

Government Spending



Basics

- Public sector spending began to rise after WWII
- Two kinds
 - ◆ Buying goods & services
 - ◆ Transfer payments
 - ★ Grant-in-aid
 - ★ Social Security
 - ★ Welfare

Federal Budget

- 2/3 mandatory spending
 - ◆ Interest, Social Security, medicare
- 1/3 Discretionary spending—must get annual authorization
 - ◆ Military, education, welfare
- Fiscal year October 1-Sept. 30

The Process

- President confers with OMB, cabinet
- Sends budget to Congress by early February
- House breaks down discretionary spending into 13 appropriation bills
 - ◆ Subcommittees review and vote
 - ◆ House Appropriations Committee
 - ◆ Entire House by Sept. 15th
- Senate
 - ◆ May revise or accept bill
 - ◆ If revised, must have joint House-Senate committee to approve
- President must sign

Major Categories

- Social Security
- Defense
- Medicare
- Income Security
- Health
- Interest
- Education
- Transportation
- Veteran's Benefits
- Science, Space, Technology
- International Affairs

Deficits and the Nat'l Debt

- Deficit—spending in excess of revenues
- Federal debt—total amount borrowed to finance deficit spending accumulated over time
- Dept of Treasury sells bonds, T-bills to finance deficit spending
- Current Debt: \$9 Trillion or ~\$30,000 per person

Public vs. Private Debt

- Most of Fed. Debt owed to itself
- No payment plan, issues new bonds to pay
- When govt pays, purchasing power goes to someone else
- Private debt owed to others
- Repayment plan
- Give up purchasing power until debt paid down

Impact of National Debt

- Causes a transfer of purchasing power from the private to the public sector
- The larger the federal debt, the larger the interest payments
- If taxes are increased:
 - ◆ may diminish incentives for Americans to work, save, and invest.
- In selling bonds to raise money,
 - ◆ government competes with the private sector for scarce resources
 - ◆ leads to higher-than-normal interest rates.

Reforms

- Gramm-Rudman-Hollings (1985)
 - ◆ Set federal deficit targets so that \$0 deficit by 1991
 - ◆ Failed
 - ★ Congress passed spending bills that took effect 2 or 3 years later
 - ★ Economic decline in July 1990
- Budget Enforcement Act of 1990
 - ◆ “pay-as-you-go”—new spending had to be offset by reductions elsewhere
 - ◆ Applies only to discretionary spending
 - ◆ Can be suspended if economy enters low-growth phase or president declares emergency

- Omnibus Budget Reconciliation Act of 1993
 - ◆ Goal to reduce \$500B from deficit over 5 years
 - ◆ Intended to reduce rate of growth, not deficit itself
 - ◆ Included spending reductions and tax increases to top 1.2 % of taxpayers (makes income tax more progressive)

- **Balanced Budget Agreement of 1997**
 - ◆ Spending caps—spending limits to assure balanced budget by 2002
 - ◆ Unpopular cuts in health, science and education
 - ◆ 1998—Success!
 - ★ Strong economy=record tax collections
 - ★ Reduced federal spending
 - ◆ entitlements