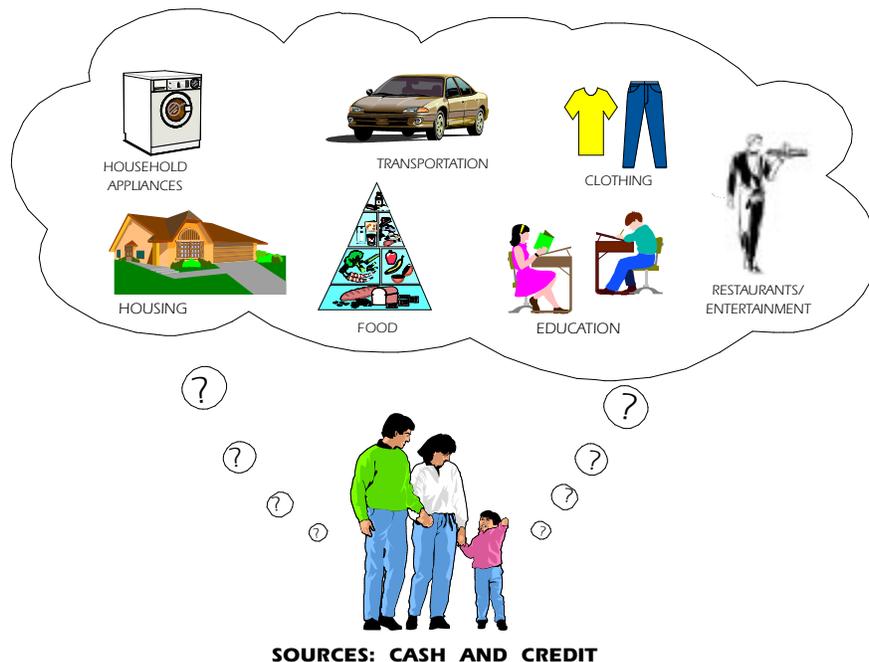


## **2. Where the Money Comes From— and Where it Goes**

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

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

**Chart 2-1. Family Budgeting**

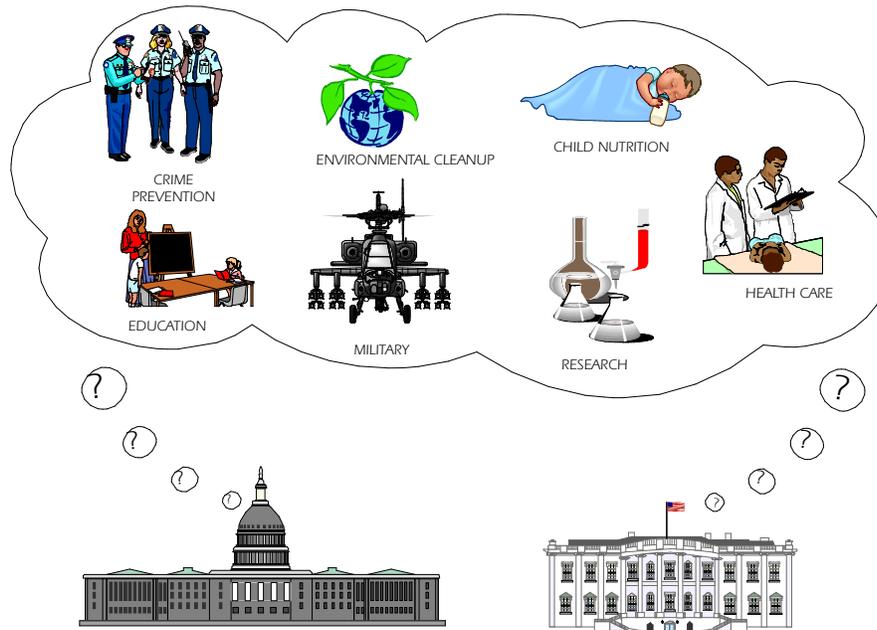


Generally speaking, the Federal Government plans its budget much like families do. The President and Congress determine how much money they expect the Government to receive in each of the next several years, where it will come from, and how much to spend to reach their goals—goals for national defense,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

They decide how much spending they will finance through taxes and how much through borrowing. They debate how to use the budget to help the economy grow, or to redistribute income. And, especially lately, they debate how to reduce spending in order to eliminate the deficit and balance the budget.

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

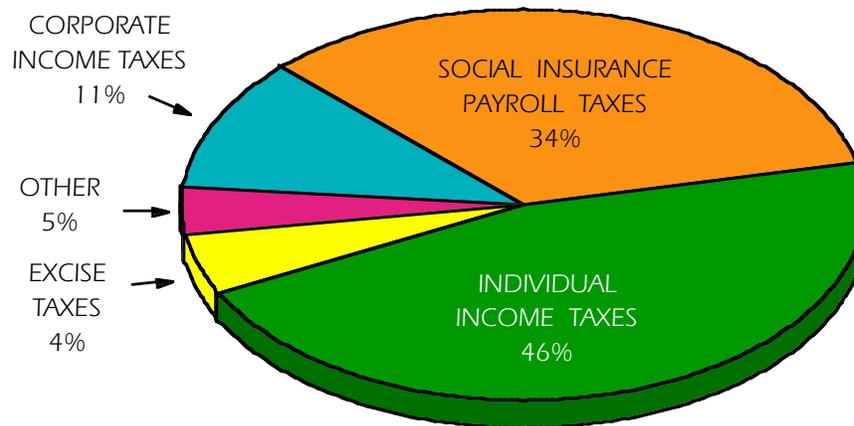
**Chart 2-2. National Budgeting**



**SOURCES: TAXES AND BORROWING**

## Revenues

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



The money that the Federal Government uses to pay its bills—its revenues—comes mostly from taxes. In recent years, revenues have been lower than spending, and the Government has borrowed to finance the difference between revenues and spending—that is, the deficit.

Revenues come from these sources:

- Individual income taxes will raise an estimated \$791 billion in 1999, equal to about nine percent of GDP—slightly higher than the average of the last 40 years.
- Social insurance payroll taxes—the fastest growing category of Federal revenues—include Social Security taxes, Medicare taxes, unemployment insurance taxes, and Federal employee retirement payments. This category has grown from two percent of GDP in 1955 to nearly seven percent in 1999.
- Corporate income taxes, which will raise an estimated \$198 billion, have shrunk steadily as a percent of GDP, from 4.5 percent in 1955 to 2.3 percent in 1999.

**Table 2-1. Revenues By Source—Summary**

(In billions of dollars)

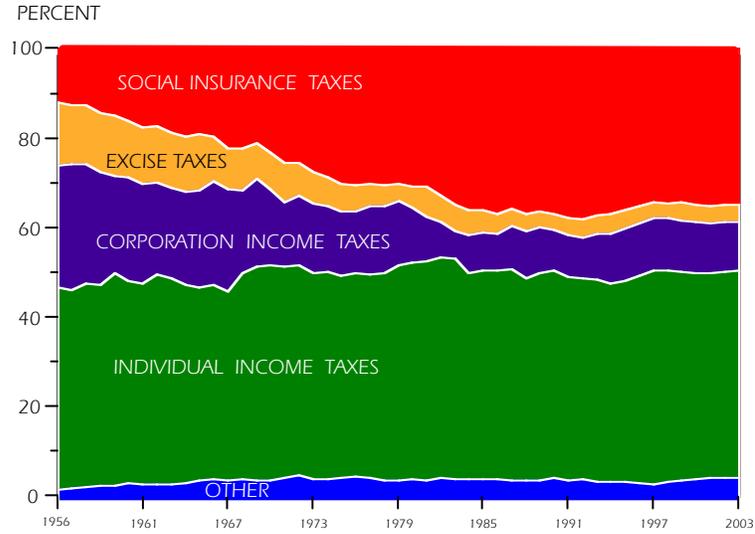
Source	1997 Actual	Estimate					
		1998	1999	2000	2001	2002	2003
Individual income taxes . . . . .	737	768	791	805	833	877	916
Corporate income taxes . . . . .	182	191	198	203	209	215	220
Payroll taxes . . . . .	539	571	596	623	649	678	707
Excise taxes . . . . .	57	56	72	70	72	74	75
Estate and gift taxes . . . . .	20	20	21	22	23	24	26
Customs duties . . . . .	18	18	18	20	20	22	24
Miscellaneous receipts . . . . .	25	34	47	52	56	59	61
<b>Total receipts . . . . .</b>	<b>1,579</b>	<b>1,658</b>	<b>1,743</b>	<b>1,794</b>	<b>1,863</b>	<b>1,949</b>	<b>2,028</b>

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

Numbers may not add to the totals because of rounding.

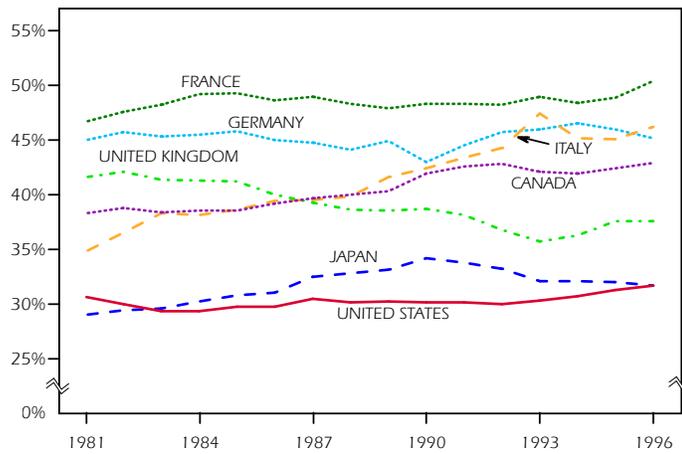
- Excise taxes apply to various products, including alcohol, tobacco, transportation fuels, and telephone services. The Government earmarks some of these taxes to support certain activities—including highways and airports and airways—and deposits others in the general fund.
- The Government also collects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

**Chart 2-4. Composition of Revenues**



*Between 1960 and 1997, payroll taxes have increased substantially as a percent of GDP, and corporate income taxes have declined, but individual income taxes have remained roughly constant.*

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



Source: OECD, calendar year data.

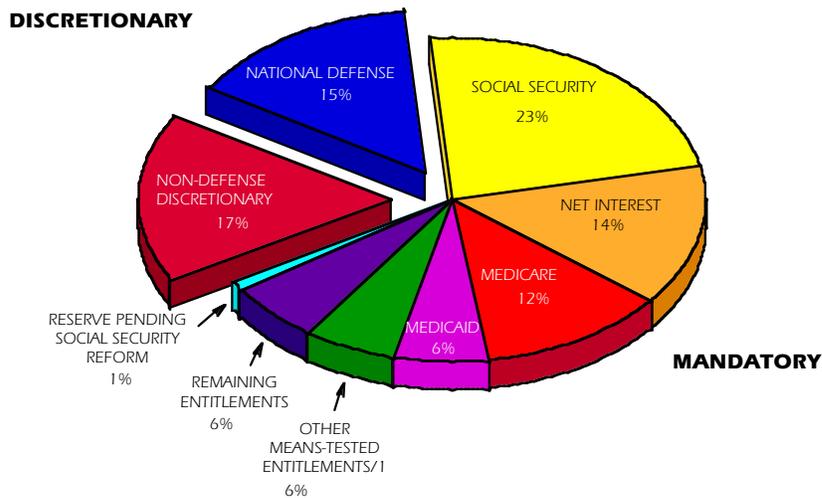
*The United States and Japan have the lowest revenues as a percent of GDP of the seven countries listed above.*

## Spending

As we have said, the Federal Government will spend over \$1.7 trillion<sup>1</sup> in 1999, which we divided into eight large categories as shown in Chart 2-6.

- The largest Federal program is Social Security, which will provide monthly benefits to nearly 45 million retired and disabled workers, their dependents, and survivors. It accounts for 23 percent of all Federal spending.
- Medicare, which will provide health care coverage for over 39 million elderly Americans and people with disabilities, consists of Part A (hospital insurance) and Part B (insurance for physician costs and other services). Since its birth in 1965, Medicare has accounted for an ever-growing share of spending. In 1999 it will comprise 12 percent.

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



<sup>1</sup> Means-tested entitlements are those for which eligibility is based on income. The Medicaid program is also a means-tested entitlement.

<sup>1</sup> In calculating Federal spending, the Government deducts collections (revenues) generated by the Government's business-like activities, such as fees to national parks. These collections will total an estimated \$210 billion in 1999. Without them, spending would total an estimated \$1.9 trillion in 1999, not \$1.7 trillion.

- Medicaid, in 1999, will provide health care services to over 35 million Americans, including the poor, people with disabilities, and senior citizens in nursing homes. Unlike Medicare, the Federal Government shares the costs of Medicaid with the States, paying between 50 and 83 percent of the total (depending on each State's requirements). Federal and State costs are growing rapidly. Medicaid accounts for six percent of the Federal budget.
- Other means-tested entitlements provide benefits to people and families with incomes below certain minimum levels that vary from program to program. The major means-tested entitlements are Food Stamps and food aid to Puerto Rico, Supplemental Security Income, Child Nutrition, the Earned Income Tax Credit, and veterans' pensions. This category will account for an estimated six percent of the budget in 1999.
- The remaining entitlements, which mainly consist of Federal retirement and insurance programs and payments to farmers, comprise six percent of the budget.
- National defense discretionary spending will total an estimated \$267 billion in 1999, comprising over 15 percent of the budget and three percent of GDP.
- Non-defense discretionary spending—a wide array of programs that include education, training, science, technology, housing, transportation, and foreign aid—has shrunk as a share of the budget from 23 percent in 1966 to an estimated 17 percent in 1999.
- Interest payments, primarily the result of previous budget deficits, averaged seven percent of Federal spending in the 1960s and 1970s. But, due to the large budget deficits that began in the 1980s, that share quickly doubled to 15 percent, where it stands today. As the budget comes into balance in 1999, interest payments will drop to an estimated 14 percent.

**Table 2-2. Spending Summary**

(Outlays, in billions of dollars)

Source	1997 Actual	Estimate					
		1998	1999	2000	2001	2002	2003
Discretionary:							
National defense . . . . .	272	265	267	270	271	273	289
International . . . . .	19	19	19	19	19	19	19
Domestic . . . . .	258	269	281	285	285	285	287
Subtotal, discretionary . . . . .	548	553	566	574	575	577	595
Mandatory:							
Programmatic:							
Social security . . . . .	362	378	393	409	427	447	468
Medicare . . . . .	187	195	205	214	230	232	253
Medicaid . . . . .	96	101	108	115	123	133	143
Means-tested entitlements (except Medicaid) . . . . .	98	104	112	117	121	124	129
Other . . . . .	115	141	151	165	172	175	185
Subtotal, programmatic . . . . .	859	919	968	1,021	1,073	1,111	1,178
Undistributed offsetting receipts . . . . .	-50	-46	-42	-46	-47	-56	-48
Subtotal, mandatory . . . . .	809	872	925	975	1,026	1,056	1,129
Net interest . . . . .	244	243	242	236	234	227	221
Subtotal, mandatory and net interest . . . . .	1,053	1,115	1,167	1,211	1,259	1,283	1,350
<b>Total . . . . .</b>	<b>1,601</b>	<b>1,668</b>	<b>1,733</b>	<b>1,785</b>	<b>1,834</b>	<b>1,860</b>	<b>1,945</b>

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

**Table 2-3. Spending by Function**

(Outlays, in billions of dollars)

Source	1997 Actual	Estimate					
		1998	1999	2000	2001	2002	2003
National defense:							
Department of Defense-Military . . . . .	258	251	253	256	257	260	276
Other . . . . .	12	13	13	13	13	12	13
Total, national defense . . . . .	270	264	265	269	270	272	289
International affairs . . . . .	15	14	14	15	15	16	16
General science, space, and technology . . . . .	17	17	18	18	18	19	19
Energy . . . . .	1	*	-1	*	-*	-*	-*
Natural resources and environment . . . . .	21	24	23	24	24	23	24
Agriculture . . . . .	9	11	11	11	9	9	9
Commerce and housing credit . . . . .	-15	4	4	12	11	11	10
Transportation . . . . .	41	42	42	43	43	44	45
Community and regional development . . . . .	11	12	11	10	10	9	8
Education, training, employment, and social services . . . . .	53	55	59	63	63	63	66
Health . . . . .	124	132	141	150	160	171	183
Medicare . . . . .	190	198	207	217	233	235	256
Income security . . . . .	231	239	253	263	272	278	287
Social security . . . . .	365	381	396	413	430	450	471
Veterans benefits and services . . . . .	39	43	43	44	45	45	47
Administration of justice . . . . .	20	22	26	26	27	26	26
General government . . . . .	13	13	17	17	18	18	19
Net interest . . . . .	244	243	242	236	234	227	221
Allowances . . . . .			3				
Undistributed offsetting receipts . . . . .	-50	-46	-42	-46	-47	-56	-48
<b>Total . . . . .</b>	<b>1,601</b>	<b>1,668</b>	<b>1,733</b>	<b>1,785</b>	<b>1,834</b>	<b>1,860</b>	<b>1,945</b>

\* \$500 million or less.

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

**Table 2-4. Spending by Agency**

(Outlays, in billions of dollars)

Source	1997 Actual	Estimate					
		1998	1999	2000	2001	2002	2003
Legislative Branch . . . . .	2	3	3	3	3	3	3
Judicial Branch . . . . .	3	4	4	4	4	4	4
Agriculture . . . . .	53	55	54	56	57	58	60
Commerce . . . . .	4	4	5	6	4	4	4
Defense-Military . . . . .	258	251	253	256	257	260	276
Education . . . . .	30	31	34	36	37	37	38
Energy . . . . .	14	14	15	15	15	14	15
Health and Human Services . . . . .	340	359	381	401	428	441	476
Housing and Urban Development . . . . .	28	31	32	32	31	31	29
Interior . . . . .	7	8	8	8	8	8	8
Justice . . . . .	14	15	18	19	19	18	18
Labor . . . . .	30	32	36	38	39	40	42
State . . . . .	5	5	5	5	5	6	6
Transportation . . . . .	40	40	41	42	43	43	44
Treasury . . . . .	379	387	399	402	408	411	414
Veterans Affairs . . . . .	39	43	43	44	45	45	47
Corps of Engineers . . . . .	4	4	3	3	3	3	3
Other Defense Civil Programs . . . . .	30	31	32	33	34	35	36
Environmental Protection Agency . . . . .	6	6	7	7	7	7	7
Executive Office of the President . . . . .	*	*	*	*	*	*	*
Federal Emergency Management Agency . . . . .	3	4	3	2	1	1	1
General Services Administration . . . . .	1	1	*	*	*	-1	*
International Assistance Programs . . . . .	10	10	9	10	10	10	10
National Aeronautics and Space Administration . . . . .	14	14	14	13	13	13	13
National Science Foundation . . . . .	3	3	3	4	4	4	4
Office of Personnel Management . . . . .	45	46	49	51	53	55	58
Small Business Administration . . . . .	*	-*	-*	-*	1	1	1
Social Security Administration . . . . .	393	410	426	443	462	482	504
Other Independent Agencies . . . . .	-2	14	14	22	22	22	22
Allowances . . . . .			3				
Undistributed offsetting receipts . . . . .	-155	-160	-162	-172	-181	-197	-199
<b>Total . . . . .</b>	<b>1,601</b>	<b>1,668</b>	<b>1,733</b>	<b>1,785</b>	<b>1,834</b>	<b>1,860</b>	<b>1,945</b>

\* \$500 million or less.

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

Numbers may not add to the totals because of rounding.

## “On” and “Off” Budget

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

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

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

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

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

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

