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**MTEF in US, UK and Other
Countries**
**Medium-term Perspectives in Budgeting :
The U.S. Case**

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Medium-term Perspectives in Budgeting: The U.s. Case

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1. Introduction

In the United States, medium-term aspects of budgeting are an integral part of the annual budget process, and as such are somewhat difficult to disentangle from the annual budget process. The following paper will outline the major rules and process in multi-year budgeting, covering both the executive and legislative budget processes.

After presenting the necessary institutional background for understanding the U.S. public sector, the evolution of budgeting, and key actors, the paper turns to multi-year macrofiscal forecasting in the annual budget process. The paper then turns to sectoral allocation of resources, including conflict resolution mechanisms. The paper then briefly addresses the question of policy content and ownership of the executive budget, the role of the legislature, and in-year spending ceilings. The paper concludes with a summary assessment of multi-year budgeting in the U.S. and some lessons learned.

2. Background

Governmental structure and public finance roles.

The United States has a presidential system of government. Power is separated between three branches of government (executive, legislative, judicial).

- The legislature (Congress) has the ultimate authority over spending, granted to it under the Constitution.¹ Providing authority to spend is exclusively a legislative power. The executive branch may not spend more than the amount appropriated, and it may use available funds only for the purposes approved by Congress. In theory, the Congress could develop a budget without any presidential input, although this has not been the case in modern history. It is also important to point out early that while the President does propose one comprehensive budget, the Congress enacts the budget through 13 separate appropriations bills or votes, roughly corresponding to function.
- The President and executive branch have important roles in the budget process by virtue of (i) proposing the budget first, thus setting the agenda; (ii) having the detailed spending information needed to prepare good budgets; and, (iii) the President has Constitutional power to approve or veto legislation (including the 13 appropriations bills).

Evolution of Budgeting.

The relationship between the executive and legislative branches over budgeting and control of public finances has developed gradually over the 200 years of the country's

¹ "No money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law ..."

history, with the balance of influence over spending shifting between the two branches. Until 1921, spending agencies submitted budget requests directly to the Congress. While Congress had preeminent authority in spending decisions, it was very dependent on the budget estimates and requests submitted by spending agencies. As the complexity of the public finances expanded, this uncoordinated approach placed too high a burden on Congress to prepare a coherent fiscal position, and also provided too little formal room for Presidential policy in advancing a coherent executive fiscal position.

The Budget and Accounting Act of 1921 established the executive budget process, requiring the President to prepare and submit a comprehensive federal budget to Congress annually. The Act also created the Bureau of the Budget (renamed the Office of Management and Budget (OMB) in 1974) to support the President in carrying out coordinating the executive branch budget. OMB's assists the President in overseeing the preparation of the Federal budget and also supervises budget execution/implementation. OMB evaluates the effectiveness of agency programs, policies, and procedures, assesses competing funding demands among agencies, and sets funding priorities. OMB ensures that agency reports, rules, testimony, and proposed legislation are consistent with the President's budget and with Administration policies. In addition, OMB oversees and coordinates the Administration's procurement, financial management, information, and regulatory policies. And, not a small task, OMB is in charge of general management oversight and reforms in the public sector.

Along with OMB, the Council of Economic Advisors and the Treasury Department assist the President by providing economic projections and revenue estimates.

With the passage of the Budget and Accounting Act, influence over budgeting shifted to the executive branch. This tendency generally continued until the early 1970's, when Congress began to reassert its role. By the mid-1960's, the size and complexity of the Federal budget had grown significantly. Some programs from the Depression (Social Security) and War on Poverty (such as Medicaid and Medicare) were large and growing, and were entitlement programs not governed by the annual budget. To manage these programs required more than an annual focus in the budget.

In 1970, Congress passed the Legislative Reorganization Act, requiring more budgetary information from the President, including that the budget cover the budget year and four additional years.

In 1974, Congress passed the Congressional Budget and Impoundment Control Act. The Act further reinforced the congressional budget role establishing important tools for managing its handling of the budget. The House and Senate Budget Committees were created to coordinate congressional consideration of the budget, and the Congressional Budget Office was established as a source of nonpartisan analysis and information, including providing an alternate economic forecast for the Congress. The law also established a specific timetable for action on the budget and a concurrent budget resolution on budget aggregates (a legislative device that does not require Presidential approval, but guides legislative action on the budget).

CBO's role is to provide the Congress with objective, nonpartisan analyses on economic and budget decisions, and with information and estimates for the budget process. CBO prepares analyses and estimates relating to the budget and the economy, and presents options and alternatives for the Congress, but does not make policy recommendations. CBO helps the Congress formulate a budget plan, stay within that plan, and assess the impact of federal programs.

Congress also has the Congressional Research Service, which provides research on specific topics for Members of Congress, as well as the General Accounting Office - the Supreme Audit Institution or external audit body - that provides evaluations of programs in addition to audit reports.

To understand the U.S. budget process generally, including multi-year budgeting, it is important to understand both the executive and legislative budget processes.

3. Foundations of Budget Preparation: Macroeconomic

Executive Branch Macroforecasting, expenditure forecasting and fiscal envelope.

Formal econometric models are not used in preparing economic forecasts of key economic variables for use in the President's Budget. Professional economists in OMB, Treasury, and the Council of Economic Advisors (the 'troika') focus on trends in six key variables:

- (1) real GDP growth;
- (2) CPI (higher CPI lowers indexed tax revenues and increasing budget spending via automatic cost-of-living allowances, etc.);
- (3) GDP price index (higher GDP growth increases tax revenues);
- (4) unemployment;
- (5) short term interest rates (90-day Treasury Bill rate); and,
- (6) long term interest rates (10 year Treasury bonds yield).

Some attention is also paid to projected income distributions, which will effect tax revenue projections (profits versus wages). Policy discussion focuses more on the wedge between the GDP price index and CPI than on each measure itself. The CPI generally outpaces the annual rate of GDP growth. The rule of thumb: the wider the gap between the two measures, the worse for the Federal Budget.

In debating the appropriate level of key economic variables for use in the President's Budget, participants do receive other forecasts as benchmark levels (several academic private sector estimates, as well as estimates by international organizations).

The existence of these alternate estimates is thought by some to place constraints on the extent to which political officials might manipulate economic estimates beyond reason in order to support their political agenda via the budget. Regardless, alternate estimates do provide substantive grist for the debate.

Incremental Changes to Official Forecast. The process of forecasting is really an incremental one. Analysts begin with the most recent official forecast, and then proceed to review the key variables in light of trends in the economy. The current forecast is modified where a consensus is reached among OMB, Treasury, and CEA on necessary changes.

Generally, only first-order effects on the economy are considered. Professional economists in the executive branch are loath to attempt second-order estimation (e.g. the effect on tax revenues of a change in tax laws which change behavior).

Forecasts are updated every six months. Executive branch economists constantly monitor key statistical releases on economic activity, and are always thinking of the implications of the news for the official forecast.

Process: from Policy Approval to Budget Production.

Once staff of the troika have finished their review and developed opinions on necessary revisions, senior policy officials meet to discuss the forecast. Eventually, the Chairman of the CEA, the Director of OMB, and the Secretary of Treasury must agree on the final numbers before they can be used to develop the Budget.

Policy consensus must be reached for economic forecasts. The key policy officials involved in fiscal policy must reach some consensus on broad policy directions as they consider the economic forecasts. (In the 1980's, this policy review often resulted in more optimistic estimates, which led to the appellation 'rosy scenario' forecasting based on economic theory dubbed 'voodoo economics'.)

Generally, the key policy officials will include the troika, as well as senior administration officials (possibly the President, Vice-President, Chief of Staff, and other White House political staff). These arrangements have varied by Administration. Under President G. H.W. Bush, domestic and economic policy were the domain of two very influential officials, the Chief of Staff John Sununu and the Director of OMB Richard Darman.

Under President Clinton, a formal advisory body called the National Economic Council (NEC) was established in 1993 to provide advice to the President and build consensus among key policy officials. The Council was composed of the President, Vice-President, seven domestic Cabinet Secretaries, The Secretary of State, Director of OMB, Chair of the Council of Economic Advisors, National Security Advisor, Assistant to the President for Domestic Policy, and Secretary of Defense.

The important point to bear in mind is that there were vehicles for achieving policy consensus within Government. As of 1993, these have become more formalized in the NEC. This would be roughly analogous to Cabinet consensus in Parliamentary systems.

From forecast to budget preparation.

Once approved, CEA staff use a private sector econometric model (dubbed the 'black box') to produce somewhat greater detail for the forecast, especially consumption, investment, and export components of the national accounts. Also, greater detail in terms of income distribution is sought for use by Treasury in forecasting revenues. While based on an econometric model, the black box really is an accounting device or reverse model, where key variables are entered, and consistent details are generated. The black box assures that basic national accounting identities are observed to produce a generally consistent set of supporting detail for the approved policy variables. This black box output detail is then given to OMB and Treasury for production of further detail.

The U.S. Treasury is responsible for tax-based revenue forecasts, while OMB generally estimates user fees and similar non-tax revenues. Treasury has formula based on historical tax collection records of estimated revenues given the basic national account and income distribution data.

OMB has simple formulae based on recent historical trends and simple regression models which provide greater detail on inflation, a wider array of interest rate estimates, etc. (e.g. Medical inflation is, on average, 2 % greater than the CPI estimates). These more detailed estimates are then provided to the executive branch agencies for use in estimating future year or budget year costs. Agencies use estimates of inflation and possible pay increases in calculating their budget requests (policy) and current services estimates.

The set of variables which the Federal Executive Branch has determined are necessary for producing the budget are listed in Box 1.

Expenditure Trends.

Many of the routine budget tasks, such as applying a pay inflator to base year pay and projecting into future years, are automated in the OMB budget database system. The appropriate economic estimate is fed into the OMB computer, and the relevant accounts are directly updated.

Box 1. Economic Variables used in developing the President's Budget

Basic Budget Data

1. Pay and Personnel-related costs for civilian employees
2. Pay and Personnel-related costs for military personnel
3. Non-pay costs for discretionary programs

Alternate Price Measures

4. GDP Deflator (chain-weighted);
5. CPI-W (quarterly and annual);
6. states-local expenditure Index;
7. Federal non-pay, non-defense expenditure deflator;
8. Federal non-defense non-residential structure construction;'
9. private construction non-residential structures.

Revenue-related estimates

10. GDP (quarterly and annually)
11. GDP Price Index (quarterly and annually)
12. Civilian Unemployment (quarterly and annually)
13. Corporate profits
14. Goods imports
15. Personal Income, broken into wage and non-wage income (interest income, dividend income, rental income, proprietors' income) (quarterly and annually)
16. Civilian Labor force (quarterly and annually)
17. Treasury bill rates (91, 182, and 364-day rates (quarterly and annually)
18. Treasury notes and bonds (2,3, 5, 7, 10, and 30-year rates) (quarterly and annually)
19. Prime Rate (quarterly and annually)
20. LIBOR (quarterly and annually)
21. AAA State & Local Bond Rate (quarterly and annually)
22. Mortgage Rate (quarterly and annually)
23. Energy Prices (imported and domestic oil, coal, natural gas, and a hybrid gas & oil index) (quarterly and annually)
24. Housing starts, mortgage originations (existing and new homes), average single-family home

In early budget discussions at the macro level, OMB uses the most recent approved budget information (congressionally-approved budget), adjusted for information on implementation of the current budget, to make projections of spending trends. Several concepts unique to the U.S. budget system need to be understood: baselines; discretionary spending; and, mandatory spending.

Baselines; discretionary spending; and, mandatory spending.

Baselines provide the President and Congress with a framework for making and enforcing budgetary decisions, serving as a benchmark. OMB and CBO baselines project federal spending, revenue, and budget surplus or deficit amounts that would occur if existing budget policies were left unchanged. The rules for calculating the baseline are set in law.

Discretionary spending applies to programs whose funding must be provided annually in the budget. **Mandatory spending** encompasses entitlements to individuals and other programs whose spending is controlled via separate legislation, and not subject to the annual budget.

Mandatory spending and receipts are generally assumed to continue at the level prescribed by existing law. Discretionary spending is assumed to continue at the level of the current year's spending level, adjusted to reflect certain assumptions. The projections for mandatory spending, receipts, and discretionary spending are based upon economic assumptions (e.g., economic growth, inflation, and unemployment) and technical assumptions (e.g., demographic and workload changes).

Executive Branch and Federal Reserve Forecasting: no formal coordination. There is no formal or informal discussion between executive branch staff and staff at the Federal Reserve on economic forecasts. However, Washington, D.C. based economic professionals do have a general idea of what others in their field are thinking.

The Federal Reserve has their own model, and do not share their forecasts. The Federal Reserve MPS model does, however, have some close similarity to the private sector economic model the executive branch uses for obtaining more detailed estimates. However, since the President's Budget is released publicly, including the basic economic assumptions underlying the budget, the Federal Reserve has the basic information on Executive Branch economic thinking to use in their own forecasts and decision-making.

Congressional Budget Office Forecasting.

Once the President's Budget economic forecasts are released with the President's Budget, the Congressional Budget Office makes their own set of estimates. CBO is thought to follow a similar consensus and incremental approach to forecasting. However, CBO does invite private and academic forecasters in the present their views of the economy. Also, CBO, being a single agency, has a somewhat easier time in arriving at consensus estimates, versus the executive branch with three separate agencies involved. CBO does subscribe to some private sector forecasting services, though which ones, and how these private forecasts are used in developing the official CBO forecast, is not known.

OMB and CBO do have some different assumptions and conclusions on income distribution and some key variables. Particularly with regards to income distribution, OMB has tended to estimate greater GDP growth and greater corporate profits - which are highly taxed - and hence greater Federal tax revenues, than CBO has projected.

Because of lingering suspicion over OMB economic estimates after President Clinton's inauguration, the President declared that CBO economic assumptions would be used instead of OMB's. While only lasting for a short while, the President's decision did serve to remove different economic estimates as a source of budget debate, and also chastened the troika to produce more pragmatic estimates.

Publication of the economic estimates in the President's Budget also allows close scrutiny of the soundness of the estimates.

Revenue forecasting.

As noted above, within the executive branch, the Treasury has general responsibility for tax policy, including estimating the effect on revenues of changes in tax policy.

Most of the laws establishing the federal government's revenue sources are permanent and continue year after year without any additional legislative action. Revenue legislation may be considered in the congressional budget process when President proposes changes in taxes.

Debt.

Within the executive branch, the Treasury also has responsibility for debt policy. Because of the size of the economy, debt policy has generally not been a major focal point in budget debates, except for the 1990's under President Reagan, and again now with the rapid increase in deficits. Most of the focus has been on taxes (revenues) and spending, with deficits and debt a residual. (Note that for smaller or less open economies with more limited access to capital markets, debt policy is a far greater issue.)

Perhaps the more immediate administrative issue for the Treasury in debt policy is Congressional limits on debt. The gross federal debt consists of the debt held by the public plus the debt held by government accounts. Almost all of the gross federal debt is subject to a public debt limit. The Treasury can borrow funds only up to statutory debt limit. Most gross federal debt is held by the public, though a significant amount (roughly 30 percent) is held by government accounts (primarily trust funds such as Social Security, whose surpluses must be invested in special federal government securities by law).

Congress occasionally will enact increases to the debt limit. Within the congressional budget process, the annual congressional budget resolution specifies the appropriate level of the public debt for each fiscal year covered by the resolution. In order to actually change the public debt limit, however, legislation must be passed by both Houses of Congress and signed by the President. The House of Representatives Ways and Means Committee and the Senate Finance Committee are the responsible committees of Congress for debt limit issues.

In addition to the annual budget process, debt limits are another means for Congress to control the executive branch, and force the executive to discuss debt issues directly.

A Mid-session Review is also required by the law to be sent to Congress by July 15 of each year. The Mid-session updates the economic estimates and President's Budget proposal.

4. Strategic Allocation

Sectoral ceilings.

In the U.S., sectors are termed functional classification. The President's budget classifies federal budgetary activities into functional and subfunctional categories that represent the major purposes of the federal government. Each budgetary activity of the federal government, including budget authority, outlays, tax expenditures, and credit authority, is classified into a subfunction based on the primary purpose it serves without regard to the agency or other unit responsible for it. There are currently 21 functional and 77 subfunctional categories. Figure 1 presents the current functional and subfunctional classification.

The functional categories provide a broad statement of budget priorities and facilitate the analysis of trends in related. They are not used for setting ceilings.

Indicative ceilings for the annual budget process in the U.S. are set according to the ministry (department) classification set for the budget year, and four subsequent years. Generally, OMB begins with the second year of the prior budgets' multi-year forecast, and makes adjustments for total spending trends and limits, economic or legislative changes, and also to reflect known policy preferences. A 'new policy reserve' has sometimes been set at this stage, representing a pool of unallocated resources that will be used to fund new initiatives (whether arising from the President or from ministries). In some cases these are provided to the President for information, and in other instances not, depending on the degree of interest of the President in budget issues and the degree of

delegation to staff and the Director of OMB.

(Note: While the formal President's Budget document includes the budget year and four additional year, down to the program level, over the last decade or so the Senate has included language in the budget resolution requiring ten-year estimates. The executive has generally complied with this request, submitting these estimates at a more aggregate level.)

Figure 1

FUNCTIONAL CLASSIFICATION

050 NATIONAL DEFENSE	570 MEDICARE
051 Department of Defense-Military	571 Medicare
053 Atomic energy defense activities	
054 Defense-related activities	600 INCOME SECURITY
150 INTERNATIONAL AFFAIRS	601 General retirement and disability insurance (excluding social security)
151 International development and humanitarian assistance	602 Federal employee retirement and disability
152 International security assistance	603 Unemployment compensation
153 Conduct of foreign affairs	604 Housing assistance
154 Foreign information and exchange activities	605 Food and nutrition assistance
155 International financial programs	609 Other income security
250 GENERAL SCIENCE, SPACE AND TECHNOLOGY	650 SOCIAL SECURITY
251 General science and basic research	651 Social security
252 Space flight, research and supporting activities	700 VETERANS BENEFITS AND SERVICES
270 ENERGY	701 Income security for veterans
271 Energy supply	702 Veterans education, training, and rehabilitation
272 Energy conservation	703 Hospital and medical care for veterans
274 Emergency energy preparedness	704 Veterans housing
276 Energy information, policy and regulation	705 Other veterans benefits and services
300 NATURAL RESOURCES AND ENVIRONMENT	750 ADMINISTRATION OF JUSTICE
301 Water resources	751 Federal law enforcement activities
302 Conservation and land management	752 Federal litigative and judicial activities
303 Recreational resources	753 Federal correctional activities
304 Pollution control and abatement	754 Criminal justice assistance
306 Other natural resources	800 GENERAL GOVERNMENT
350 AGRICULTURE	801 Legislative functions
351 Farm income stabilization	802 Executive direction and management
352 Agricultural research and services	803 Central fiscal operations
370 COMMERCE AND HOUSING CREDIT	804 General property and records management
371 Mortgage credit	805 Central personnel management
372 Postal Service	806 General purpose fiscal assistance
373 Deposit insurance	808 Other general government
376 Other advancement of commerce	809 Deductions for offsetting receipts
400 TRANSPORTATION	900 NET INTEREST
401 Ground transportation	901 Interest on Treasury debt securities (gross)
402 Air transportation	902 Interest received by on-budget trust funds
403 Water transportation	903 Interest received by off-budget trust funds
407 Other transportation	908 Other interest
450 COMMUNITY AND REGIONAL DEVELOPMENT	909 Other investment income
451 Community development	920 ALLOWANCES
452 Area and regional development	921-929 Allowances [Assigned by OMB]
453 Disaster relief and insurance	950 UNDISTRIBUTED OFFSETTING RECEIPTS
500 EDUCATION, TRAINING, EMPLOYMENT, AND SOCIAL SERVICES	951 Employer share, employee retirement (on-budget)
501 Elementary, secondary, and vocational education	952 Employer share, employee retirement (off-budget)
502 Higher education	953 Rents and royalties on the Outer Continental Shelf
503 Research and general education aids	954 Sale of major assets
504 Training and employment	959 Other undistributed offsetting receipts
505 Other labor services	999 MULTIFUNCTION ACCOUNT [used for accounts that involve two or more major functions]
506 Social services	
550 HEALTH	
551 Health care services	
552 Health research and training	
554 Consumer and occupational health and safety	

The ministry ceilings are indicative. OMB requests that agencies stay within the ceiling, but there are no formal sanctions for not doing so. Because the ceilings are not Presidentially-approved or sanctioned, they have few 'teeth.' Even if there were, it is highly unlikely a cabinet member would be reprimanded or dismissed for not meeting the ceiling. However, there are more informal pressures for compliance that operate more at a career staff level. In advising the Director of OMB and President, OMB staff do make note of whether the ministry complied, and by how much they were off ceiling. Further, even if the ministry does not specify where they would reduce to meet the ceiling, OMB staff will recommend where reductions should take place. So, it is in the interest of ministries to themselves identify low priorities.

Further, implicitly, there is always some question in ministry budget staff minds as to whether OMB scrutinizes their budget more closely if ceilings are ignored. (For small agencies, over which OMB has more direct influence, there is greater likelihood of compliance with the ceilings.) Regardless, ministry requests are generally within 5-10 percent of ceilings.

Conflict resolution and consensus-building.

After receiving ministry requests, OMB prepares policy papers for the President's decision. There is a well established process for decision-making, with only the most significant issues ever making it to the President's desk. Many will be made by the OMB director, and for smaller issues, by political appointees within the OMB.

After decisions are taken, the decisions are 'passed-back' to the ministries, usually around Thanksgiving (November). Ministries are given a tight deadline for reviewing and formally registering any appeal to the passback levels. This process of passback and appeals can be very contentious between OMB and ministries.

The process of resolving appeals involves direct meetings between OMB staff and ministry budget staff, and focused debate. Efforts are made to resolve as many issues as possible at a staff level, before raising the issues to a political level. Eventually, some issues may need to be resolved by the Director of OMB and affected cabinet secretary. Generally, few issues require appeal all the way to the President. Some Presidents (Ford, Carter, and Clinton) have taken a direct role in deciding appeals. Others (Nixon, Reagan, George H.W. Bush and George W. Bush.) have delegated appeal decisions to presidential aides or the OMB Director.

Through-out this process, it is the better prepared, better argued, and better documented case that tends to win out. For OMB and agency staff, the premium tends to be on data and analysis. For highly political issues, of course the political officials will take the decision and weigh many factors. Even the best analysis will not win-out against politics. But for the majority of issues OMB would deal with during this time, data, documentation and analysis are the key factors.

Out-year estimates can sometimes also be used in resolving disputes with agencies, at least for discretionary spending. There have been instances where an agency agreed to a lower increase in its proposed budget in exchange for increases in its budget for the budget year +1 or beyond. Of course, the subsequent years ceiling will be revisited in light of changing circumstances during the next budget cycle, and the agreed increase may not in fact happen.

With this in mind, OMB puts a premium on hiring the best staff, and having access to as much data as possible. It is not uncommon for OMB staff --- outnumbered by budget staff in ministries --- armed with an agencies own data, to provide critical information or data at a key moment in negotiation that wins out --- when the agency may not have itself reviewed its own data.

Once agreements are reached and appeals resolved, the ministries are responsible for preparing the budget documentation and justification. In addition to the formal President's Budget, each agency will prepare a separate budget justification for transmittal to Congress, as well as congressional testimony for their executives. OMB reviews and approves all these documents before they are sent to Congress, to assure they are all in alignment with Presidential/administration decisions and policies.

Agencies do have direct relationships with Congressional committees and staff, and have been known to provide information informally which sometimes undermines the budget. However, OMB staff closely monitor these discussions, and do report back to the Director of OMB on ministry behavior. Egregious breaches might solicit a call from the OMB Director to a Minister, but these are not common.

Final budget allocation.

Final budget allocations (passback, and appeals) are set relative to the ceilings. This has been especially true with the enactment of legally binding ceilings on discretionary and mandatory spending through the Budget Enforcement Act (BEA). While the BEA addresses aggregate spending levels, these are translated into ministry ceilings, and the sum of ceilings must of course match the legal limits.

The actual ministry budget allocation, while taken relative to the ceiling, is really determined by the accumulation of individual decisions on programs and policies. The policy papers prepared for decision (referred to above) incorporate extensive analysis by OMB staff of agency budget requests, as well as other research or findings (e.g. audit findings) regarding programs and policies. The analysis results in OMB staff recommendations for specific changes in funding, programs, policies, employment, etc. It also reflects the 'findings' of OMB staff from budget hearings held with each agency (at which each agency can make their case for their request). As each decision is taken, its effect relative to the ceilings is monitored to assure the totals are not exceeded.

While only some appeals will be addressed directly by the President, in the end it is the President's Budget that is transmitted to Congress, under his signature. The President is ultimately responsible for its content. The Cabinet does not formally approve the budget.

Roles.

The U.S. does not have a formal MTEF. The budget process has evolved, particularly after 1974, to incorporate medium-term projections in the process, as well as ministry strategic plans. Generally, the relationship between OMB and ministries has not changed dramatically due to the introduction of medium-term forecasts. Other factors influence relations more. For example, during periods of deficits, President's with a policy of spending reduction, and OMB Directors with high influence over domestic policy, OMB tends to be stronger relative to the ministries, and during these times OMB may be less 'collegial' in relations with ministries. At other times, OMB influence may be less, and relations with Ministries become far more collegial.

That said, there was some movement under President Clinton towards a more collegial approach by OMB. Early in the Clinton Administration, a survey was conducted of spending ministries as to what they thought of OMB, and barriers to agency efficiency. Not surprising, the results were rather negative, with ministries feeling OMB was too much into rule-mongering and second-guessing, too high-handed. The results were at first surprising to OMB staff, and certainly not accepted. After a series of brown-bag discussions between staff and the OMB Director, some acceptance of the results seemed to sink-in, with staff understanding that to really be effective, the ministries needed to be partners and understand the over-all constraints. No subsequent surveys have been taken, so it is not clear if the ministries would report differently now than a decade ago.

5. Policy and budgets

Generally, because of the requirement for the President to submit a budget, and that the budget embodies the President and Administration policies, it is 'owned.' President's can and do issue veto threats to Congress over exclusion (inclusion) of issues that they support (oppose).

Much of the President's involvement in the budget takes place through the OMB. When macroforecasts are developed and the budget outlook prepared, OMB advises the President and presents policy recommendations. The President makes policy decisions, which are passed to agencies through OMB. These initial policy decisions may set out

broad budgetary goals, or may include specific policy proposals and spending ceilings to

guide agencies in preparing their budget requests. Policy guidance on budget development often varies from year to year, depending on current economic and political conditions.

As noted above, ministries develop their budget requests. Direct Presidential involvement in many details is limited by the nature of the process. Presidential involvement tends more to policies, and some specific proposals. Figure 2 presents a stylized picture of the process, illustrating the points at which the President is involved in the process.

With respect to multi-year budget estimates, it is important to note that the President's Budget includes two sets of estimates for Congress: current services baseline and President's policy (showing the multi-year impact of the President's policy choices). These aid in transparency, and allow quick identification of those areas where major budget policy changes are proposed.

6. Legislature

As noted in the introduction, the Congress has the authority to change the executive budget proposal completely, including total revenue, total expenditure, deficit, debt, and allocations to ministries. This authority is in practice counterbalanced by the executive authority to veto the budget bills.

Over time the congressional budget process has been improved to give Congress greater ability to manage its own affairs. General examples of these from the early 1970's were mentioned in the introduction. This section will go into the congressional budget process in more detail.

The Congressional Budget and Impoundment Control Act of 1974 established the basic structure for the congressional budget process, creating the House and Senate Budget Committees and CBO. The Congress' budget process starts in February with the submission of the President's budget, after which the House and Senate Budget Committees begin developing their budget resolutions.

The annual budget resolution establishes total spending and revenue for five or more years, allocates spending by functional classification, and includes CBO baseline estimates of revenues. The spending amounts are then allocated to the House and Senate Appropriations Committees for discretionary spending, to the authorizing committees for mandatory spending, and to the House Ways and Means Committee for revenue targets. The Appropriations Committee of each house subdivides the discretionary allocation among its 13 subcommittees (broadly, the major functions). The committee allocations are one means of enforcing the aggregate s

pending levels in the budget resolution by holding committees accountable for meeting their targets.

After extensive hearings, each of the subcommittees reports one of the 13 regular appropriations bills to its respective full appropriations committee, which in turn reports the bills to their Chamber. A cost estimate of each bill is prepared and compared to the amount allocated or subdivided to the relevant subcommittee. The Congressional Budget Act prohibits bills from exceeding the budget resolution committee allocations. However, to be enforced, a Member of either Chamber must raise a point of order when the bill is being considered on the floor of the respective Chamber.

For mandatory spending, revenues and debt limits, the process of reconciliation (also established under the Congressional Budget and Impoundment Control Act) is used to enforce the budget resolution allocations.

Congress includes reconciliation instructions in the budget resolution directing the authorizing committees to recommend changes in law to achieve the direct spending, revenue, and debt limit targets in the budget resolution. The Budgets Committees of each Chamber then compile the various proposed legislative language from the authorizing committees into a reconciliation bill. Unlike the process for discretionary spending, there are no points of order for a reconciliation bill that does not meet the budget resolution mandatory spending targets. Amendments on the floor of each Chamber may seek to bring the reconciliation bill closer to the budget resolution targets, but that is entirely at the discretion of a

Member, and subject of course to a successful vote for the amendment. For revenues, a point of order may be raised for amendments that would reduce revenues below the budget resolution.

The Congressional Budget and Impoundment Control Act does prohibit either Chamber from considering amendments to a reconciliation bill that would increase the deficit. The law also provides a congressional budget process timetable: the budget resolution should be adopted by April 15, and the reconciliation bill by June 15. (These are frequently not met.)

The Budget Enforcement Act of 1990 also required that any measure reducing revenues below the budget resolution or increasing mandatory spending be offset with equivalent revenue increases or mandatory spending reductions (commonly referred to as the pay-as-you-go rule). This is also enforced by a sequestration process, whereby any violation will trigger an offsetting sequestration of nonexempt mandatory spending programs.

7. In-year Effect

In-year effect of ceilings. Generally, OMB has been responsible for costing new legislation. As a practical matter, not all legislation is costed. Only executive branch proposals, and legislation in Congress likely to be passed by Committee and proceed to the floor.

During the budget process, 'scorekeeping' (measuring the budgetary effects of pending and enacted legislation against the baseline) is used to compare proposed budget policy changes to existing law and to enforce spending and revenue levels agreed upon in the budget resolution and other budget legislation, such as the discretionary spending caps and pay-as-you-go rules.

During the fiscal year, scorekeeping is also used for new legislation. As OMB must clear all legislation before transmittal to Congress, no uncosted or unfunded legislation is transmitted from the executive. All proposals must fit within the ceilings.

8. Discussion and Over-all Assessment

This presentation of medium-term budgeting in the U.S. has focused on the process, technical details, rules and roles. It has tried to provide both the hard facts, and some of information on how it works in practice. But to the reader it may appear a dizzying blizzard of rules and procedures. This summary tries to draw out the key features of the process, and also the key strengths and weaknesses of the process.

One aspect of note is in fact the interplay between executive and legislature. The competition between the two branches has led to innovations in budgeting and a fairly high degree of accountability in public finances. That is not to say all spending is efficient. But there are pressures to become more efficient.

For the medium term aspects of budgeting, the important points are:

1. in considering policy and programs, thinking beyond one year to the outyear effects of proposals and existing spending is common throughout the system. Over a quarter century of requirements for multi-year estimates, and progressively greater attention to these estimates, have made multi-year thinking a normal part of public finance.
2. The baseline estimates serve as a useful reference point for considering changes in policy and programs over several years, and better inform decision-makers. This has likely led to different choices in programs, and in reallocation from lower to higher priority programs, early in the budget process --- but it is not possible to systematically measure this effect.
3. Beyond the 'information' effect noted above, including use of indicative ceilings in the budget process, the multi-year estimates had limited bite. Not until the large deficits of the 1980's and general political and public consensus that deficits were 'bad' did multi-year estimates and ceilings gain real teeth. And further, not until the Gramm-Rudman-Hollings and Budget Enforcement Act legislated ceilings and pay-go requirements did the real effect of ceilings and estimates come to be felt.
4. Some means of bringing consensus on multi-year policy is critical. It is this consensus that shapes behavior and changes direction the most. For the U.S., consensus within the executive branch is achieved through the NEC. Within the legislative branch, it is achieved via the negotiations that take place in the Budget Committees in crafting the budget resolution (frequently including negotiation with the executive branch). And finally, the Budget Enforcement Act represented the executive-legislative consensus necessary in the U.S. political system to really begin to reign-in deficit spending.
5. Despite the presence of multi-year estimates for a quarter century, this has not prevented growth in spending. It has influenced choices, and might even have contributed to a shift towards more mandatory spending programs not directly under annual budget control. For the U.S., information on future impact has not been enough to effectively limit spending growth. This might be part of the curse of riches, where deficits and postponement of decisive choices on fiscal matters can be financed given the easy access to international capital markets enjoyed by the U.S. The impact of multi-year information might be greater for

countries with less easy access to capital markets. For the U.S., hard, legally binding fiscal targets were required to make a difference.

6. The Gramm-Rudman hard targets proved too demanding, and the targets could not be reached through the political process. The BEA proved more successful, by limiting discretionary spending and requiring off-sets for deficit-increasing changes to entitlement programs. These procedural rules changed the incentives in the budget system to limit spending growth, and this proved more successful than hard deficit reduction targets.
7. With the short-lived budget surpluses in the late 1990's and early 2000's, the consensus on budget discipline broke down, and the BEA lost emphasis. The multi-year estimates are firmly entrenched and still prepared, and at least provide the political officials with clear information on the direction they are heading. The availability of this information does likely serve as some break on excess, but again the 'teeth' are lacking. However, as the outyear picture worsens with continuous provision of multi-year estimates, the pressure to contain spending will likely reassert itself --- a self-correcting mechanism, albeit with lags in effect. Even in the absence of hard legal constraints, multi-year information is of value.

While the deficits are large, and there is increasing suggestions of the imprudence of current policy, some of the expansionary fiscal policy is intended to boost economic growth. The policy is intended as counter-cyclical --- just as large surpluses were incurred during years of strong growth and used to pay down the debt, so now deficits are incurred. One can debate whether it is really needed, or needed in the size and form in which it is incurred (tax cuts), it is a legitimate debate. It does not mean the underlying budget system is entirely broken. Where a policy decision is taken to operate an expansionary fiscal policy, it does not mean the underlying process is dysfunctional. It would be if the expansionary policy were taken absent information on likely outcome, but that is not the case.

Figure 2

