretionary spending for defense, international affairs, and domestic programs. Second, it created ``pay-as-you-go'' rules for entitlements and taxes: those who proposed new spending on entitlements or lower taxes were forced to offset the costs by cutting other entitlements or raising other taxes.

For what it was designed to do, the law worked. It did, in fact, limit discretionary spending and force proponents of new entitlements and tax cuts to find ways to finance them. But the deficit, which Government and private experts said would fall, actually rose.

Why? Because the recession of the early 1990s reduced individual and corporate tax revenues and increased spending that is tied to economic fluctuations. Federal health care spending also continued to grow rapidly.

In 1993, President Clinton and the Congress made another effort to cut the deficit. They enacted a five-year deficit reduction package of spending cuts and higher revenues. The law was designed to cut the accumulated deficits from 1994 to 1998 by about $500 billion. The new law extended the limits on discretionary spending and the "pay-as-you-go'' rules.

Although the 1993 plan exceeded all expectations in reducing the deficit, the task of reaching balance would require one final push. That would come with the historic 1997 Balanced Budget Act (BBA).

Originally designed to balance the budget by 2002, the BBA provided for $247 billion in savings over five years. It also extended the solvency of Medicare's trust fund for at least 10 years while providing for the largest investment in higher education since the G.I. Bill in 1945, the largest investment in children's health care since the creation of Medicaid in 1965, and a $500-per-child tax credit for about 27 million working families.

Clearly, the President's deficit reduction efforts have paid off. The deficit fell from $290 billion in 1992 to a surplus of $69 billion in 1998.

The President is now proposing to reserve the surplus until Social Security is reformed. His plan for reform uses 62 percent of the projected unified budget surplus of the next 15 years to put the Social Security system on sound financial footing well into the next century. In 2000 the challenge for both the President and the Congress is to maintain fiscal discipline and reach comprehensive Social Security reform while continuing to invest in the American people. The next chapter describes the President's plans for achieving that goal.

5. THE PRESIDENT'S 2000 BUDGET

The President's 2000 budget promises the third balanced budget of this Administration. With it, the Nation's fiscal house is in order and we are prepared to meet the challenges of the next century. It continues on the path the President has followed for the past six years of maintaining fiscal discipline and investing wisely in our Nation's priorities.

It invests in education and training so Americans can make the most of this economy's opportunities. It invests in health and the environment to improve our quality of life. It invests in our security at home and abroad, strengthens law enforcement and provides our Armed Forces with the resources they need to safeguard our national interests in the next century.

The President's budget makes these investments while maintaining the fiscal discipline that allowed the Federal Government to record its first surplus in a generation last year. The budget forecasts that the Government will produce a surplus again this year, and will continue to do so for decades to come. Our success in eliminating the budget deficit proves that we are capable of fulfilling great responsibilities, and there is now every reason for us to rise to the next challenge. The President believes it is now time to work together to save Social Security.

Investing in the Future

In his State of the Union address, the President proposed a framework for a comprehensive, bipartisan solution to the long-term financing problems of Social Security. The President's plan proposes using 62 percent of the unified budget surplus of the next 15 years to strengthen Social Security. It would tap the power of financial markets by investing roughly one-fifth of the surplus dedicated to Social Security in private financial instruments, including corporate equities. This proposal would substantially improve the program's fiscal position, strengthening it until the middle of the next century. Then, in a bipartisan effort envisioned by the national dialogue of the last year, the President is urging Congress to join him to make the difficult but achievable choices to save Social Security until 2075.

Once Social Security is on sound financial footing, the President proposes saving and improving Medicare, the Federal program that finances health care for millions of seniors and disabled Americans. The President's framework will reserve 15 percent of the projected budget surplus of the next 15 years for Medicare, ensuring that its trust fund is secure for 20 years.

The President is also committed to helping all Americans save and invest so that they will have additional sources of income in retirement. Dedicating just over 10 percent of the surplus of the next 15 years to Universal Savings Accounts will help Americans save for the future by allowing them to invest as they choose and receive matching contributions.

And looking ahead to the Nation's other vital needs that will arise in the future, the President's framework will reserve 11 percent of the projected surplus for military readiness, education, and other critical domestic priorities.

The President's budget builds on efforts to invest in the skills of the American people. It continues his policy of helping working families with their basic needs—raising their children, sending them to college, and expanding access to health care. It also invests in education and training, the environment, science and technology, law enforcement, and other priorities to help raise the standard of living and quality of life of Americans.

In this budget, the President is proposing major initiatives that will continue his investments in high-priority areas—from helping working families with their child care expenses to allowing Americans from 55 to 65 to buy into Medicare; from helping States and school districts recruit and prepare thousands more teachers and build thousands more classrooms to making every effort to fight tobacco and its use among young people.

For six years, the President has sought to help working families balance the demands of work and family. In this budget he proposes a major effort to make child care more affordable, accessible and safe, by expanding tax credits for middle-income families and for businesses to expand their child care resources, assisting parents who want to attend college meet their child care needs, and increasing funds with which the Child Care and Development Block Grant can help more poor and near poor children. The budget proposes an Early Learning Fund, which would provide grants to communities for activities that improve early childhood education and the quality of childcare for those under age five.

The President has worked hard to expand health care coverage and improve the Nation's health. The budget gives new insurance options to hundreds of thousands of Americans aged 55 to 65 and it advocates bipartisan national legislation that would reduce tobacco use among the young. The President's budget proposes initiatives to help patients, families, and care givers cope with the burdens of long-term care; and it helps reduce barriers to employment for individuals with disabilities. The budget also enables more Medicare beneficiaries to receive promising cancer treatments by participating more easily in clinical trials. And it improves the fiscal soundness of Medicare and Medicaid through new management proposals, including programs to combat waste, fraud, and abuse.

The President's efforts have also enhanced access to, and the quality of, education and training. The budget takes the next steps by continuing to help States and school districts reduce class size by recruiting and preparing thousands more teachers and building thousands more new classrooms. The President's budget proposes improving school accountability by funding monetary awards to the highest performing schools that serve low-income students, providing resources to States to help them identify and change the least successful schools, and ending social promotion by funding additional education hours through programs like the 21st Century Community Learning Centers. The budget also proposes further increases in the maximum Pell Grant to help low-income undergraduates complete their college education and more funding for universal reemployment services to help train or find jobs for all dislocated workers who need help.

The budget proposes a historic inter-agency Lands Legacy initiative to both preserve the Nation's Great Places, and advance preservation of open spaces in every community. This initiative will give State and local governments the tools for orderly growth while protecting and enhancing green spaces, clean water, wildlife habitat and outdoor recreation. The Administration also proposes a Livability Initiative with a new financing mechanism, Better America Bonds, to create more open spaces in urban and suburban areas, improve water quality, and clean up abandoned industrial sites. In addition, the budget would restore and rehabilitate national parks, forests, and public lands and facilities; expand efforts to restore and protect the water quality of rivers and lakes; and better protect endangered species.

The President has worked to bring peace to troubled parts of the world, and has played a leadership role in Northern Ireland, Bosnia, and most recently in the Wye River Memorandum on the Middle East. The budget reinforces America's commitment to peace in the Middle East by providing for an economic and military assistance package arising from the Wye River Memorandum. The work of diplomacy, advancing peace and United States interests, has inherent dangers, as the death toll from the terrorist attacks on two U.S. Embassies in Africa last year reminds us. The budget proposes increased funding to ensure the continued protection of American embassies, consulates and other facilities, and the valuable employees who work there. It supports significant increases in funding for State Department programs to address the threats posed by weapons of mass destruction. The budget also increases programs that support U.S. manufacturing exports and continues our long standing policy of opening foreign markets.

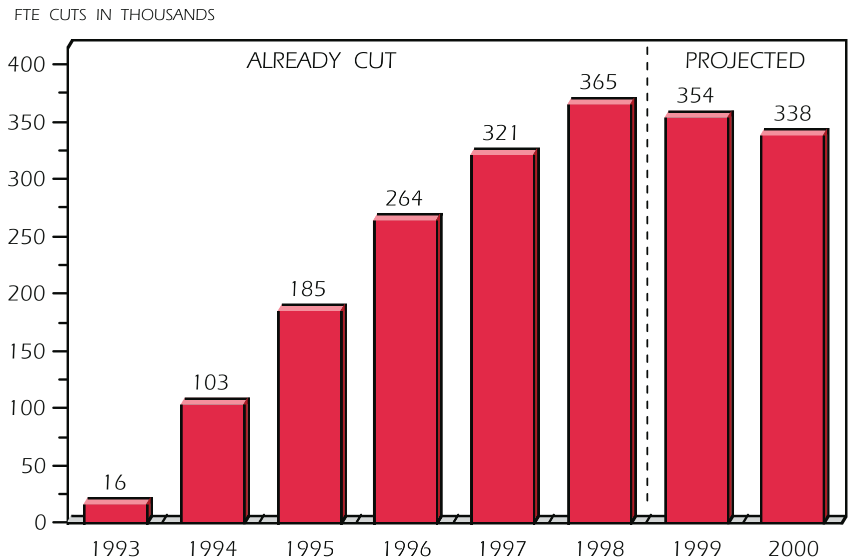
The mission of our Armed Forces has changed in this post-Cold War era, and in many ways it is more complex. Today, the U.S. military must guard against major threats to the Nation's security, including regional dangers like cross-border aggression, the proliferation of the technology of weapons of mass destruction, transnational dangers like the spread of drugs and terrorism, and direct attacks on the U.S. homeland from intercontinental ballistic missiles or other weapons of mass destruction. The U.S. Armed Forces are well prepared to meet this mission. Military readiness—the ability to engage where and when necessary—is razor sharp, and this budget provides resources to make sure that it stays that way for years to come. The budget provides a long term, sustained increase in defense spending to enhance the military's ability to respond to crises, build for the future through programs for weapons modernization, and take care of military personnel and their families by enhancing the quality of life, thereby increasing retention and recruitment.

Improving Performance Through Better Management

A key element in the Administration's ability to making these investments, while balancing the budget, is the reinvention of Government—doing more with less. Efforts led by Vice President Gore's National Partnership for Reinvention have streamlined Government, reduced its work force, and focused on performance to improve operations and delivery of service. And these efforts, by reducing the cost of Government operations, have improved the bottom line and contributed to our strong economy.

Since 1993, the Administration, working with the Congress, has eliminated and reduced hundreds of unnecessary programs and projects. The size of Government, that is, the actual total of Government spending, has equaled a smaller share of GDP than in any year of the previous two Administrations, and in 2000 will drop to 19.4 percent of GDP, its lowest level since the early 1970s. Finally, the Administration has cut the size of the Federal civilian work force by 365,000, creating the smallest work force in 36 years and, as a share of total civilian employment, the smallest since 1933 (see Chart 5–1).

Chart 5–1. Cuts in Civilian Employment



Note: In 1993, the President pledged to cut the Federal work force by 252,000 full-time equivalent (FTE) positions. Simply put, one full-time employee counts as one FTE, and two employees who work half-time also count as one FTE.

The Administration, however, is working to create not just a smaller Government, but a better one, a Government that best provides services and benefits to its ultimate customers—the American people. It has not just cut the Federal work force, it has streamlined layers of bureaucracy. It has not just reorganized headquarters and field offices, it has ensured that those closest to the customers can best serve them.

For 2000, the Administration once again is turning its efforts to the next stage of "reinventing" the Federal Government. It plans to dramatically overhaul 32 Federal agencies to improve performance in key services, such as expediting student loan processing and speeding aid to disaster victims. It also plans to continue tackling critical challenges, such as ensuring that Government computers can process the year 2000 date change and making more Government services available electronically.

Under the 1993 Government Performance and Results Act, Cabinet departments and agencies have prepared individual performance plans that they will send to Congress with the performance goals they plan to meet in 2000. These plans provided the basis for the second Government-wide

Performance Plan which is contained in this budget. In 2000, for the first time, agencies will submit to the President and the Congress annual reports for 1999 that compare actual and target performance levels and explain any difference between them.

Glossary

Appropriation

An appropriation is an act of Congress that enables Federal agencies to spend money for specific purposes.

Authorization

An authorization is an act of Congress that establishes or continues a Federal program or agency, and sets forth the guidelines to which it must adhere.

Balanced Budget

A balanced budget occurs when total revenues equal total outlays for a fiscal year.

Budget Authority (BA)

Budget authority is what the law authorizes, or allows, the Federal Government to spend for programs, projects, or activities.

Budget Enforcement Act (BEA) of 1990

The BEA is the law that was designed to limit discretionary spending while ensuring that any new entitlement program or tax cuts did not make the deficit worse. It set annual limits on total discretionary spending and created "pay-as-you-go'' rules for any changes in entitlements and taxes (see "pay-as-you-go'').

Balanced Budget and Emergency Deficit Control Act of 1985 (Gramm-Rudman-Hollings, or GRH)

The Balanced Budget and Emergency Deficit Control Act of 1985 was designed to end deficit spending. It set annual deficit targets for five years, declining to a balanced budget in 1991. If necessary, it required across-the-board cuts in programs to comply with the deficit targets. It was never fully implemented.

Budget Resolution

The budget resolution is the annual framework within which Congress makes its decisions about spending and taxes. This framework includes targets for total spending, total revenues, and the deficit, as well as allocations, within the spending target, for discretionary and mandatory spending.

"Cap''

A "cap'' is a legal limit on annual discretionary spending.

Deficit

The deficit is the difference produced when spending exceeds revenues in a fiscal year.

Discretionary Spending

Discretionary spending is what the President and Congress must decide to spend for the next fiscal year through 13 annual appropriations bills. Examples include money for such activities as the FBI and the Coast Guard, housing and education, space exploration and highway construction, and defense and foreign aid.

Entitlement

An entitlement is a program that legally obligates the Federal Government to make payments to any person who meets the legal criteria for eligibility. Examples include Social Security, Medicare, and Medicaid.

Excise Taxes

Excise taxes apply to various products, including alcohol, tobacco, transportation fuels, and telephone service.

Federal Debt

The gross Federal debt is divided into two categories: debt held by the public, and debt the Government owes itself. Another category is debt subject to legal limit.

Debt Held by the Public

Debt held by the public is the total of all Federal deficits, minus surplus, over the years. This is the cumulative amount of money the Federal Government has borrowed from the public, through the sale of notes and bonds of varying sizes and time periods.

Debt the Government Owes Itself

Debt the Government owes itself is the total of all trust fund surplus over the years, like the Social Security surplus, that the law says must be invested in Federal securities.

Debt Subject to Legal Limit

Debt subject to legal limit, which is roughly the same as gross Federal debt, is the maximum amount of Federal securities that may be legally outstanding at any time. When the limit is reached, the President and Congress must enact a law to increase it.

Fiscal Year

The fiscal year is the Government's accounting period. It begins October 1 and ends on September 30. For example, fiscal 2000 ends September 30, 2000.

Gramm-Rudman-Hollings

See Balanced Budget and Emergency Deficit Control Act of 1985.

Gross Domestic Product (GDP)

GDP is the standard measurement of the size of the economy. It is the total production of goods and services within the United States.

Mandatory Spending

Mandatory spending is authorized by permanent law. An example is Social Security. The President and Congress can change the law to change the level of spending on mandatory programs—but they don't have to.

"Off-Budget"

By law, the Government must distinguish "off-budget" programs separate from the budget totals. Social Security and the Postal Service are "off-budget."

Outlays

Outlays are the amount of money the Government actually spends in a given fiscal year.

"Pay-As-You-Go"

Set forth by the BEA, "pay-as-you-go" refers to requirements that new spending proposals on entitlements or tax cuts must be offset by cuts in other entitlements or by other tax increases, to ensure that the deficit does not rise (see BEA).

Revenue

Revenue is money collected by the Government.

Social Insurance Payroll Taxes

This tax category includes Social Security taxes, Medicare taxes, unemployment insurance taxes, and Federal employee retirement payments.

Surplus

A surplus is the amount by which revenues exceed outlays.

Trust Funds

Trust funds are Government accounts, set forth by law as trust funds, for revenues and spending designated for specific purposes.

Unified Federal Budget

The unified budget, the most useful display of the Government's finances, is the presentation of the Federal budget in which revenues from all sources and outlays to all activities are consolidated.

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