

# RESTRICTED

THE FEDERAL BUDGET

821

5 December 1951

## CONTENTS

	<u>Page</u>
INTRODUCTION--Brigadier General J. L. Holman, USA, Deputy Commandant for Education .....	1
SPEAKER--Mr. Frederick J. Lawton, Director of the Bureau of the Budget.....	1
GENERAL DISCUSSION.....	14

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# RESTRICTED

# RESTRICTED

827

Mr. Frederick J. Lawton, Director of the Bureau of the Budget, was born in Washington, D. C., 11 November 1900. He was graduated from Georgetown University in 1920 and received his LL.B. degree from Georgetown University in 1934. He started his career in government service in 1921 and served in various accounting and administrative positions in the Treasury Department until 1935. He has been an executive of the Bureau of the Budget since 1935. He was executive assistant to the Director of the Bureau of the Budget for ten years before becoming assistant director, except for five months in 1948 when he was an administrative assistant to the President. He served as special adviser to the Senate Select Committee on Government Organization from 1937 to 1939. He was appointed Director of the Bureau of the Budget on 13 April 1950.

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# RESTRICTED

# RESTRICTED

823

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GENERAL HOLMAN: Gentlemen, it is a genuine privilege to introduce to both colleges Mr. Frederick J. Lawton, Director of the Budget. In our studies of war finance, it is important for us to understand the evolution and the composition of the Federal Budget, its relationship to our fiscal policy, the national economy, and the current economic trends.

The Federal Budget is probably the most important single document issued by the Government each year and it is of extreme interest to all of us. As government officials, military planners, and as individuals and taxpayers, it is important that we know something about it.

Mr. Lawton, it is a great privilege and a pleasure to have you with us and to hear your discussion of the Federal Budget.

MR. LAWTON: Gentlemen, I welcome this opportunity this morning for two reasons to discuss with you some of the problems of Federal budgeting in a defense emergency:

First, because a budget of 70 billion dollars--which comprises 25 percent of the total national income--is of tremendous importance to all citizens of the Nation.

Second, because many of you gentlemen play an important part in the budgeting process, even though you may not be aware of it.

Budgeting is not an exclusive function of the Bureau of the Budget. It is a government-wide operation in which all agencies play a part and today the Department of Defense is playing a vital role in the formulation of our national budget.

Many of you have probably participated in the development of budget estimates for military activities and the formulation of some of the basic decisions regarding the strength and structure of the armed forces and the requirements for supplies and equipment necessary to support these forces. If so, then you have already played an extremely important role in the development of the national budget. In the current fiscal year military functions alone will absorb 60 percent of our budget dollars; 15 percent of our national income; 50 percent of the total number of Federal civilian employees; and if you include the armed forces, more than 7 percent of the Nation's total supply of manpower.

# RESTRICTED

# RESTRICTED

854

These programs in the military field are so complex and their implications are so far-reaching that, today, a top career in the armed forces is one of the most challenging and difficult jobs which our society can offer. The task of administering our military program requires not only military skills but also a firm grasp of the political, economic, and social problems which inevitably arise in a defense emergency. These two colleges, the Industrial College of the Armed Forces and the National War College, offer the type of training which is designed to help you cope with these problems.

The national budget, even though it is big and complex, is not a jumble of unintelligible figures. It is a vital and living statement of the Government's program and, as such, it directly affects all of us--not only the taxes we pay but our jobs, our incomes, the price and volume of goods, and services which we enjoy.

Because it is so important, the budget is one of the most widely debated documents published by the Federal Government. It is discussed--often with considerable heat and vehemence--in the halls of Congress, in the newspapers, in public meetings, in country stores, in schools and colleges, and in offices and factories, throughout the country.

Because its size and complexity make the budget difficult to comprehend, there is an understandable tendency for many people to assume that it contains large and hidden amounts of pork, or waste, or extravagance. As a result there is an annual barrage of oversimplified proposals or magic formulas for cutting the budget by "X" percent or "Y" billion dollars. We are often told that the budget can be easily balanced, if by applying these formulas we simply eliminate unnecessary and nonessential activities, or weed out frills.

These formulas often have a superficial glamour which gives them wide appeal, but they do not stand up when put to the test. In the Bureau of the Budget we who have been scrutinizing government programs for many years have never been able to utilize these formulas. This does not mean, however, that we are not deeply concerned with the problem of reducing Federal expenditures to the minimum required to carry out effectively the laws passed by Congress. We have been and shall continue to be concerned with this problem, but we know from long experience that there are no pat answers, no magic formulas, no quick and easy solutions.

The budget is a program of action, spelled out in dollar terms, which tells us what the Government intends to do and how much it will cost in the coming year. As such it is a valuable management tool which permits the President to control the level of government activities, to see that they are coordinated and in balance with each other, and to see that the responsibilities of the Government are being effectively discharged.

RESTRICTED

# RESTRICTED

825

Most citizens have little conception of the great number and variety of government programs and services which are provided for in the budget. The 1952 Budget provides for the development of atomic energy, for carrying the mail, the inspection of food and drugs to protect our citizens against impure and fraudulent products, the patrolling and protection of our borders, the construction of bridges, dams, and highways, the inspection of rail and air carriers to insure safe public transportation, the collection of weather data, and the search for causes and cures for heart disease and cancer, as well as providing for the rapid build-up of our military forces and for military and economic aid to our allies.

The process by which we weigh the importance of each of these activities and assign dollar values to them through the budget process is one of the most important functions of free government. Before I discuss some of the fiscal and economic problems which arise from the present defense effort, I should like to discuss briefly the process of developing the Federal Budget.

To us who are familiar with war and postwar budgets and the tremendous impact which those budgets have upon our national life, it is almost inconceivable that there should have been a time when there was no executive budget; yet, 30 years ago that was the case. The annual appropriation requests of the various departments and agencies were simply added up and submitted to the Congress without any attempt to fit them into a well-balanced program. Within the Congress itself the various appropriation requests of the executive branch were reviewed and enacted individually by separate committees. Under such conditions it was obviously impossible for the Government to obtain an over-all picture of its financial requirements and to develop a fiscal program which would meet the needs of a growing nation.

The Budget and Accounting Act of 1921 established for the first time one budget for the entire Government. The President was given the responsibility of reviewing the requests of the Departments and agencies and of reaching a decision as to what should be included in the Government's fiscal program. The Bureau of the Budget was created by this same act to assist the President in carrying out these responsibilities. In the Reorganization Act of 1939, the Bureau was removed from the Treasury Department, where it had initially been established, and placed in the Executive Office of the President. From that time on the Bureau has been able to undertake a more active part in the general management of the executive branch and in the strengthening of budgetary controls.

Contrary to widespread belief the expenditures in the President's budget are based almost entirely on programs which have been authorized or required by Congress in basic law and not solely on schemes and plans

# RESTRICTED

# RESTRICTED

826

dreamed up by the President and executive agencies. The Constitution specifically provides that "no money shall be taken from the Treasury but in consequence of appropriations made by law." Consequently, no program can be undertaken by any government agency without congressional authorization. With the exception of certain items which are clearly earmarked as proposed legislation, the budgeting process cannot begin until each program is so authorized.

The first step in developing a national budget takes place within the various agencies of the executive branch from 12 to 18 months prior to the beginning of the budget year. Agency heads and their principal advisers, including their budget officers, make a forecast of work load trends for the coming year and prepare budget estimates which are designed to fit the needs of the program as they see them.

These estimates, after a very close scrutiny on the departmental level, are usually submitted to the Bureau of the Budget in September, more than nine months before the beginning of the new fiscal year. In the Bureau, every estimate is analyzed by budget examiners who have familiarized themselves over the years with the programs and operations of particular agencies. At this time informal hearings are held in which top agency officials and their staff advisers discuss in detail the assumptions and reasoning underlying the budget request for each individual program. On the basis of the work of the budget examiners and the information obtained in the hearings, the main budgetary issues for each program are then reviewed by the Director and top officials of the Bureau.

This Director's Review again surveys each program, relates it to other programs and the over-all needs of the Government, and seeks to resolve the problems and issues that have arisen in the course of the staff review.

Needless to say final action on the Bureau's recommendations are taken by the President. As the recommendations of the Bureau are prepared, they are taken to the White House where major policy issues are discussed and final decisions reached. The budget in its truest sense is the President's own work--it is his program.

Perhaps some of you are thinking at this point that the agencies can offset any major reductions in their estimates by anticipating the Bureau's action and padding their initial requests by an amount equal to the anticipated reductions. This might be the case if it were not for the ceiling process which enables the President to influence agency requests prior to their submission to the Bureau of the Budget.

In the spring, some 18 months before the beginning of the fiscal year, the Bureau of the Budget prepares estimates of receipts and expenditures, which take into account anticipated economic conditions

# RESTRICTED

# RESTRICTED

827

and trends in individual programs over the next three to five years. In the light of this outlook, the current or short-run economic situation, program trends, over-all budget policies, and agency ceilings are developed by the Bureau, approved by the President, and transmitted to the agencies.

The process by which agencies develop their budget requests thus takes place within a framework of budget policy and within a ceiling figure which represents a maximum above which agency estimates cannot go. In the present emergency the Department of Defense is not subject to the usual ceiling process, but its estimates are carefully reviewed by the Budget Bureau and are, of course, subject to approval by the President.

The next step in making money available to the executive agencies is the appropriation process in Congress. There the agency requests are carefully analyzed and reviewed by the appropriate subcommittees of the Appropriation Committees of both Houses, where once again the agencies must justify their requests. The appropriation bills as finally enacted by both Houses are not, of course, blank checks, which permit agencies to spend money for whatever activities they see fit. The appropriation language carefully specifies the purposes for which the money can be spent and sometimes specific purposes for which it cannot be spent.

The system of expenditure control does not end with the appropriation process. The Bureau of the Budget is authorized to review agency programs four times a year and to apportion the agency's money over the four quarters of the fiscal year. This apportionment is designed to prevent overobligation by the agencies in the early part of the year, which would make it necessary to return to the Congress for additional funds later in the year. The Bureau also has the power to establish reserves whenever it becomes obvious that funds available for a given purpose are larger than necessary. The surpluses which the Bureau picks up in the form of reserves result principally from changes in economic and program conditions which were unforeseen when the budget was originally developed.

The Bureau of the Budget has several other major tasks assigned to it by law. The first of these recognizes the fact that the control of expenditures is intimately connected with the promotion of efficiency, good organization, and sound management. Thus, the Administrative Management Division of the Bureau devotes much effort to the continuous study of means by which the organization and working methods in the executive branch of the Government can be improved. This effort to achieve a better-run Government is a continuing one that goes on every day in the year in cooperation with the other executive agencies. Its chief aim is to see that the taxpayer receives a full dollar's worth of service for every dollar spent by his Government.

# RESTRICTED

# RESTRICTED

828

The second task which the Bureau performs in addition to the review of the budget estimates is the coordination and analysis of all legislative proposals which are submitted by agencies in the executive branch to Congress. This function originated from a realization that much of the proposed new legislation involves increased expenditures and that the proper time to control such increases is before the legislative proposals are submitted to Congress. The Bureau now checks all legislative proposals from the executive agencies for conformity with the program of the President.

Another function of the Bureau is the coordination and improvement of Federal statistics. This activity is aimed primarily at simplifying and reducing the number of government forms so as to minimize the burden of reporting upon the general public and private business and developing a more adequate government-wide statistical program so that the Government, business, and the public will have better information about the operation of our economy.

With this general background as to what the Bureau of the Budget does, let me turn now to the budget document itself.

The 1952 Budget, which contemplates expenditures of approximately 70 billion dollars, is the largest peacetime budget in the history of our country. An examination of the many items of expenditure included in this budget will show that it is first and foremost a defense budget. Approximately 50 billion dollars, or 70 percent of the total budget expenditures will go to finance seven major security programs.

Military functions of the Department of Defense and the Mutual Defense Assistance Program (MDAP), which may run as high as 44 billion dollars, represent about 60 percent of all budget expenditures. The other important security programs which, taken together, will cost about six billion dollars in this fiscal year include foreign economic aid designed to strengthen and stabilize the economies of our allies; the stockpiling of critical and strategic materials; the development of atomic energy; the construction of a fast fleet of merchant vessels to support military activities; defense production and economic stabilization; and defense housing and civil defense.

Of the remaining total of 20 billion dollars in the 1952 Budget, two large programs, interest on the public debt and veterans' services and benefits, will absorb more than half. Interest on our Federal debt, which was largely incurred to finance our defense effort in World War II, will cost 6 billion dollars in 1952. Expenditures of 4.9 billion dollars will go for benefits and services to 19 million veterans, most of whom took part in World War II.

RESTRICTED

# RESTRICTED

829

Thus, the three categories of budget expenditures which I have discussed thus far, major national security programs, interest on the debt, and veterans' services--which represent the cost of current defense and past wars--account for about 60 billion dollars, or 85 percent of the total expenditures for 1952. All other programs of the Federal Government will cost only 9.5 billion dollars. In this 9.5 billion dollars, however, are found a very large number of relatively small programs dollarwise, which furnish essential services to the public and indeed to the defense effort. It is this small area, however, at which the general charges of waste, extravagance, and unnecessary spending are most frequently leveled.

Let me emphasize three important points about this "all other" segment of the budget. First, we cannot expand our security effort without taking essential steps elsewhere in the budget to support that effort. The rapid build-up of our military strength must necessarily have priority in all that we do. But military strength does not depend entirely upon armed forces alone. These forces must be equipped by our industry; fed by our farmers; served by our railroads, highways, and airports; provided with materials and products from our mines and forests; and supported by all the people. There must be a continuing balance between the build-up of military strength and the build-up of our strength as a nation. The "all other" portion of the 1952 Budget contains many programs which are essential to preserve that balance.

Second, there are many programs in this portion of the budget which directly support the defense effort. The port security program of the Coast Guard and the internal security activities of the FBI are examples of such supporting programs which have been expanded during the defense effort. The air navigation control system operated by the Civil Aeronautics Administration serves not only the expanding number of military air bases but also the increased civilian air traffic growing out of the defense effort. The public power program in the Northwest and the Tennessee Valley which directly serve important atomic energy installations and defense plants producing aluminum, magnesium, and chemicals also have had to be expanded to meet the vastly increased load requirements.

Third, there are several other programs in this "all other" portion of the budget whose size and scope reflect increases in the level of our economic activity, growing out of the defense effort. For example, the volume of mail to be handled has increased markedly, and the job of collecting taxes and issuing checks in payment of government orders is bigger.

I do not want to leave the impression that all programs in the budget have been expanded since Korea or that nothing has been done to make reductions. The entire budget has been placed under a succession

# RESTRICTED

# RESTRICTED

830

of very stringent reviews. All projects and undertakings which could possibly be postponed until after the peak of the mobilization effort were eliminated. Let me give an example of this type of action in the field of civil public works.

During the fiscal year 1951 a total of 30 Corps of Engineers' projects which had been under construction in 1950 received no additional funds. In the 1952 Budget the base of going projects has been further reduced. Nearly 35 projects which were under construction in 1951 were recommended for deferral in this fiscal year and no funds were recommended for them. The total cost of completing those deferred projects is well above 200 million dollars.

We are constantly asked why the Budget for the fiscal year 1952 is so large. This question should not be too difficult for you in the armed forces to answer. However, a comparison of the 1952 Budget with that of the prewar year 1940 will show clearly what has happened to the major categories of government expenditures.

First, the major national security expenditures increased from a total of 1.6 billion in 1940 to around 50 billion dollars in 1952, an increase of no less than 3,000 percent. In the same period interest on the public debt increased 450 percent, and expenditures for veterans jumped 720 percent. The "all other" portion of the budget has increased from 5.9 billion dollars in 1940 to 9.5 billion in 1952, an increase of only 60 percent. This increase must be viewed in the light of increased costs. From 1940 to 1952 the average cost of government salaries rose 80 percent, construction costs rose 112 percent, and the general level of wholesale prices rose 105 percent. I believe that this small increase in expenditures for the normal operations of the Government in the face of mounting costs is adequate testimony of our strenuous efforts to hold down the cost of the so-called nondefense programs.

We must conclude then that the budget is large primarily for two reasons:

First, because the cost of defense has mounted tremendously. Let me give you a few examples. The cost of constructing the Navy's new supercarrier, presently estimated at more than 200 million dollars, is approximately two-thirds of the Navy's entire annual budget 20 years ago. The cost of initially equipping an armored division in the Army has risen from 40 million dollars in World War II to 293 million dollars in 1952. This cost of equipping an armored division incidently is approximately equal to the total annual cost of military activities of the War Department 20 years ago. The fly-away cost of a heavy bomber, B-29, in World War II, was 680,000 dollars, while the heavy bomber currently in use, the B-36, costs five times as much. It is interesting to note that the cost of electronic equipment alone on the B-36 exceeds the total cost of the B-29 in World War II.

# RESTRICTED

# RESTRICTED

831

Second, the budget is large because we are still paying for World War II, in the form of veterans' benefits and interest on the public debt.

Now let us look at the receipts side of the 1952 Budget. Estimates of revenue for this fiscal year which, of course, take account of the new tax laws recently passed by Congress range from 61 billion dollars to 65 billion dollars. Thus, if expenditures reach the estimated 70 billion dollars, we are faced with a deficit of at least 5 billion dollars for fiscal year 1952.

What about the budget outlook for 1953 and beyond? Until recently many people had the idea that we would be "over the hump" by the end of this fiscal year. The truth of the matter is that the full impact of the defense program on budget expenditures will not be felt until late in fiscal year 1953 or early in fiscal year 1954. This is true primarily because it takes considerable time for budget authorizations to be translated into actual expenditures. For example, in the field of military procurement, several years may elapse between the time when Congress makes the necessary appropriations for ships, planes, or tanks and the date when delivery is made and the check for final payment to the contractors. Between the appropriations of funds and actual expenditure from the Treasury, time must be allowed for the armed forces to design and contract for the equipment industry to expand, tool-up, produce, and deliver; and the Government to test the final product.

An extended lag between the appropriation of funds and the delivery of goods is, of course, most usual in the military program but these lags occur throughout the budget. The Bureau of the Budget, for example, is still paying for the travel of certain of its employees who were on field trips last June. This is because railroads often take several months to present their bills to the Government for payment.

Thus, it can be seen that new obligational authority enacted by Congress in any one year becomes a major determinant of expenditures in subsequent years. For example, in fiscal year 1950 the total new obligational authority enacted by Congress amounted to 50.2 billion dollars. Actual expenditures were only 44.6 billion dollars. New obligational authority for fiscal year 1952 enacted by Congress to date totals approximately 90 billion dollars, but total expenditures for 1952 are estimated in the neighborhood of 70 billion dollars. On this basis, it can be seen that the Federal Government will enter the fiscal year 1953 with a carry-over of about 70 billion dollars still available for expenditure. And this 70 billion dollars would be available, even if Congress refused to appropriate a single dollar for 1953. Actually, of course, expenditures from 1953 appropriations will be added to the 70 billion dollar carry-over.

# RESTRICTED

# RESTRICTED

856

Military expenditures are rising rapidly and will continue to rise in the months ahead. During the last quarter of fiscal 1951, expenditures for the military functions of the Department of Defense and MDAP were running at an annual rate of 29 billion dollars. For the first quarter of the current fiscal year the rate had increased to about 35 billion dollars, and it is now estimated that in the last quarter of fiscal year 1952 expenditures will rise to an annual rate of about 50 billion dollars. It is also estimated that this rate will continue to rise during fiscal 1953 and might possibly reach an annual rate of about 60 billion dollars at the end of 1953.

On the basis of these trends, we currently estimate that total budget expenditures for 1953 will exceed 80 billion dollars. About 75 percent of this total will go to finance major national security programs--military functions, foreign aid, stockpiling, atomic energy and others--while the remainder will be spend for interest on the public debt, veterans' benefits, and other government programs.

Nor does there seem to be any prospect at present that expenditures in fiscal year 1954 will be lower. The military program on which the 1952 Budget was based anticipated a gradual leveling off in the rate of expansion in national security programs during fiscal year 1954, but recent increases in the military program, together with slippages in delivery schedules, may keep defense expenditures at a high rate throughout fiscal 1954.

Unless there is a change in tax laws, budget receipts in 1953 will not increase as rapidly as expenditures. Relatively small increases in receipts, reflecting the larger incomes of individuals and business firms, are anticipated. Even with this gradual increase in receipts, however, it now seems apparent that budget deficits for 1953 and 1954 under present tax laws will be somewhat larger than the forecast for 1952.

The most difficult economic problem which we as a nation face over the next few years is the problem of controlling inflation. Even without budget deficits the Nation faces a potentially dangerous inflationary situation. Large increases in defense spending by the Federal Government have increased incomes of consumers and business and at the same time decreased the amounts of materials and consumers' goods which are available. Federal defense programs generate demand for goods and services many months in advance of actual expenditures. Holders of Government contracts must order materials and equipment and hire labor before they can begin to produce and deliver goods. The peak in contract letting has not yet been reached and will probably not come until later in the current fiscal year. This means that inflationary pressures have not yet reached their peak.

# RESTRICTED

# RESTRICTED

833

The cumulative effect of a series of large budget deficits on an economy which is already generating strong inflationary pressures could be extremely serious.

Thus all of us have continuing and urgent responsibility to do everything we can to lessen the danger of inflation through budgetary action.

It is only natural that our first response to this challenge should be to investigate thoroughly the possibility of reducing the size of the anticipated deficits by drastically curtailing so-called nondefense expenditures. Let us examine this possibility.

The greatest difficulty we face in trying to effect significant reductions in expenditures in this nondefense area arises from the fact that it is composed chiefly of a large number of fixed commitments which cannot be altered through the budgetary or appropriation process in any one fiscal year. The first and largest of these fixed commitments is interest on the public debt. Payments to holders of the public debt will amount to 6 billion dollars in this fiscal year.

A second type of commitment stems from basic legislation previously enacted by Congress which directs the Government to undertake certain programs which inevitably result in higher expenditures. For example, when Congress passed the Servicemen's Readjustment Act of 1944, authorizing educational and readjustment benefits for veterans of World War II, the Government was legally committed to an expenditure program which will, by the end of this fiscal year, cost the Nation an estimated 18.5 billion dollars.

Again, the Social Security Act of 1935, as amended, authorizes a program of Federal contributions to the States for public assistance which will cost 1.3 billion dollars in this fiscal year. Short of curtailing these programs through changes in basic legislation, neither the executive branch nor the legislative branch can exercise any significant degree of control over budget expenditures in any given fiscal year. The level of expenditures for any of these programs depends not upon governmental determination, but upon the number of veterans who elect to go to college, the number of totally disabled persons who apply at state welfare agencies, or the amount of wheat, cotton, and corn offered by farmers to the Commodity Credit Corporation.

Another type of commitment in the budget stems from the fact that a large portion of our expenditures in any one fiscal year carryover from the obligations incurred in prior years. The Government, like any private company, must pay for goods on order or subject itself to costly suits and claims for failure to carry out its part of a contract.

# RESTRICTED

# RESTRICTED

834

If you subtract from the 20 billion dollar nondefense expenditures those expenditures which the Government must pay because of legislative commitments and prior obligations, you have left only 4 to 5 billion dollars of expenditures which can be effectively controlled through the budget process in a given fiscal year. And within that 5 billion dollars are many important programs which are vital to the functioning of a modern industrial society and to the defense effort, such as the activities of the Coast Guard, Census Bureau, Bureau of Mines, Federal Communications Commission, Forest Service, and the Coast and Geodetic Survey. Moreover, these programs have already been severely cut back in the past two fiscal years. Any further major reductions in these programs would be too small to alter the over-all fiscal situation and would only serve to impair seriously the effectiveness of the Government's operations.

The greatest opportunity for achieving really significant reductions in expenditures lies in the defense area which accounts for about 70 percent of total expenditures. In this area small percentage reductions are far more important dollarwise than the total elimination of programs in the nondefense area. For example, if it were possible to reduce military expenditures by 10 percent, the amount saved would exceed the total amount of controllable expenditures in the nondefense area.

Yet, in the military area, as in the other areas of the budget which we have already discussed, large reductions are difficult to make. First, a large portion of the estimated expenditures in this fiscal year will go to liquidate obligations or contracts which were entered into prior to the beginning of the year. The second difficulty is that we do not know when or where aggression will strike. Thus simultaneously we are faced with the need for a rapid build-up of our armed forces in the short-run future and for a mobilization base which will provide sufficient long-run strength.

Yet there are many actions which can be taken in both the budgetary process and day-to-day operations which can reduce military expenditures without impairing our security. I want to emphasize that the type of actions which I have in mind require improvement in management and programming rather than alterations in the basic assumptions of the military program as to size and composition of forces. Let me list a few of the actions which could be taken:

1. Military requirements for manpower and materials should be screened and rescreened to make sure that computations are correct and that they represent the minimum amounts required to do the job. Attaining accuracy and firmness in these estimates of requirements is a most important task. These estimates are the basis for materials and manpower requirements as well as financial requirements in the budget.

# RESTRICTED

# RESTRICTED

835

If these estimates are inaccurate, the economy is thrown out of balance and the resulting waste will impair the whole defense effort.

2. Production and procurement of easy-to-get, common-supply items, which are used by the military and civilian sectors of the economy alike, must be phased out over as long a period as possible, thus keeping inventory close to actual consumption needs.

3. When adequate reserves of plant capacity are available, stocks of war reserve goods should be held to a minimum.

4. The construction and rehabilitation of facilities and public works which are not absolutely essential to the defense effort should be postponed until after the build-up is completed. In reviewing Department of Defense requests for public works last year, we found, for example, a proposal to spend 15,000 dollars for the rehabilitation of a set of quarters that originally cost only 13,000 dollars. This is a case where a little economy would not impair the defense effort.

5. Significant reductions in operating costs can result from the improvement of the organizational structure of the military establishment, the manpower control system, and procurement and property management techniques.

I do not wish to intimate that the Department of Defense and the military services are not interested in economy. What I am saying is that their interest must be more than academic; for the achievement of economy in the military program is one of the greatest challenges which faces all of us who are concerned with budgeting in this defense emergency. Given an aggressive effort along the lines which I have mentioned, it is entirely possible that we may have more defense, rather than less defense, for the expenditure of fewer dollars.

For this reason I would strongly recommend the application of the same type of policies to the military programs which have already been applied to the so-called nondefense programs in the budget. These policies require that: Estimates for 1953 should plan only for the support of minimum essential service assuming the most economical and efficient operation. All programs should be reviewed in the light of their direct contribution to the defense effort and to essential civilian need.

If these stringent over-all budget policies had been applied by the military services, I do not see how the 24 new Cadillacs could have been proposed by one of them for inclusion in the 1953 budget. The Cadillacs certainly will not make a "direct contribution to the defense effort." It is only reasonable and fair that all nonessentials be eliminated from the budget, no matter where they occur.

RESTRICTED

# RESTRICTED

836

It is extremely important that we lay the foundations of our defense program solidly and carefully during this build-up period. We must do this because hasty actions might lead to overfinancing, inflation, and serious economic dislocations. If this should happen, a sudden relaxation in international tension might leave the United States straining under the burden of maintaining a large military machine without sufficient economic strength to carry the load. Russia would certainly welcome such a situation, for an economic collapse in the United States would serve Soviet ends almost as effectively as a full-scale military defeat.

Thus in formulating the budget, in developing fiscal policies, and in setting the levels of programs--including the military program--all of us must weight the economic risks as well as the security risks. A few months ago a United States Senator took an extremely pessimistic view of the future. "At the rate we are moving," he said on the floor of the Senate, "I can see only two ultimate destinations--military safety at the price of economic disaster or economic safety at the price of military disaster." I do not think the outlook is that gloomy, but his statement at least warns of the principal dangers we must avoid in developing a national budget which will provide for armed strength and long-run, economic stability.

The solution to this problem is not one which concerns only the President and the fiscal officers of the Government. The development of an adequate national budget is the responsibility of all of us in the Government; and it should be of particular concern to you in the Department of Defense who lay the plans and develop the requirements which absorb the greatest portion of our financial resources and a large portion of our productive and human resources. For this reason the initial impetus for the solution of the fiscal problems which I have outlined must come from inside the military services and must stem full appreciation of the fiscal and economic implications of military planning. In the final analysis, workable solutions to problems of such national importance will only come from the intelligent, sustained, and cooperative efforts of all agencies and all officials throughout the Government.

Thank you.

QUESTION: Mr. Lawton, you indicated that all legislation initiated by the executive agencies was reviewed for their budget implications or budget requirements. What I would like to know is, what action is taken to review legislation that is initiated by the Congress itself and how is that integrated into the budget requirements? Approximately what percent of the budget is what we call pork-barrel legislation?

# RESTRICTED

# RESTRICTED

837

MR. LAWTON: Well, as to the process of legislation initiated by the Congress if, as is usual, the committee handling that legislation requests the views of the executive agency on the legislation, those reports are cleared through the Budget Bureau. If a committee, for example, has a piece of legislation and asks the opinion of one or two agencies, those reports come to the Bureau of the Budget. If we find there are other agencies interested, we get comments from those agencies. We will then indicate to the agency submitting the report, before it goes to Congress, whether or not that program or that legislation in its present form is in accord with the President's program. The agency in turn must include that advice in any report it makes to Congress. Sometimes it may be that the advice will be that if amended in a certain way, the legislation will be in accord with the President's program, and the agency may have suggested those same amendments; or we may suggest amendments that may be incorporated. The volume of that is tremendous. We handled 2,000 reports on legislation during the last session of Congress.

The second part of your question as to the effect of legislation on the budget, I might state that in the 1952 Budget the sum of between 7 and 8 billion dollars was in there because of legislation that had been enacted in the Eightieth and Eighty-first Congresses. One large segment of that, of course, was the Military Aid Program, but otherwise, taking that out of the picture, there was probably 2 or 3 billion dollars worth of legislation in there which had been enacted by those other two Congresses and only in there because it had been enacted; sometimes it had been amended.

As to pork-barrel legislation, that is usually applied to public works rather than any other program. The outstanding authorizations on the books at the present time for water control, flood control, power, and things of that sort for the Corps of Engineers alone are about 10 billion dollars worth of projects for which no appropriation has as yet been made in any part. There have been some investigations and surveys made, but there is that much backlog. In the area of total public works, there are unfinanced authorizations worth 18 billion dollars on the books and the Congress is still adding to that legislation. In some cases we have recommended against such legislation; in other cases we have recommended for it.

QUESTION: Mr. Lawton, would you please explain how budget ceilings are derived and the figures that go into making the determinations?

MR. LAWTON: Budget ceilings for particular agencies and sometimes for particular programs depend largely on the economic situation. This is true in the public assistance programs and the price support programs of the Department of Agriculture and programs of that nature. When they depend largely on general economic conditions, we get from the Council

# RESTRICTED

# RESTRICTED

838

of Economic Advisers a preview of what the economic situation is going to look like in the next fiscal year; based on that, plus discussions with agency heads as to any unusual features, they think may assist us in making that decision as to the total level of those programs. In those cases it depends on the question of what we see the total budget picture is going to be.

For example, if we foresee a deficit, we will decide in certain areas that the Government cannot go into expansion. Therefore, we will rule out any new or expanding programs. Perhaps that may be in the public works field; it may be in the field of medical research; or it may be a question of additional housing starts--things of that sort. But largely it is based on those two things--the economic situation which will confront us in the succeeding year or the financial situation faced in that year.

After the review of agencies in the spring of 1951 and a review of the economic and fiscal situation, we made a general decision that there would be no expanded programs, that personnel in general would be held to existing levels. We would have to recognize, of course, Internal Revenue where it had been saddled with that monstrosity of the gambling tax and also with some new legislation which added to the number of taxpayers. We would have to allow for that increase. But in other places we wouldn't attempt to reduce backlogs. Work backlogs would have to remain where they were. Some of the decisions are, to a degree, arbitrary; others are based rather directly on the economic implications of the program.

QUESTION: Mr. Lawton, some of us recently saw a letter in which Mr. Wilson said to the President that the Munitions Board was unable to project its requirements far enough into the future to satisfy ODM. Wouldn't it be possible to set up ceilings, anticipate or estimate ceilings, for three or four years in advance? Admittedly they wouldn't be too accurate but they would allow JCS to project requirements and thus furnish claimants for raw materials several years in advance. Would this be feasible?

MR. LAWTON: Well, I am not too sure that you could get a sufficient degree of accuracy to provide that program, primarily because of a number of changes in technology and so forth which are constantly taking place, where the type of equipment will vary as research and development takes place and where the program as a whole is as undetermined as it is at the present time.

For example, an expansion of the atomic energy program is currently being discussed. I have seen some of the requirements for that program translated into materials and into services such as the generation of power. It has been estimated that that program would take 97 percent

# RESTRICTED

# RESTRICTED

839

of the total available supply of one metal for a five-year period. To make the distinction between that program and other programs competing for that metal would be a difficult thing to do, unless the basic decision is made as to the place of atomic energy warfare versus conventional warfare.

The power demanded ran up to several million kilowatts, which is a difficult problem at a time when you are straining for copper for a number of other things, particularly when you are running rather tight on brass fittings which are consumed in ammunition. If we could make a determination in advance as to exactly what our force and strategic commitments are or what our strategic needs would be for the next four or five years, possibly we could translate it into the material situation, but I don't believe there is any greater degree of firmness to that than there is to materials at the present time.

QUESTION: Mr. Lawton, in more nearly normal times than these, how does the Bureau of the Budget reconcile its decisions on ceilings for programs which have been based upon decisions or recommendations by the National Security Council?

MR. LAWTON: In the first place you are implying that they are purely budgetary decisions by the Bureau of the Budget. That is not completely the case. The decisions in many cases have been made by the Chairman of the National Security Council, the President. I assume you may be referring to ceiling process applied to the military services a few years back. That case was decided largely on one basis--how much of our total economy do we feel it is necessary to utilize for defense purposes? It was the relationship of defense dollars against total dollars in the budget, against a total of income, a total of economic level then prevailing in the United States. It was really a question--putting it in its simplest terms--of how much of our total availability of dollars that we can foresee through normal receipts should be applied to defense and how much should be applied to those programs for increasing the development of the national economy.

QUESTION: I visualize literally hundreds of people working in this budget area in the Department of Defense. What is the number of examiners--whatever you call them--in your shop working on this Department of Defense budget, what are their grades, what is their training in the whole area, what is their significance in relation to the hundreds of people working within the Department of Defense?

MR. LAWTON: Well, I hope these people are working because I would like to see that Defense budget in detail pretty soon if I am going to get it in the next budget.

# RESTRICTED

# RESTRICTED

8-10

More directly to your question, the number varies between 25 and 30 people who deal with the budgets of the Department of Defense. A great many of those people have been in the military services organization. I think about two-thirds or three-fourths of them have had military experience. In a good many cases they have been budget makers or budget examiners in the Department of Defense--some of them during the past war, and some of them at an earlier date. Their grades vary from 13 to 15, with maybe two or three in 11 or 12. Most of them are in grades from 13 to 15. Their competence is based primarily on the education, training, and experience they have actually had in the development of budget operations, budget techniques, budget examinations within the Bureau of the Budget and in other areas of the Government.

They are not strategists; don't attempt to be. The point of departure from which they start is the approved levels for structure and number of men set by the President. The question of missions is one that we don't get into very often except in a case such as we found where the Defense Department was operating under a ceiling and didn't want to make the decision as to which of two agencies would have a certain mission. Both of them had the money in the budget for it. Now our only decision in a case like that is, "We will provide for the mission, provide the dollars necessary for it; you decide who is going to do it. We won't provide for it twice."

On the mathematical type of estimate such as pay allowances, things of that sort, a person with accounting competence is as well, or better perhaps, equipped to deal with that as one with any other background. I think the people in the research field are relatively competent, at least they are competent enough for the Research and Development Board to try to take them at a higher grade.

QUESTION: The amount of money in the present-day budget is misleading in that a dollar now even on the basis of the 59-cent dollar in 1933, doesn't buy nearly so much as it did two or three years ago. Does the Bureau of the Budget have a figure for the price of the dollar now?

MR. LAWTON: I think that in that period of time the general price range has gone up, the wholesale prices, for example, about 170 percent. Salaries have gone up 80 percent; private salaries have gone up more than that--little over 100 percent. Of course, you have all this doubling of a number of things that get into these programs, both labor and material costs, but it is not solely that. That is the change in the defense program. There is the question of the type of weapons which are now so vastly different from the guns that we used in the period of 20 years ago and the extremely high cost of that type of weapon. There is the whole electronics field, guided missiles, and

# RESTRICTED

# RESTRICTED

841

things of that sort, which are very different from the conventional type of artillery shell or artillery piece you were buying in the midthirties. The gadgets, if you will, that have been added to all types of equipment are really the main elements in the increased cost; the greater increase in firepower that we find now as compared with the World War I device. The World War II device is costly to obtain and to maintain. We haven't attempted to distinguish between the basic costs, given the same item, that might occur in the present budget as against one that occurred 20 years ago, 25 years ago, or 10 years ago, or 3. We haven't attempted to decide how much of the cost is based on new types of weapons, a higher cost type, as against certain basic components that might be the same in both years except for changes in price.

Again you have in this current program the same thing that faced you in the beginning of World War II, in the building-up stage and in the development stage of many of these items of equipment the cost is much higher than it will be as you get into quantity production at some later point. The present concept of a couple of Air Force planes that are in the developmental stage is extremely high per plane, but when you get into production, you will have a vastly decreased cost. I couldn't give you a real guess as to how much of the cost of this program is due to change in prices and how much is due to a change in the type of equipment.

QUESTION: The amount of money being spent by the Department of Defense is a lot for peacetime but we are not at real peace. Can you tell how much the Korean affair is costing us as provided for in this year's or next year's budget?

MR. LAWTON: No. Neither can the Department of Defense. The only thing I know is that the Department promised us a supplemental for 1953 of about 2 billion dollars, which is considered to be additional Korean costs, but it is an almost impossible task to make the actual distinction.

You could pick some items of transportation, things like that; you can definitely pick out the cost of moving equipment over there; you could make some guess as to the cost of excess attrition. But, as you know, in the budget for this year we have assumed only peacetime attrition for Korea. Now the difference that the Department says will be made by a continuation of fighting is a couple of billion dollars. When we actually get that estimate, the picture may change, but I know when the Department has attempted to make some figures available to the committees at various times, it has cushioned them so heavily that nobody could rely on them.

# RESTRICTED

# RESTRICTED

842

QUESTION: Mr. Lawton, would you care to comment on the impact of the performance type of budget that the military people are burdened with now and the review and evaluation that you people are concerned with?

MR. LAWTON: The Air Force started off with a performance budget. I think it is much easier for us to get a picture of the program from the present performance type of budget than it was. Our only prior experience was where it was intermingled with the Army budget, both here in the War Department and the Navy. With the performance budget, I think we are able to get a clearer picture of actual ultimate uses of funds and look at them on a program basis in a total picture for a program rather than trying to fit the parts of it from several different spots.

The burden which you have picked up, of course, was one advocated strongly by the Department of Defense and the Secretary of Defense's office and involved an amendment to the National Security Act.

The attempt toward a performance budget generally has been on the basis that you can find from the budget what you are spending the money for rather than solely how you are spending it. You get the budget based on the term "end cost" or "end programs" rather than on how many oyster forks, things of that sort, you need to buy.

QUESTION: Some of the appropriations that are made are on a "good until used" basis, but the vast bulk of them are on a one-year basis, which means that the unexpended balance goes back to the Treasury. That leads to wasteful use of that money toward the end of the year rather than lose it. I wonder why it wouldn't be better to have more expenditures on this "good until used" basis. Can you throw any light on that?

MR. LAWTON: There have been a number of discussions as to whether or not you would budget on a continuing basis and provide in a sense continuing contract authority--which is what it would amount to--with annualization, or extend the basis "good until used." There are a few items in the budget that have a five-year life; some have a two-year life; some have a life "good until expended; then, as you say, the bulk of them are on an annual basis. I think it depends a great deal on the type of program. For a program that involves large expenditures for construction which will take two or three years, there is no sense of trying to annualize that program. While they would normally have been on an annual basis, they were actually renewed from year to year, so the funds continued to be available throughout the period of the war.

RESTRICTED

# RESTRICTED

843

The problem of end of the year expenditures is one that I think is somewhat overstated. The rush to get funds used which has been cited at times has been in some cases because of the method of planning programs. Under some types of program it may have been necessary to make sure that certain personnel costs were met for a full year and in order to be sure of getting them, you held back on procurement until the latter part of the year.

The Chamber of Commerce put out a booklet, which got wide circulation during the latter part of the last fiscal year, about the horrible example of government purchasing in going out to spend huge amounts of money in June. Actually if you take the public debt interest out of the budget, there were five months of the year which were higher than June. I may also use as an example the last day of June when the Government did put a billion dollars into the market. Actually a large part of that was interest on trust funds; 250 million was veterans' bonuses which were to reach the veterans on the first of July and were expended from the Treasury on June 30 and mailed on that date.

Now the rush to expend, I don't believe is governed nearly so much by the annualization of appropriations as it is by procurement practices within the agencies. In many cases it is not a case of getting rid of the money; it is a case of inability to decide just what are the priorities of the things they want. As they reach the end of the year they have to make a decision as to which of those things they will buy because they are going to lose the money. It is simpler in the large, continuing procurement where you have long lead time. I think it would probably be an advantage in that case to provide for a continuing appropriation. In cases where you are going to buy over a two- or three-year period, you want to have the opportunity to decide as late as possible the kind of model and the latest improvement you can get. Of course, that works in reverse. Many times money may be available and you keep trying to get something a little bit better.

COLONEL HARDENBERGH: Mr. Lawton, on behalf of both colleges I thank you for a very informative lecture and an interesting discussion period.

(28 Feb 1952--350)S/en

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