Reforms for Improved Efficiency in Public Budgeting and Finance: Improvements, Disappointments, and Work-in-Progress

JOHN L. MIKESELL AND DANIEL R. MULLINS

The past half-century has brought heightened expectations for what systems of budgeting and finance may be expected to deliver for the public. From systems to provide a first defense against theft and gross misappropriation, they have become systems to help lawmakers direct public resources where they can give the best public return, to help managers efficiently utilize resources under their control, and to communicate plans and results to the public. Government fiscal systems have developed more useful expenditure classification, established new measures for identifying public performance, brought nontraditional spending into control systems, and made finances considerably more transparent. Systems should, in combination with robust democratic institutions, make the public sector perform in the best interests of the citizenry. But in the face of great fiscal system improvements, governments struggle with staying fiscally sustainable, with meeting financial obligations to vulnerable populations, and even with avoiding default, receivership, or bankruptcy. Even as systems improve, government finances decline amid considerable private sector prosperity. Research over the past decade has done little to aid or explain the sweeping expectation and limited success of budget systems to transform essential elements of governance. It is the purpose of this paper to review progress in the development of robust fiscal systems, identify the major obstacles and failures, and link this evidence to the record of recent governmental financial distress, paying particular attention to the struggles of American governments. The broader questions needing to be addressed are the same questions at the forefront of public sector finance 100 years ago; however, the present focus has not been on these broader implications.

INTRODUCTION

Historian Barbara Tuchman had low expectations from government: “Mankind, it seems, makes a poorer performance of government than of almost any other human
Unfortunately, American public budgeting and finance provides only the most modest evidence against her expectations. Achievements should be better, because the purpose and function of public sector budgeting has not changed over the decades and neither have many of the problems with and failures of budgeting systems. The structures and processes that constitute budgeting should serve to (1) insure fiscal discipline, control, responsibility, and fiscal sustainability; (2) insure that budgetary resources are directed toward the programs of greatest public return; (3) induce programs to make most efficient use of resources they have been allocated; and (4) provide transparent information about programs and finances to the public. In the past half-century, American governments—federal, state, and local—have developed a number of innovative features for their budget processes that aim to better implement these functions. With all of the effort, however, it is not clear that the progress in these areas has been substantial. The age-old issues of measurement and assessment absent a market remain. At the same time, there has been very little progress dealing with other substantive fiscal issues. The sections that follow will examine some of the more interesting innovations, giving an idea of their strengths and weaknesses and some of the bigger continuing failures.

For some background, it is helpful to note that the concept of a public budget has been unchanged for many years. In 1915, Cleveland defined a budget as “... a plan for financing an enterprise or government during a definite period, which is prepared and submitted by a responsible executive to a representative body (or other duly constituted agent) whose approval and authorization are necessary before the plan may be executed.” That conceptualization works as well in 2011 as it did in 1915. The budget process as a whole involves the development, approval, execution, and evaluation and audit of that budget. It should be noted that when Cleveland established his conceptualization, the federal government had neither a budget nor a budget process. Congress focused on appropriating—giving federal departments authority to spend—and the executive branch focused on operating within those appropriations. There was no budgeting (developing plans, getting approval of those plans, executing the approved plan, and auditing that execution). Appropriating is required by the U.S. Constitution, hence the attention to this effort. The essential elements of budgeting in this country were developed from scratch and grafted into the existing structure. Reforms and innovations have and will focus on changing technical elements of this process, but what constitutes its broader essential


4. “No money shall be drawn from the treasury, but in consequence of appropriations made by law ...”: Article 1, Section 9, Clause 7, U.S. Constitution.
elements remain the same. Nothing of substance has altered the importance of these elements over the past century and their need for continued attention remains. The future of meaningful budgetary progress does not lie in accrual presentations or measurement of outputs/outcomes. It lies in understanding the economic and political incentives, actors, processes, and institutions that permeate, facilitate, and constrain the budgeting and governance function.

Just as the process has proven durable, so too the expectations from that process remain little changed. The features that will be discussed here involve efforts to improve the functioning of the process in terms of these four expectations of returns from budget systems: fiscal discipline, resource allocation, technical efficiency, and transparency. In the flow of discussions about improvements to budget processes, transparency is the most recent principle to be added to the discussions. And, on reflection, it would appear to be the most important of the principles for budget making and execution in a democratic nation because, absent transparency, the public will have no basis for making its choices.

The Logical Model: Budgeting and Financial Management for the Public Good

Seventy years ago, V. O. Key posed the simple question that encapsulates all budget decisions: “On what basis shall it be decided to allocate X dollars to activity A instead of activity B?”5 As it turns out, answering this question has not been a problem for either theory or in practice. It has not stumped practitioners—they have made those decisions for years, even before Professor Key raised it and, indeed, even before there were formal public budgets. And it certainly has not been an unanswered question for prescriptive economic analysis: allocate resources between the private and public sector and between competing uses in the public sector so that moving $1 from one sector or use to another yields exactly the same return in the new use as it did in the old. The basis is the welfare of the public, the allocation standard is easily understandable (equate returns at the margins), and—whether the innovators understood it or not—recent innovations in budgeting have been square-on with working toward achievement of this result.6 Similarly, answering the budgeting question has been no mystery for descriptive analysis: public choice maintains that politicians and bureaucrats are driven by individual self-interest and both will seek to allocate resources in a way that satisfies those individual interests, not some concept of the public interest. However, the fact that the budgeting question has been regularly answered in practice and in both prescriptive and descriptive theory does not retard efforts

5. V. O. Key, “The Lack of a Budgetary Theory,” The American Political Science Review 34, December (1940): 1137–1144. The problem with answering this question is, of course, the traditional straw man quotation for “theoretical” discussions of public budgeting.

to alter processes and procedures to produce results that are, at least to some calculations, better than those being achieved, meaning that they better fulfill the four roles of a budget process.

There is, however, a technical stumbling block and it is politics. Building processes and procedures that are in some sense better will not necessarily lead to budget outcomes that are better, in the sense of providing a superior allocation of resources because the processes bridge the technical and the political. Wildavsky points out the big stumbling block: “[T]he budget lies at the heart” of politics. “The victories and defeats, the compromises and bargains, the realms of agreement and the spheres of conflict in regard to the role of . . . government in our society all appear in the budget.”

Without both political will and motivation, innovations in budgeting and financial management will be futile, both in terms of getting the innovations adopted and in terms of getting the desired result from them. The political dimension elevates the value of process rather than outcomes. In fact, Wildavsky has also noted that one measure of a “good” budget is simply its enactment—that it emerged from the compromises of the political system. While this may appear as quite a low standard, the budgetary stalemates of nearly the past quarter half century suggest the vital nature of process to both political and technical outcomes.

One significant barrier to easy movement between political and technical in the budget process is that there is no single measure of public welfare that applies across all public services. And a second major barrier is the fact that elected officials generally care more about the people they represent, the ones who directly vote for them, than they do for the general public welfare. No single measure applies to all services—nutrition programs for mothers and children, safe highways, tax collection, prevention of environmental degradation, and so on yield radically different returns and come in different service units, so how may marginal returns be compared across them all and how do we compared these public returns from that resulting from leaving resources with private holders? While we do have measures of the work that government agencies do, of the way that they do that work, and of the number of workers who do that work, we lack measures of the results of that work and how those results contribute to the common welfare. The desire for such a measuring stick has, in some ways, been the holy grail of budgeting for nearly a century. Such are the inherent complications of getting a budget process that generates improvements in the common welfare. Without a measure, we do not know what we have or how we are changing.

In spite of the complications, the history of budget reforms has been one of search for a rational linkage between ends and means to answer the Key question. And the items in that

---


8. As pointed out later, Congress regularly fails to pass its budget (the Budget Resolution) and almost never gets all appropriation acts approved before the start of the fiscal year. States do considerably better at enacting state budgets, but even they periodically fail. So, Wildavsky has a good point here. It is a low standard, but apparently a challenging one.

9. And they may care even more for the interests of their financial contributors than to the interests of the general electorate.
history are numerous, a list that includes, among others, the 1921 Budget and Accounting Act, the work of the Hoover Commissions, the Congressional Budget and Impoundment Control Act of 1974, the Program Planning Budgeting reforms of the 1960s, zero base budgeting in the 1970s, the Emergency Deficit Control Act (Gramm-Rudman-Hollings), the Budget Enforcement Act of 1990, the Government Performance Results Act (GPRA) of 1993, the program assessment rating tool (PART) effort from 2002 to 2007, the creation of a Chief Performance Officer by the Obama administration, and most recently the Budget Control Act of 2011. There have been so many efforts because success has been elusive. Some are mostly aimed at executive responsibilities, some are mostly aimed at the legislative, and some aim at a more rational process, but all attempt to repair deficiencies and all make the systems more complicated. Their impacts are on what budget documents contain, how the documents are organized, and how the processes work. Attempts to “rationalize” budget systems are often criticized because they may require unattainable objectivity and consensus. However, accurate they may be on their face, objections to reforms based on excessive complexity and information constraints appear without standing; the functions of government are themselves complex—complexity is the modus operandi and, to be relevant, budgeting must reflect this environment.

Reform efforts of recent years are in no way path breaking. In many respects, they follow the rethinking prescribed in federal planning programming budgeting systems (PPBS) of the 1960s. They even trace back to reform proposals of the early 1900s. PPBS met its demise from multiple wounds by the end of the 1960s but not before permanently changing the information content and structure of U.S. budgeting. PPBS continued in the Department of Defense even as other parts of the federal government formally abandoned it (it is now called the Planning, Programming, Budgeting, and Execution System in that department) and the Department of Homeland Security, the National Aeronautic and Space Agency, and the National Oceanic and Atmospheric Administration have recently adopted such systems. Rational prescriptions of today build on previous initiatives at the same time that they repeat past errors of hubris. However, obvious technical and political issues remain, which will continue to elevate the importance of process as a standard for assessing the efficacy of budgetary outcomes.

The ultimate measure of budgeting processes and procedures is whether they improve the allocation of resources, both between private and public uses and among alternate public options. But information and standards for evaluating the economic quality of budgeting

---

10. The ideas are not much different from those of the New York Bureau of Municipal Research in the early 1900s.
outcomes are scarce. This makes public sector resource allocation inherently complicated and a process perpetually open to “improvements” and “reforms;” the improvements sometimes only appear to be reforms in the eyes of those proposing them.

Budget evaluations often default to measurement of process achievements because there is no objective information for judging budget results. The fundamental process questions include the following: (1) was there reasonable balance between revenues and expenditures, (2) did budget stages, including final passage of appropriations, meet calendar deadlines, (3) was the adopted budget executed as it was enacted, (4) did the process allow a balanced competition among alternatives, (5) did participants see the decision outcomes as legitimate, and (6) did all interests get represented in budget deliberations. These tests of procedures are not grand evaluations. But they cannot be swept away as being beneath our concern because our budget processes so frequently fail them.

Trying to Get Better Results from the Budget Process: Some Possible Improvements

Components of American government budget processes have changed considerably over the past half-century. A comparison over the years would show easier accessibility of fiscal information, improved organization of information for making budget decisions, more information provided for making those decisions, and some new structures designed to allow better response to public demands for services. The federal government continues to work with a unified budget that does not treat capital spending differently from operating and no formula has emerged to replace political choices with technocratic choices and continued ad hoc arrangements to get through political stalemates, but there have been changes to both processes and what goes into them. Likewise, state and local governments show considerable improvements in information organization and availability. A number of these changes/innovations have been used at all levels of American government. Some may have had demonstrable results.

The Results/Outcomes Focus: Looking at the Right Stuff. The challenge has been to redirect budget processes and procedures away from attention to agencies, what they purchase, and how they operate toward the actual services that governments provide. Governments, probably driven by a desire for operational control, have a predisposition to focusing on inputs (the purchases) and organizations in their budget processes. Inputs are easily tangible and identifiable and their acquisition is usually unambiguous. They can be counted and measured—and labor inputs have the added feature of being able to vote in elections that select lawmakers who pass budgets. Organizations have clear administrative leadership and those leaders can be held responsible for resources appropriated to the organization. Therefore, inputs and organizations are most easily controlled and that has historically been what American governments have required of their budget processes.

That focus is misguided. Just as no sane bakery would order ingredients without first deciding whether it faces demand for cakes or for pies, no government agency at any level of government should build its operating plan without attending first and foremost to what services it must provide the public. Nevertheless, for decades governments have built their budgets primarily with a focus on inputs, particularly on their labor force, with but indirect attention given to services that the public demands and how those services may most efficiently be delivered. For instance, when authorization for activities of the U.S. Department of Transportation threatened to expire in 2011, the call for action by both the president and Senators supporting that work focused on the jobs that were at jeopardy (1.8 million) and not at all on the actual services that would not be performed. The concern was with inputs to be purchased, rather than on the role of government as service provider—in other words, as an alternative to provision by the private sector. The input focus is crazy—Americans love Apple not because of the people the company employs but because of the wonderful electronic devices that have changed the way the world behaves, in other words, for what it produces. Fiscal control and micromanagement (plus a political imperative for votes) provide a powerful incentive for governments to organize their budgets in a less-than-useful fashion, control the wrong measures, and test the wrong result. Even more troubling is that many local governments and their agencies continue to develop their budgets by adding a percentage change to prior year input expenditure categories, thereby perpetuating the attitude that governments function as spenders and employers, but not service providers.

Recent decades have produced two changes to improve the budgeting focus: (1) functional classification of spending and (2) attention to outcomes rather than inputs or activities in the process. These budget reforms provide better focus on social outcomes from the use of public resources and a better context for consideration of alternative uses of scarce resources in the attainment of one outcome versus another. Together, they organize public spending according to helpful categories for consideration and focus attention of decision makers, administrators, and the public on the proper objectives.

The first, the functional, or programmatic classification, provides for a comparative assessment of program options and gives decision makers and the public a clear understanding of the relative service emphases intended by the entity. No longer is it necessary to parse

---


16. Interestingly, this is a nearly universal phenomenon, with the budgets of liberalized, reforming, and unreformed alike fixated on inputs. It appears the convenient and easiest organizing framework for a budget. See Mikesell and Mullins (2001, op cit).

17. At the federal level, functional classification was required in the Congressional Budget and Impoundment Control Act of 1974. Classification by program was also inherent in the Planning Programming Budgeting system in the first part of the 1960s, but it was not carried through after the demise of PPBS in the Nixon Administration. Various state and local governments experimented with the classification from the late 1960s onward, with the extent of utilization dependent on the particular cohort of elected officials.
out unrelated programs within the responsibility of administrative agencies or to add together related programs located in several agencies to understand the total commitment to a particular area by a government. Because only administrative units, not functions or programs, can be responsible for public resources, the functional classification does require a crosswalk to the administrative structure, but the technology of information management now makes this translation relatively simple. It is now common, but certainly not universal, practice for all levels of government in the United States to carry both administrative and functional classifications in their budget presentations, something rare even less than two decades ago. That classification provides decision makers, the public, and the media insights into government operations and fiscal plans that were previously not attainable. The combination provides both fiscal control (through the continuing administrative classification) and better capacity to allocate government resources (through the functional classification).18

The second change in focus—one that has been given more prominence in both practical and academic discussions—is that associated with the movement toward performance or results-oriented (or outcome-oriented) budgeting. The outcome focus moves attention down the production relationship for government services, moving from attention to the materials purchased for the production of government services (inputs) and from attention to how governments use those inputs (the activities, tasks, or outputs that governments produce), to the services that governments provide for the public (results, ends, or outcomes). Economists have argued for a results focus for decades, but now even the most orthodox bureaucrat understands the importance of results (and marginal returns), not inputs and not tasks performed in getting from inputs to results.

Recognizing the need does not make the task easy. There remains great difficulty in specifically identifying results, getting agreement that those are the proper results for the entity, measuring those results, and figuring out what the reported measures actually mean for performance—and then deciding what that performance should mean for the budget. It is not simple to establish certain and verified linkages between means and results; there are environmental factors that complicate the linkage and make the link found in one jurisdiction less than certain in another, and the results themselves are difficult to identify and quantify for many government services. These complications cause many budget processes to revert to a focus on means and the activities conducted by administrative units rather than on outcomes. An outcome orientation is much more difficult in application than it is conceptually.

The language of these results or outcome oriented budgeting programs resembles that of program budgeting of the 1960s. The conceptual difference is that measured “outcomes”

18. As countries became independent of the old Soviet Union, they had to create new budget classification systems. The central planning system that drove their economic sectors produced fiscal statements (something like budgets) that carried a classification roughly like functions or programs. Their first reform was to create administrative budgets, rather the reverse of American budgetary change. But if the system lacks clear administrative budgets, it lacks appropriate fiscal responsibility and control.
occur within (not across) organizational units and there is much attention given to identifying, measuring, and presenting those outcomes. Outcome assessment does not span organizational boundaries as it does in a functional program structure, even when the budget presentation also includes a functional classification of spending. Outcomes are controlled at the agency level, not by function. In some performance measurement schemes, the measures appear in a report not connected to the budget process, further complicating the process of getting fiscal attention directed to service delivery. Then, this was also a problem observed by the New York Bureau of Municipal Research in 1917.19

The fact that outcomes are what, logically, ought to be measured does not reduce the difficulty of identifying and measuring them. As a result—and possibly because of the administrative unit organization of the process—the measured outcomes better fit the definition of activities/outputs. The “outcome” language functions as window dressing disguising a lack of substantive implementation. This has been typical of the federal GPRA and the PART (discussed below), as well as the performance budgeting/budgeting for results initiatives used by state and local governments.

The failures in applied outcome orientation do not mean that an outcome focus is inappropriate, ill-advised, or impossible. They do underline the difficulties in application and suggest that performance measures be identified with great care to assure that their successful pursuit will make for good results for society, even if they are not true “results.” State and local government experience shows that output measures often serve as substitutes for outcomes, with output achievement creating uncertainty as to the implications for social welfare. Being able to measure a performance attribute becomes an important selection standard, even though measurability may have little importance for the citizenry. This measurability problem is not new. Performance budgeting of the past couple of decades professes differences from that of the past which include (1) better measurement, (2) better information technology, and (3) broader integration of budget processes into strategy and performance management. However, none of this circumvents the difficult challenge of measuring the value of public services. The challenge remains for fundamental public services, and links with mission statements or development of citizen satisfaction surveys will not alter that challenge. These links can help rationalize internal organization management and assess operations but they are more evolutionary than revolutionary and they do not alter the fundamental difficulty of an outcome focus.

The zenith of modern performance budgeting, at least so far, as a tool for executive budget formulation is almost certainly the PART system employed by the administration of President George Bush. It reflects the most extensive use of performance budgeting to drive development of an executive budget in American experience. The system was distinct from the institution of strategic plans, performance measurement, and performance reporting

---

stimulated by the National Performance Review\textsuperscript{20} and the GPRA of 1993, but certainly built on logic emerging from those efforts. GPRA was somewhat unique in that it was the product of something of a competition between the executive and legislative branches for performance management superiority. Its adoption occurred concurrently with Vice President Gore’s National Performance Review and received both legislative and executive support. Unlike most past “reforms” that had been executive driven, support from Congress promised to make GPRA different, but that was generally not the result. By 2001, citing a GAO survey, the administration concluded that the GPRA had produced performance measures that were ill defined, poorly integrated into decision making and largely ignored.\textsuperscript{21}

It should be noted, however, that, despite that negative assessment, after GPRA agency budget submissions started systematically carrying performance information, some focusing on outcomes, which had never appeared previously.

The PART system, introduced in 2002, required explicit performance assessment and evaluation, quantitative performance scoring for government programs, and transparent presentation of that scoring, with the understanding that program scores would drive agency budgets. Office of Management and Budget (OMB) had developed PART scores for 98 percent of federal programs by 2008.\textsuperscript{22} The system was the fundamental tool for budget control and policy management in the Bush administration.\textsuperscript{23}

Assessments of the use of PART have emphasized the intent to institute an objective processes and ratings, although political factors dampen the influence of the scores.\textsuperscript{24} This is the reality of budgeting in a democratic environment. Still, PART scores appear to have influenced budget decisions, particularly administration proposed budget increases.\textsuperscript{25} However, “program purpose” and “design”—all dimensions of management—seemed more influential than did “results.” Thus, the PART system was probably more focused on internal performance than on outcomes.

\textsuperscript{20} Documents of the National Performance Review, renamed the National Partnership for Reinventing Government are available from: \url{http://govinfo.library.unt.edu/npr/library/review.html}; accessed 15 November 2011.


PART scores had less influence on Congressional appropriation decisions.\textsuperscript{26} Regardless of their inclusion in budget justifications or mention in hearing testimony, there appears to be little linkage between scores and funding, not surprising in that appropriation are Congressional choices and the scores are purely executive. That pattern does not mean that the PART system was a failure. The president must build a budget driven by his plans and objectives and if the PART system serves for that role, it has met its objective, regardless of what Congress ultimately does.

The possible contributions of PART withstanding, the use of performance information by federal managers did not fare well during the decade between 1997 and 2007. In attempting to convey lessons for the next administration, the GAO found that the use of performance information for setting priorities, resource allocation, adjusting work processes, coordinating programs, and establishing employee expectations had either stagnated or declined.\textsuperscript{27} The GAO also concluded and cautioned that “For the collection of performance information to be considered more than meaningless paperwork exercises, it must be useful to and used by federal decision makers at all levels—including Congress.” That is not yet the case.

The “output/outcome” focus has also not escaped rather continuous state and local attention. To be sure, as indicated above, it originated at the local level. The initial focus was on control, and uniform accounts and accounting methods were first advocated by the National Municipal League in 1899.\textsuperscript{28} By the 1920s, the emphasis began to shift from control to management. Managerial efficiency and effectiveness have been continuing objectives and programmatic approaches focused on priorities, goals, and objectives are recurrent themes of reform; however, these give way to across the board cuts, narrow efficiency determinations and short-sighted service pricing and contracting in periods of fiscal austerity.\textsuperscript{29} The situation is no different in the present. The value of a broader informational perspective often becomes most apparent in times in which it is least achievable. During the latter 1990s, there was renewed interest in governmental efficiency and effectiveness and in improved accountability and this emerged in an era of relative prosperity. State and local governments began to respond to pressure to reconsider and adjust budgeting systems, reopening the book of budget reform. Nearly all states were identified as having adopted elements of performance budgeting and results oriented management employing performance measures.\textsuperscript{30} The range

\begin{enumerate}
\item Frisco and Stalebrink (2008, op cit).
\end{enumerate}
of implementation varies considerably and the contribution to better resource allocation is not clear. In reality, there was little difference in this renewed interest beyond that recognized by the Bureau of Municipal Research in the first two decades of the last century, the 1940s through 1950 extensions to performance budgeting, program budgeting of the 1960s, or management by objectives and zero base budgeting of the 1970s. The “new” performance “informed” budget systems reveal little new under the sun. While the existence of performance budgeting practices are frequently cited, output measures prevail and usage appears primarily limited to budget formulation and executive review. The appeal is, however, broad with the Governmental Accounting Standards Board (GASB) toying with provisions to require the reporting of service efforts and accomplishments just after the change of the millennia.31

Some things are clear from the recent experience with performance/outcome oriented budgeting. First, there is no standard definition of what this style of budget process actually is, with the result that different researchers report on findings from different numbers of implementations. Under that label fall many varieties of process, structure, reporting, and monitoring. The federal PART system was probably the most thoroughgoing effort to put performance principles directly into budget construction, but state and local systems are typically much different from this federal system. Two exceptions: the Indiana PROBE (Program Results: an Outcome-Based Evaluation) system and the Illinois SMART (Strategic Management Accountability Reporting Tool) system are generally based on the PART model.32

Second, in practice, performance measures presented in the budget process are quite often outputs, activities, and tasks rather than outcomes and much of the focus continues to be on inputs and activities. It is not clear whether this is purely a reflection of the difficulty of identifying and measuring outcomes when public goods are involved or whether this reflects a continuing preference for the more easily controllable activities and purchases.

Third, whatever is ultimately measured becomes the performance objective of agencies, crowding out other things that the agency does, so it is critical that the measure is right because whatever is measured is what the public will get. It is important to keep Campbell’s Law in mind in this regard: “The more any quantitative social indicator is used for social decision-making, the more subject it will be to corruption pressures and the more apt it will be to distort and corrupt the social processes it is intended to monitor.”33 For instance, it should be no surprise that schools and school districts cheat when test scores drive budgets, etc.

---

31. This position was opposed by the International City/County Management Association and the Government Finance Officers Association based on concerns that GASB lacked technical competence in such areas.

32. Indiana Governor Mitch Daniels was head of the Office of Management and Budget when the federal PART was implemented.

school evaluations, teacher employment conditions, and so on.\textsuperscript{34} An implication of this incentive is that measures done by third parties are better than measures that come from agencies themselves. There are many examples of agencies manipulating measures when the stakes are high. Unfortunately, third-party measures are not frequently available or are expensive to obtain, so the performance system frequently falls back on measures generated by reporting systems of the entity being measured. One implication is that if measures are going to drive resources, then an auditing process to assure the veracity of reported measures may be as important as an audit of financial operations.

Finally and possibly strangely, examinations of the impacts of performance reforms themselves generally focus on the budgeting process and seldom on the results or outcomes of the budget process. There is no clear evidence that moving toward a performance budgeting model does more than make participants in the process feel better about the process. Analysis has generally focused on problems of implementation, reactions within the agencies, and operations of the system and not on what actually happens when the new system goes into action. It is not clear that use of the system constrains spending or redirects spending toward more deserving government programs.

The outcome orientation in practice has not been the driving force in evaluations of outcome oriented budgeting itself. But, at last, government agencies and public decision makers are organizing to ask the right questions. Political power and influence may overwhelm the information being provided, but that is the nature of a democratic process. However, the attention to outcomes has recently suffered a setback. On October 5, 2011, the House Subcommittee on Oversight and Investigations conducted the first of a promised series of hearings titled “Administration Efforts on Line-by-Line Budget Review,” apparently intending a review of budgets on an input line basis. The intent of the hearings may be purely political, designed to poke at the Obama administration’s repeated promise to conduct a “page by page, line by line” review of the federal budget to purge programs that are not needed, duplicative, or wasteful. Or the hearings may represent a serious misunderstanding of budgeting for the 21st century—outcomes, not line items.

\textit{Countering Threats from Tax Base Erosion: The Tax Expenditure Budget. “... a rose by any other name would smell as sweet.”}\textsuperscript{35} Public spending that is hidden, unmeasured, and permanent conflicts with concepts of good governance. Tax expenditure budgets are an intended check of such spending. Spending through the tax code has not only become an alternative to direct spending, it has also become preferred for some functions. Its use for stimulus purposes is a case in point. Of the $787 billion (revised to $840 billion) allocated under the American Recovery and Reinvestment Act in February of 2009, $298.5 billion (or 42 percent of the 717.4 billion distributed to date) has come in the form of tax expenditures. More than half (57 percent) of the supplemental stimulus package introduced

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{34} The Atlanta, Georgia Public School System cheating experience reported in 2011 is one recent illustration. See Kim Severson, “Systematic Cheating is Found in Atlanta’s School System,” \textit{New York Times} (July 8, 2011).
\item \textsuperscript{35} William Shakespeare, \textit{The Most Excellent and Lamentable Tragedy of Romeo and Juliet} (London: Thomas Creed, 1599).
\end{itemize}
\end{footnotesize}
by the administration in September 2011 was in the form of tax cuts. Irrespective of the attempts to codify and shine the light of transparency on this spending (beginning with the 1974 Congressional Budget and Impoundment Control Act), subsidization through tax preferences still face less analysis and control than does direct spending and contributes much toward a form of “stealth” governance.

The Congressional Budget and Impoundment Control Act of 1974 defines tax expenditures as “… revenue losses attributable to provisions of the federal tax laws which allows a special exclusion, exemption, or deduction from gross income or which provides a special credit, a preferential rate of tax, or a deferral of tax liability.” A direct budget subsidy could accomplish the same thing, but the tax expenditure, relative to the budget subsidy, is hidden outside the fiscal control and scrutiny of annual appropriation process, and a back-door expenditure. The tax expenditure budget provides transparency and fiscal control that otherwise would be absent from the budget process.

Assistant secretary of the U.S. Treasury, Stanley Surrey, introduced the tax expenditure concept to government finance in the late 1960s. The Congressional Budget and Impoundment Act of 1974 (Public Law 93–344) required a statement of federal tax expenditures in each federal budget. By 2010, 41 states were preparing tax expenditure budgets, as were virtually all countries of the Organization for Economic Development and Cooperation. Presentation of a tax expenditure statement is recommended by both OECD and the IMF to advance fiscal transparency.

Tax expenditure measurement and reporting makes the fiscal size of preferences known and permits the preference to be compared with alternative ways of providing the subsidy. It also provides an important check against losses to the treasury and control over what become permanent subsidies allocated through tax laws. In contrast with the annual appropriation process, tax provisions continue in law until the law is revised, making them more or less permanent. Without tax expenditure estimates, tax preferences are subsidies of unknown size. Permanent and invisible are not features likely to produce good public outcomes.

For the best contribution to the budget process, the tax expenditure budget system has the following three requirements: (1) the normal or baseline structure needs to be formally identified (what would the tax structure without preferences be?), (2) the tax expenditures need to be identified and publicized in the same structure as the direct expenditure portion

36. Surrey produced the first federal tax expenditure budget in U.S. Secretary of the Treasury, Annual Report of the State of the Finances: 1968 on an experimental basis. It did not become a regular component of the federal budget process until a few years later. William Vickery developed the idea in Agenda for Progressive Taxation (New York: Ronald Press, 1947), but Surrey was able to put the concept in actual practice.


of the budget (years, classification), and (3) the tax expenditures need to be fully inte-
gerated into the budget process (subject to the same constraints, reviews, approvals, and cycles). In spite of the periodic arguments about what the normal structure should be, the American federal tax expenditure meets the requirements in all regards except in subjecting the tax expenditures to the same legislative committee reviews and approvals as are direct expenditures. This, however, is a big omission. Without this, tax expenditures receive only a minuscule fraction of the attention devoted to direct spending and this lack of attention leads to much less transparency, irrespective of the presentation of tax expenditure estimates in the president’s budget submission.

The tax expenditure budget process has not eliminated federal tax expenditures and even has not dramatically constrained their use in federal finances. The first Joint Committee on Taxation report in 1972 found 43 separate individual income tax expenditures for that year. The comparable report for 2010 listed 139 preferences with an impact above $50 million each and 53 more with smaller impact. And, once a tax expenditure is in place, it tends to stay in place: of 270 provisions in place in 1988 or enacted at any time between 1987 and 2007, 202 remained in place in 2007. This reflects the permanence, relative to direct appropriations, that makes tax preferences so attractive to interested parties. This is a permanence that tax expenditures share with entitlement spending (discussed below): once in the system, they are not regularly reviewed and they will remain in the system without additional legislative action. When there are outlay ceilings, as there have been at various points in recent American fiscal history, the tax expenditures are not covered in the controls. The Tax Reform Act of 1986 did broaden the individual income tax base by eliminating a number of tax preferences, thus allowing a considerable reduction of nominal tax rates, and it is tempting to see the influence of tax expenditure budgets in this. However, there is no clear evidence of major influence, and lawmakers proceeded with more narrowing almost as soon as the ink was dry on the 1986 act, even with the tax expenditure budgets numbers lurking within the process.

The tax reforms of the mid-1980s sought to significantly reduce the level of tax expendi-
tures and had some success, but only for a short time. Tax expenditures have grown faster than direct outlays. In 1980, tax expenditures were equal to 24.9 percent of direct spending across the functional spending areas in which they are classified. By 1990, that total was 27.4 percent and it reached 29.8 percent in 2010. Growth in the role of tax expenditures

39. State tax expenditure budgets do not meet these three criteria as well: they are less likely to identify the “normal” tax structure, tax expenditures are not regularly classified on the same basis as direct expenditures, and the tax expenditure presentations are often not connected to the rest of the budget.


Table 1 reports direct expenditures and tax expenditures for major budget functions for fiscal 2010 and fiscal 2011. Those data show that tax expenditures are larger than direct expenditure, often by a large amount, for commerce and housing, education, fiscal assistance to subnational governments, and international affairs. Also, tax expenditures through the individual income tax are generally greater than those through the corporate income tax, creating something of a political barrier to reducing the preferences. A comparison of the average annual rate of increase of direct outlays and tax expenditures over the 1980–2010 period (starting with 1980 to give some adjustment time for the required preparation of the tax expenditure budget) shows a rate of increase for tax expenditures of 5.9 percent and a rate of increase for direct outlays of 5.2 percent. That gives little comfort to the view that the tax expenditure budget process significantly dampened the use of the tax system to provide preferences. However, absent the process, the rate of increase could well have been much greater.

### Table 1

<table>
<thead>
<tr>
<th>Budget function</th>
<th>Direct outlay 2010</th>
<th>Total tax expenditures 2010</th>
<th>Corporate tax expenditures 2010</th>
<th>Individual tax expenditures 2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>21,356</td>
<td>880</td>
<td>40</td>
<td>840</td>
</tr>
<tr>
<td>Commerce and housing</td>
<td>(82,298)</td>
<td>365,230</td>
<td>37,150</td>
<td>328,080</td>
</tr>
<tr>
<td>Community and regional development</td>
<td>23,804</td>
<td>2,520</td>
<td>1,220</td>
<td>1,300</td>
</tr>
<tr>
<td>Education, training, employment, and social services</td>
<td>127,710</td>
<td>141,190</td>
<td>4,090</td>
<td>137,100</td>
</tr>
<tr>
<td>Energy</td>
<td>11,613</td>
<td>8,990</td>
<td>4,560</td>
<td>4,430</td>
</tr>
<tr>
<td>General purpose fiscal assistance</td>
<td>5,082</td>
<td>57,330</td>
<td>9,850</td>
<td>47,480</td>
</tr>
<tr>
<td>General science, space, and technology</td>
<td>31,047</td>
<td>9,450</td>
<td>8,990</td>
<td>460</td>
</tr>
<tr>
<td>Health</td>
<td>369,054</td>
<td>187,830</td>
<td>2,540</td>
<td>185,290</td>
</tr>
<tr>
<td>Income security</td>
<td>622,210</td>
<td>143,330</td>
<td>950</td>
<td>142,380</td>
</tr>
<tr>
<td>Interest</td>
<td>196,194</td>
<td>1,180</td>
<td>–</td>
<td>1,180</td>
</tr>
<tr>
<td>International affairs</td>
<td>45,195</td>
<td>50,910</td>
<td>43,140</td>
<td>7,770</td>
</tr>
<tr>
<td>Medicare</td>
<td>451,636</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>National defense</td>
<td>693,568</td>
<td>12,740</td>
<td>–</td>
<td>12,740</td>
</tr>
<tr>
<td>Natural resources and environment</td>
<td>43,662</td>
<td>2,120</td>
<td>1,510</td>
<td>610</td>
</tr>
<tr>
<td>Social security</td>
<td>683,420</td>
<td>32,330</td>
<td>–</td>
<td>32,330</td>
</tr>
<tr>
<td>Transportation</td>
<td>91,972</td>
<td>3,860</td>
<td>120</td>
<td>3,740</td>
</tr>
<tr>
<td>Veterans benefits and services</td>
<td>108,384</td>
<td>4,810</td>
<td>10</td>
<td>4,800</td>
</tr>
</tbody>
</table>

The same lawmakers who call for a simpler tax code with fewer complicated tax preferences are eager to add a new tax credit or other preference to favor higher employment, innovation, an industry from the lawmaker’s home state, or whatever. Still, the role of tax expenditure analysis cannot be dismissed because the number and amount of tax expenditures may have been much higher without the extra transparency the analysis provides. In any case, there is an important legislative process barrier to direct comparison: the Congressional committees that write tax law are not the same ones with responsibility over direct appropriations, so there will be no direct balancing of the alternate means of spending.

**Direct Citizen Participation—When, To What Extent, and To What End?.** Informing the public after the major fiscal decisions have been made is not consistent with most concepts of how democracy should work. However, that represents the approach used by most governments in the United States: public hearings are held on the budget submitted by the executive, after major decisions have been already made. Alternatives are winnowed and significant policy choices are made before this presentation and, while revisions are technically possible after the public sees and can comment on the budget, too much has been already cast for major changes to occur to that presented budget—even if the executive presenting the budget proposals needs the approval of a hostile legislature to put the proposals into action. The executive serves as the agent of the public, but obtaining specific input from the public is episodic at best.

Concerns with “democraticizing” the budget process aim to bring direct public input into the development of the budget. The logic is that elected representatives of the people, whether executive or legislative, cannot adequately serve as agents of the people and the public needs an alternative channel into fiscal decisions. In the United States, the democratization response at the subnational level has generally been to bring the public into the process through various advisory boards attached to service-providing agencies. Members of the boards would be expected to include the major “customers” of the agencies and the information they provide can be a useful input to developing programs of the agency. A less-desirable approach sometimes referred to as “participatory budgeting” has had considerable play in other countries. These structures—the one in Porto Allegre, Brazil is most often cited, although there are known to have also been experiments by localities in Albania, Brazil, Bolivia, the Czech Republic, Canada, Ireland, India, Uganda, the United Kingdom, Romania, and South Africa—bring various local interest groups formally into budget development and execution and try to involve citizens early and throughout the budget cycle. Logistical feasibility limits the system to local government choices, even though one would expect these to be the governments in which regular contact between

---

43. The New England town hall may represent the ideal for democratic participation: all voters gather in a meeting to make the fiscal decisions for the year by popular vote. Transaction costs prohibit this model for larger governments.

44. New York City has recently (Fall 2011) implemented a participatory budget project by which capital project funds have been allocated to certain city council districts, with the intent that neighborhood assemblies will decide how to spend the money. Choices will be made by self-appointed volunteer action. This apparently is more democratic than the representative electoral process.
government and citizens is already greatest. Even here, participation is modest, however: in Porto Allegre, 40,000 participants out of a city of 1.3 million, a participation rate of 3.1 percent. How this modest participation improves on the principal-agent philosophy of elected, representative government is not immediately apparent.

Along these lines, another development in budget processes is also of questionable value to the principle of producing fiscal results consistent with the public welfare. This is the formal inclusion of “civil society organizations” into the budget process. These are self-appointed, narrow-interest/special-interest groups and have little more likelihood of working in the general public interest than, say, Goldman Sachs. They have an axe to grind in the process and blinders in terms of the contributions to the public welfare of uses of scarce budget resources outside their narrow interests. Indeed, Goldman Sachs is working to serve the general interest as reflected by customer demand far more transparently and more generally than the civil society organizations (CSOs). The electoral process may have deficiencies, but it is unlikely that decisions by elected representatives are more divergent from the overall public interest than those of self-appointed interest groups.

Getting public views into the budget process early, when the program proposals are being developed, certainly stands to improve the responsiveness of government to the public interest. It certainly promises greater value than getting public views only in a budget hearing, long after fundamental choices have been made. But the process by which agencies develop programs for the executive branch that will be reviewed and approved by elected representatives almost certainly provides for more balanced responsiveness to the general welfare than would any effort to build what claims to be a complete participatory process. These “participatory processes” are often no more that institutionalized self-interested access.

Mandates—More Hidden Federal Spending. Federal mandates that require particular actions by state or local governments or private entities through laws, rulings, regulations, or whatever without providing financing to carry out those requirements has considerable political allure for federal lawmakers: they get the credit for the benefits of the program without having to finance the efforts. Federal retrenchment and consolidation provides a potent stimulus for mandates: others must bear the cost of implementing a federal objective. Mandates in the United States increased substantially in the 1980s as the federal government significantly constrained its domestic spending.45 By 1989, mandates had become an important substitute for federal spending in implementing federal policies. Because federal fiscal consolidation seems particularly likely in the current environment, even as public problems continue unabated, mandates may gain greater attractiveness.

State and local governments regard mandates as an insidious infringement of their fiscal sovereignty and a violation of basic principles of American fiscal federalism.46 They also


46. They protest even as states apply mandates to local governments and both state and local governments apply mandates to private entities.
represent a considerable source of political inefficiency and inequity: a mandate allows politicians at one level of government to receive credit for a popular policy while lawmakers at another level must find funding to pay for the policy. Such an imbalance between who bears political cost and who receives political benefit is unlikely to produce sound public decisions. This approach can be particularly attractive, of course, when the federal establishment is unwilling to raise taxes or cut other spending to deal with the new endeavor. Over the years, states have complained about federal mandates, local governments have complained about state and federal mandates, and private entities have complained about all sorts of mandates. In some respects, mandates are like special conditional grant programs—programs that have conditions, that provide no financing (a matching rate of zero), and that are not voluntary. It is no surprise that state and local governments would complain about those terms, even when programs may be in the national interest.

Public Law 104-4, the Unfunded Mandates Reform Act (UMRA) of 1995 provides some control of federal mandates. UMRA’s intent was to improve transparency by requiring cost estimates of Congressional intergovernmental mandates and by encouraging that they be funded. The law required Congressional Budget Office estimates of the cost of federal mandates placed on state and local governments and the private sector as legislation emerged from committees and it provided for a point of order objection (and thus require an explicit vote on the mandate) for mandates that exceeded a cost threshold or that lacked the appropriate CBO estimate. UMRA intended to make mandate costs more apparent and to make their adoption more transparent. However, the process only applies to certain statutory direct orders and many topics are excluded; including appropriation bills, floor amendments, and conference reports. These exclusions and the lack of a requirement that mandates be funded results in a continued significant fiscal impact at the state and local levels due to unfunded federal mandates: Major sources of this fiscal impact include Clean Air Act, Clean Water Act, Homeland Security Act, Individuals with Disability Act, No Child Left Behind, Patient Protection and Affordable Care Act, and Healthy, Hunger Free Kids.

The CBO annually reviews mandate proposals. Its 2011 report found that only 13 new laws during the first 15 years of the act had costs above the cost threshold ($70 million for 2010, inflation adjusted over time) for CBO mandate reporting. Of course, even with this added transparency, smaller mandates fall outside UMRA requirements and the

---

47. Posner points out that UMRA dealt with only statutory direct orders and that there are many other forms of “coercive federalism” that the federal government has at its disposal. [Paul Posner, “The Politics of Coercive Federalism in the Bush Era,” *Publius: The Journal of Federalism* 37, no. 3 (2007): 390–412.]
50. States, school districts, and the National Education Association sued for full funding of the No Child Left Behind program requirements but were not successful.
overall mandate cost impact continues to cause great consternation among subnational
governments. Still, there is evidence that UMRA has lowered the scope and incidence
of unfunded mandates by forcing legislative reconsideration and/or amendment.52 This is
exactly what UMRA transparency should do. Transparency may not directly stop unfunded
mandates but it should make their cost more apparent, help fuel more considered debate
and assign political responsibility, and that might reduce the scale and scope of mandating.

Greater General Public Transparency. Budget transparency may be defined as the pro-
vision of easy public availability of information about the government’s decision-making
procedures, its operations, and its finances. The information should be provided in a sys-
tematic and timely manner, the information should be freely available, and the information
should be usable by all government officials, the public, and the media.53

Transparency is a critical contributor to democratic governance. As de Renzio and
Kroth argue, “Fiscal transparency is increasingly seen as an important precondition (em-
phasis added) for effective governance, improved economic performance, and prudent fiscal
policy, resulting in lower deficits and debt accumulation. In addition to generating economic
benefits, fiscal transparency also functions as a political expression of democratic govern-
nance, giving citizens and taxpayers information that they are entitled to – and that they
can use to hold their governments accountable.”54 A number of countries have placed a
fiscal transparency requirement in their basic budget process law. The United States is not
among these countries, but the American political system appears to demand fiscal informa-
tion and, as a result, governments at all levels provide significant information in an easily
accessible fashion.

Budget processes of recent decades have dramatically expanded availability of operating
and financial information and plans and provided that material at no charge to the public
and the media. Not many years ago, documents were paper, access to copies was difficult
(both physically and procedurally), and searching them for information about almost any
topic was tedious. In that era, on the February day that the Executive Budget of the federal
government was released, long lines of assistants, interns, volunteers, and so on would form
outside the Government Printing Office to purchase the shopping bag full of the several
volumes of the budget for Congressional offices, government agencies, lobbyists, the news
media, and others—and it was an exciting day for academics when their copies would arrive

52. Theresa Gullo, “History and Evaluation of the Unfunded Mandates Reform Act,” National Tax

53. There are two methods of providing financial information to the public. Reactive disclosure is govern-
ment response when a member of the public files requests and receives information. Proactive disclosure occurs
when information is made available by the government without a request being filed. The latter disclosure is
consistent with fiscal transparency.

54. Pacio de Renzio and Verena Kroth, “Transparency and Participation in Public Financial Management:
What Do Budget Laws Say?,” International Budget Partnership Research Notes, no. 1 (2011). One international
study explicitly finds a relationship between transparency and fiscal balance: Bernardino Benito and Francisco
in the mail. But now the documents of the budget are posted on Office of Management and Budget website (http://www.whitehouse.gov/omb/budget) on the day of the budget release and are immediately accessible at no charge to anyone in the world. Much of the information is even provided in spreadsheet form so that analysis is instantly possible. In many respects, this provides the standard for transparency in all budget processes. Other documents, including both those of executive and legislative branches, are similarly available.55

Many state and local governments follow similar transparency procedures for fiscal information, although they are often slower in providing information than is the federal government, they usually do not provide the historic information that the federal government provides, and they often do not provide information in a manner that is easy to search and analyze. In particular, they seldom provide information in spreadsheet format for easy manipulation. Large local governments are, not surprisingly, more likely to provide such information than are smaller ones. Given that there are more than 89,000 local governments, it is not surprising that there are many different patterns for transparency. Information that state and local governments usually provide include the executive budget proposal, agency performance information from either the budget process or separate performance measurement reports, and the comprehensive annual financial report (CAFR) from the jurisdiction. States will also frequently post appropriation bills as they pass through the legislative process, fiscal notes on revenue or expenditure implications of bills under consideration (scores), tax expenditure budgets or reports (if they produce them), revenue forecasts and tracking reports, and audit reports.

A number of states have created a transparency portal as a single place for organizing inquiries of many sorts into a unified starting point (particularly regarding state spending). Forty states provide websites that post databases with individual payment detail (essentially, a view of the entity’s checkbook) made from government accounts, sometimes in easily searchable fashion, so that the public can see exactly to whom money is being paid.56 Unfortunately, there is no explanation of what is being purchased and for what, so there is no context that would be necessary to consider the appropriateness of the payment. (It is little surprise to find that the state police make large payments to companies that sell motor fuel.) While the data are provided, the extent of its practical use is not entirely clear. The posting certainly does less good than a quality external audit and openness in the legislative appropriation process.

There is, however, an important barrier to complete and easy transparency endemic to American government. Some financial and operational reports, data, and legislation

55. While Congressional committee reports and reports from the GAO and the CBO are easily available, that is not the case for reports from the Congressional Research Service. There is no general access to its reports but some become available through informal means.
56. Benjamin Davis, Phineas Baxandall, and Jeffrey Musto, Following the Money 2011, How the 50 States Rate in Providing Online Access to Government Spending Data (U.S. PIRG Educational Fund, March 2011). Local governments in many states have published a regular listing of all their payments for years, so this level of transparency is not completely novel, although the easy access is. It is not clear that these listings have made local governments more responsive or less corrupt in their operations.
emerge through the executive branch of government and other such information emerges through the legislative branch. The branches, even in periods of considerable cooperation, maintain their independence and few legislative entities are likely to provide their information through a transparency portal operated by the executive branch and vice versa. Getting complete fiscal information about a state (or the federal government) will necessitate investigation through at least two portals. Because local governments do not always maintain a clear separation of branches, a single portal is more likely for them—except most local governments do not have available the variety of fiscal and operating information available from other governments and seldom provide a transparency portal.

Provision of information about government finances and operations is critical for a democracy. Whether the flurry of available information makes a substantial improvement in functional transparency is not clear because dumping all information can be a useful way of hiding what matters. Probably more important than providing full citizen access is providing access to the media and third-party observers who understand fiscal systems well enough to locate, analyze, and summarize the implications of the information and providing a quality post-audit of government operations.

Because there are no standard structures or revenue/expenditure classifications across states or localities, comparisons across jurisdictions is complex and, unless the analyst is aware of classification practices, can lead to erroneous conclusions simply because the analyst does not understand what transactions are recorded where in the financial reports. Cross-jurisdiction comparisons are even more complicated because information is not maintained in comparable sites across jurisdictions (e.g., tax expenditure budgets may be maintained by the budget agency, the revenue department, the legislative analysis agency, the governor’s office, or elsewhere, depending on the choice of the state) and those locations may change from one year to the next. While regular users of information for a particular state can accommodate over time, that is a problem for cross comparison work and even regular users can be frustrated when locations change. Increased speed, accuracy, and availability of information is a vital ingredient to effective transparency, however, it is no less vital than informed consumption. Informed consumption is buttressed by comprehensive reporting and auditing. Understanding the veracity of provided information is critical and volume cannot substitute for veracity and independent verification.57

**Trying to Get Better Results from the Budget Process: Some Continuing Failures**

The American budget process is marked by some important, even critical, failures. The major failures are generally in respect to macrocontrol of expenditures and budget deficits. These are important because they involve questions of fundamental fiscal sustainability, a crucial control issue for every government and a first responsibility of any budget process.

---

57. It has become common for governments across the world, particularly in recently transitioned economies, to report ever increasing amounts of information to the public through web portals. It is far less common for these reports to have been independently verified.
The Challenge of Automatic Spending: Budgeting by Autopilot, Entitlements. Fiscal control in the American system entails a process of periodic, usually annual, provision of budget authority for agencies to use in the provision of services approved in law. Annual appropriation is the normal device for presentation and review of executive programs, approval of programs by the legislature, control during budget execution, and eventual audit and evaluation. Appropriation to budget accounts is the heart of legislative power of the purse. Entitlement programs—programs that provide automatic payment to all those who qualify for a program without the control associated with a fixed program appropriation—constitute a major exception to that control framework.58 Allen Schick seems to realistically (if not somewhat pessimistically) suggest that “Entitlements will be a problem as long as budgeting is practiced . . . “59 Payment by entitlement short circuits the spending process and jeopardizes regular fiscal discipline. Legislators have ultimate control over entitlement spending but only through specific legislative action to change the law that defines eligibility or the terms defining what beneficiaries will receive. Change is possible but difficult in Congress. Beneficiaries build political forces to retain benefits and there is considerable Congressional bias toward general inaction. A legislative change to control an entitlement is much harder than doing nothing. The inertia is magnified when the bulk of the return from fiscal discipline lies in the future, possibly beyond the legislative term of the legislator, while the political cost of the action resides in the present. It is no wonder that the American federal government has experienced great difficulty in dealing with the entitlement spending—and that state and local governments have generally tried to avoid that spending mechanism.

Entitlement spending (the federal budget classifies such spending as “mandatory”) consists primarily of spending on Social Security (the income safety net for the elderly), Medicare (health insurance for the elderly), and Medicaid (the medical program for low income persons). Total mandatory spending plus net interest on federal debt (also outside the annual appropriation process) accounted for 61 percent of total federal outlays in 2010, up from 41.7 percent in 1971 and 32.5 percent in 1962. In 2010, Social Security, Medicare, and Medicaid amounted to 55.3 percent of federal outlays.

This spending is both big and growing. Figure 1 shows how the big three entitlement programs have grown as a share of the U.S. economy from 1971 through 2010. These three programs have expanded from 4.3 percent of gross domestic product in 1971 to 10.3 percent in 2010, with Medicare spending growth being a particularly significant source of the increase. Growth has been so substantial that there are concerns that growth in healthcare spending for the aged will crowd-out other government spending. Medicaid spending, while not as large as either Social Security or Medicare, has similarly increased significantly and, because it is a shared federal/state program, that growth has significant implications.

---

58. In regard to their permanence and absence of annual appropriation and review, they share control issues with tax expenditures. And they are similarly popular with their beneficiaries.
for state government finances. Medicaid has been the fastest state spending component over the past two decades and promises to continue to be so unless the system changes.

These biggest two entitlement programs provide assistance for the elderly. They have been successful at removing the near-automatic link between being elderly and being poor and at providing greater dignity to the elderly. However, longer life expectancy and higher cost of medical technology and medications combine to create great uncertainty about the fiscal prospects for these programs (particularly the health programs) and, because they are such a sizable component of total federal spending, for the finances of the federal government itself. While relatively minor revisions in the structure of payments into the Social Security system fund, and in the benefits being paid out, could restore the finances of that program, there remains no clear solution to the continuing growth of the Medicare or Medicaid systems. The Budget Enforcement Act of 1990 (and versions extended through 2002) provided a control on expansion of entitlement program benefits by establishing a PAYGO requirement in which any legislation that improved benefit formulas had to be accompanied by legislation that would pay for that expansion. That may have constrained upward shifts in the entitlement spending profile, but it certainly did not stop the expansion of this spending. How the fiscal implications of this entitlement growth can be corrected remains unclear. This, however, is not a question that can remain unanswered for too much longer. The absence of action is action in itself. The continuing failure to address these issues reduces future flexibility.
The Great Failure: Absence of Fiscal Discipline. The innovations discussed previously have sought to develop and present information to fiscal decision makers and to alter disincentives to inefficient choices. Their record of accomplishment is mixed but there has been considerable progress in terms of providing information useful for reasoned decisions. The process is driven by politics but that is to be expected. The hope is that transparency and appropriate information can guide even political choice.

The great failure is in regard to fiscal discipline. In the period since 1960, the federal government has raised as much revenue as was spent in only 1960, 1969, 1998, 1999, 2000, and 2001. If one looks at “on budget” operations only (generally excluding the social insurance trust fund operations), there are surpluses only in 1960, 1999, and 2000. While one might expect a deficit for a national government in periods of economic recession as both the automatic stabilizers and discretionary fiscal policy seek to restore economic growth, the bulk of that period has been one of economic expansion: only 15 percent of the months from 1960 through 2010 have been recession periods. There is no economic logic to support that deficit record. Figure 2 traces the federal deficit as a share of gross domestic product from 1960, to clearly identify this failure of fiscal discipline. It reflects the fact that national politicians much prefer to spend than to raise money, a reflection of the fact that individuals would much prefer not to pay for anything if it is possible to get it without payment. The half-century has been a reflection of WalMart philosophy by the federal government: cut the price so customers pay as little as possible. It works marvelously for the private sector because if a person does not pay for a service, the person will not receive that service. It does not work for the public sector because, for most services, receiving services is not linked to paying for them. For voters, a politician who promises to cut taxes is always preferred because surely someone else will pay for services and any services cut will be those that matter to somebody else. This is particularly the case at the national level because there is truly no link between what payment a particular taxpayer makes and what federal government services that taxpayer receives. For someone else to pay is particularly beneficial to an individual and possibly the best prospect of all is for payment to be made years in the future. The cloaked reality is that this future payment will come due and it will negatively affect living standards as real resources are transferred out of the U.S. economy, distorts choices made within the economy, and constrains the capacity of the federal government to respond to current service needs of the populace. This cloak has resulted in persistent

60. Of course, the absence of entitlement control makes a significant contribution to the overall fiscal discipline problem.

61. The shock of consecutive surpluses (1998–2001) lead to estimates that the federal government would be totally debt free by 2011. This created such a concern that the Government Accountability Office was asked to report on consequences of having the federal government repay all its debt and on how other countries had managed to operate when they were without debt. This would have been uncharted territory because, from its beginnings until the present, the federal government had been debt free only for a short time in the mid-1830s. Needless to say, there was no reason for these concerns about a debt-free U.S. government.

62. It is sometimes argued that the absence of a capital budget at the Federal level in the United States partially obscures the deficit and debt picture. While this is the case, even liberal classification of national government spending as investment related do little to improve the 50-year track record.
deficits and, as a result, the federal debt has continued to increase. Debt held by the public in the middle of 2011 equaled 65 percent of gross domestic product, a level higher than experienced in any year in the history of the nation, save for at the end of World War II.\textsuperscript{63}

As Herbert Stein, a wise economist who was an advisor to President Nixon, once observed, “If something cannot go on forever, it will stop.” Stein’s Law of Fundamental Unsustainability makes clear that deficits forever—and the ensuing accumulated debt burden—must stop, if for no other reason than that the debt service requirements will choke off the capacity to provide current services. What the American federal government has not discovered is a way to stop the perpetual deficit. It needs the flexibility to run a deficit during recessions but not to allow that to happen during expansions. Policymakers have tried to put controls in place. A listing of big structural attempts to constrain the perpetual deficit includes the following\textsuperscript{64}:

1. \textit{The Budget and Accounting Act of 1921}: The law that prescribed the development of the executive budget by the president was driven heavily by the desire to control budget deficits in the aftermath of World War I. Previously, attention was solely on

\textsuperscript{63} The gross debt ratio is approximately 100 percent, but it is less relevant for gauging economic significance because so much debt is owned by entities and accounts of the federal government itself. Debt held by the public removes that debt from the calculation.

\textsuperscript{64} It does not include smaller efforts like those to permit a presidential line item veto, to institute limited PAYGO requirements, or to prevent expenditure earmarks. These range from unconstitutional to ineffective.
Congressional appropriation to meet individual department funding requests, not on spending plans as a whole.

2. The Congressional Budgeting and Impoundment Control Act of 1974: The law provided for a Congressional budget with approved expenditure ceilings, revenue floors, and maximum deficits, thereby getting Congress into the deficit control business. The law created the first Congressional budget process. Previously, Congressional responsibility lay solely in appropriating. In recent years, Congress has often failed to pass a Congressional budget.

3. The Balanced Budget and Emergency Deficit Control Act of 1985: The law established formal deficit targets for future years with formula sequestration (across-the-board spending reductions) applied if the targets were violated. After subtracting certain safety net programs, the required sequestration amount would be taken half from defense and half from domestic programs. Because defense spending was considerably greater than remaining domestic programs, the percentage reduction was much greater for domestic spending.

4. The Budget Enforcement Act of 1990 (reenacted through fiscal 2002): The law established firm outlay ceilings on discretionary spending and the PAYGO requirement that any legislation that enhanced entitlement payments or reduced revenues be accompanied by a deficit-neutral financing mechanism.

5. The Budget Control Act of 2011: The law established the Congressional Joint Select Committee on Deficit Reduction with a short deadline for producing a program of deficit reduction of at least $1.5 trillion over a 10-year horizon with the program to be voted on by Congress without amendment, up or down. If the Committee cannot produce such a program with at least $1.2 trillion in reductions, across-the-board sequestration would apply, divided equally between security and nonsecurity programs (some nonsecurity entitlements exempted).

The record previously reported in Figure 2 summarizes the failure of these efforts. While it may be possible for some to argue that, without the budget controls in place, the deficit

---

65. Under this act, Congress approves the budget resolution, often referred to as the Congressional budget, which establishes various ceilings and floors on appropriations and revenue and some have mistakenly regarded this as passage of the budget—in the sense of providing spending authority to governmental units. That is not the case, although it would be in a parliamentary system. Possibly the confusion between American and European government structures creates the confusion. Providing spending authority to agencies requires action by both the Congress and the president. The budget resolution is much briefer than the president's budget or the actual appropriation bills and Congress does not always manage to approve one.

66. The law emerged from a Congressional dispute about increasing the federal statutory debt ceiling. The dispute was unusual, in that Congress had already approved the spending that had caused debt to reach the ceiling, so the options were to allow the U.S. Treasury to borrow to meet cash needs for paying the bills from those purchases or to default on legal obligations. The ceiling was finally increased so that the bills could be paid. But a sufficient number of members of Congress suggested that default might be a reasonable option that the rating agency Standard & Poor rightly downgraded federal debt from AAA to AA+, reflecting some risk that debt service might be delayed. If there is such tangible risk, the debt ought not enjoy the highest rating.
would have been even worse, the only one of these structural efforts that appears to have had the desired result in the post-1960 era was the 1990 act—and it is not easy to distinguish among the impacts of the act, a long economic expansion, and some tax increases in the early years after the passage of the act in producing that record.67

What is clear is that the federal government, having attempted better fiscal control by strengthening the executive role in the budget process, then having attempted control by strengthening the legislative role, then trying to control deficits directly, and then trying to constrain spending, still has not discovered the formula or process that will consistently (or even regularly) provide aggregate constraint.68 When ceilings or controls would constrain in ways uncomfortable to Congress, Congress usually changes the ceilings or controls. The federal government seldom even manages to pass its appropriation legislation before the beginning of the fiscal year. The last year in which all appropriations have been enacted before the start of the fiscal year was 1997. There were 21 continuing resolutions for fiscal 2001 alone.69 Fiscal year 2011 required eight.

The record is not so bad, however, for all governments in the United States. Throughout the years since 1960, the state and local government sector has been usually in surplus, thus somewhat offsetting the macroeconomic impact of the continual federal deficits. This history is shown in Figure 3. These governments must be more wary about their finances because they have no lender of last resort to support them and their citizenry have less capacity to shift the burden of government spending to others. Most of the states operate under some form of legal balanced budget requirement, a requirement fairly easily and regularly avoided, but it does provide an atmosphere for fiscal propriety. If these governments spend, they must find the finances and they have done this far better than has the federal government.

The various efforts to make the federal budget process produce more efficient results have not produced returns for aggregate spending. How to apply macrofiscal control, in spite of the years of quest, remains a mystery for the federal government. The basics of producing fiscal discipline are clear: more revenue and less spending in some combination. But rather than work on the difficult fiscal truths, Congress continues to put the blame on the process, even trucking in worn out panaceas from the past, like zero base budgeting systems and federal biennial budgeting. As Stan Collender summarized, “... when Congress can’t or won’t do something about the budget, it often tries to change the subject by instead doing something about the budget process. The implication is that it’s the process rather than the

67. The 1921 Act may also be seen as having an impact on fiscal control. From 1920 through 1930, the federal government always had a surplus, a marked contrast with 1917–1919, years in which substantial deficits occurred. Of course, the end to World War I spending, combined with revenues from the newly enacted individual income tax and economic expansion, made the fiscal challenges somewhat less imposing. But the peace dividend could have been spent, so credit is surely due something, possibly the 1921 Act.


Representatives and Senators who implement it that is to blame for the bad or nonexisting decisions. Just change the process, they say, and it will stop me from spending more or cutting taxes again.”70 Process will not change the basic need to “just do it.” The federal government has gotten a pass because the world has been a ready purchaser of federal debt. If easy debt sale would become difficult, the required restructuring of government operations and finances would be expected to have extreme consequences for the American public.

CONCLUSION

Public budgeting continues to balance rational decision making and pure politics. That is endemic in a process that makes choices about government services/public goods in a democracy. No super formula will emerge to make sensible public expenditure choices. The hope is for processes, structures, and information that will move choices toward the best interests of the public, the beneficiaries of government services and the people who will

---

pay for those services. Reforms to public budgeting over the past half-century in the United States have a mixed record.

The record shows improvement in regard to providing better information, better classification of information, identifying the implications of fiscal instruments otherwise concealed, bringing the citizenry more intimately into the budget process, and making fiscal information more transparently available to everyone. The record is not so good in regard to controlling spending for entitlements or to providing fiscal discipline for fiscal sustainability. The achievements are more impressive in respect to problems of internal management than in terms of ultimate fiscal discipline and long-term fiscal sustainability. The unanswered question is this: are the areas in which the record is not good the product of budget systems and processes, a problem that experts in fiscal systems can ultimately repair, or is the record the product of the political structure, a problem that is beyond the capability of budget systems? Irrespective of the answer, it appears that the balance has yet to be achieved. The answer, itself, is critical to viability of the long-term outlook and the record makes clear that processes do not substitute for political will. Maybe Ms. Tuchman's pessimistic view is right. Irrespective, it is to these issues that we should turn our attention.

NOTES