

THE FEDERAL BUDGET

10 October 1955

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10 October 1955

CAPTAIN GERWICK: Good morning, gentlemen. This is the third and last budget lecture in the Economic Stabilization Unit. It is entitled, most appropriately, "The Federal Budget."

I am sorry to have to tell you that the Director of the Bureau of the Budget, Mr. Hughes, was unable to get here this morning. He is out of town on a speaking tour and did not get back. I am glad, however, to be able to tell you that the Deputy Director prepared himself for just such an emergency. In fact, I know he worked all day Saturday on it. Before he came to this job, he was the senior partner of Price, Waterhouse and Co., of New York City. He has been the Deputy Director of the Bureau of the Budget for over a year and a half. He is no newcomer to this subject.

It is a pleasure to introduce to this class Mr. Percival F. Brundage.

MR. BRUNDAGE: Good morning. I appreciate very much the opportunity to substitute for the Director before this group. I also am glad that you are giving the time you are to budgeting, because I feel that it is a tremendously important subject for all of us. It is of immediate consequence to you who are concerned with our national security programs, because those programs take over three-fifths of our total expenditures.

The budget directly affects our lives, yours and mine, as taxpayers, since it necessitates paying over to the Federal Government such a large proportion of our individual incomes. It affects us also through its influence on the entire economy of the nation, since the Federal expenditures amount to about one-fifth, 20 percent, of the national income. Furthermore, the budget mirrors and focuses the basic policies of the Federal Government--foreign, military, and domestic--and what those policies may be is of crucial importance to all of us as military and civilian officials and as citizens.

In view of the importance of the Federal budget, it may surprise you to know that until thirty-odd years ago there was no integrated budget for the entire Government. Until that time, each of the departments prepared and sent its requests for appropriations to the

Congress as part of what was known as the Treasury's Book of Estimates, without regard to what the other departments and agencies were doing, and without any regard for the total amount that all of the agencies were requesting. The Secretary of the Treasury, who transmitted these estimates to the Congress, had no responsibility except to receive and pass them along, a business which occupied the time of one Treasury official.

At the close of World War I, Congress finally took up the problem of budgetary reform, stimulated largely by the wartime expansion of Federal activities and the sharp increase in the public debt, which had risen twenty-fold from 1915 to 1919--from 1.2 billion to 25.5 billion dollars. Their discussions resulted in the passage of the Budget and Accounting Act of 1921, the basic elements of the philosophy of which are (1) that the President himself assume responsibility for the budget, thus eliminating the concept of departmental self-determination; (2) that the budget is the financial expression of the Government's program for the fiscal year; (3) that the budgetary process is designed to eliminate duplication, waste, and inefficiency, both within and between agencies, and that this is achieved by a supra-agency review; (4) that the budgetary process is used as a device for obtaining better administrative management, as well as for fiscal planning and control; and (5) that the budget should clearly indicate the relationships between proposed expenditures and anticipated revenues.

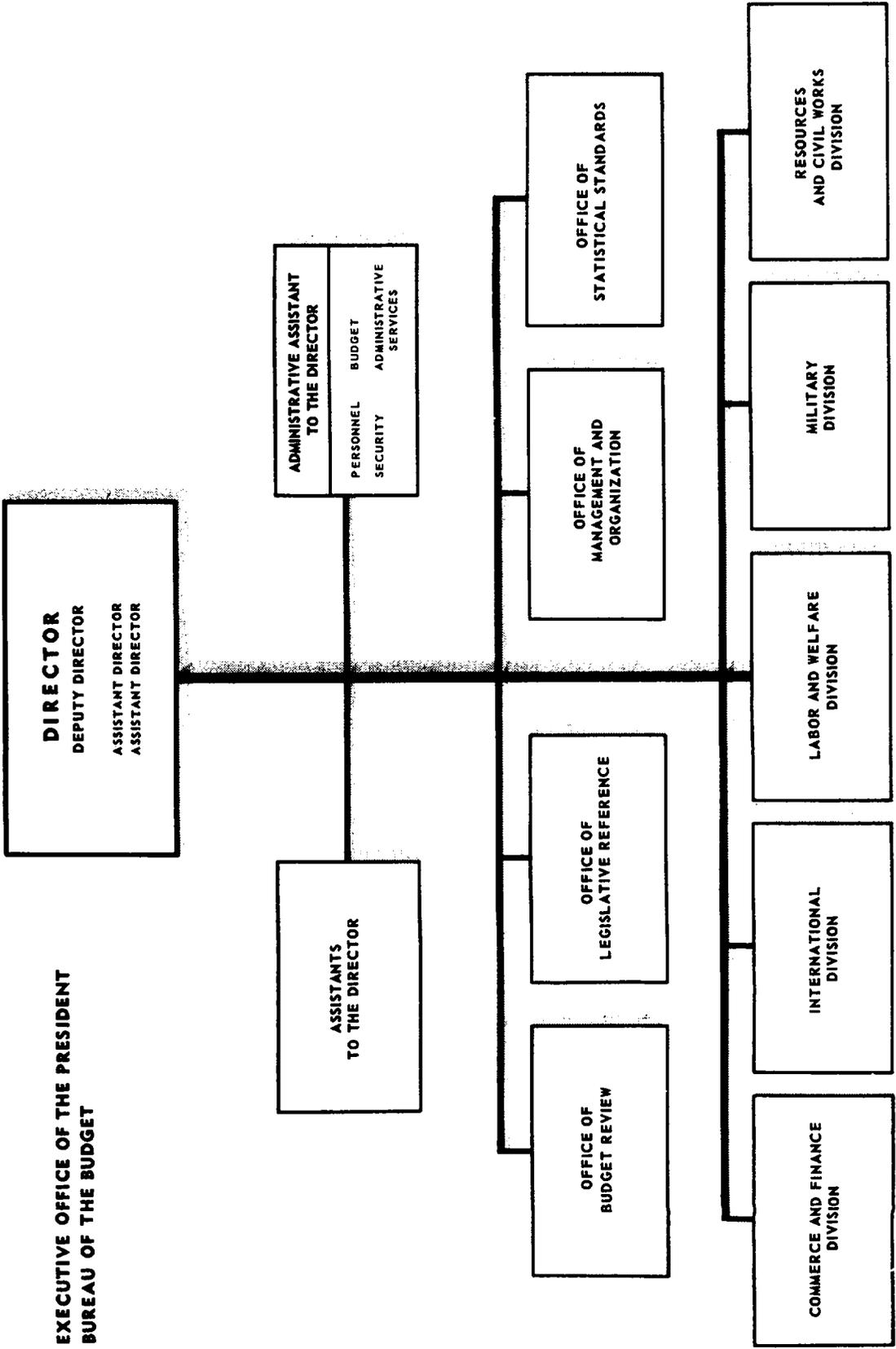
I am going to start with a few words about the Bureau of the Budget itself and its organization.

Chart 1, page 3, gives the general setup. You see, the Bureau is administered by a Director, a Deputy Director, and two Assistant Directors. There are four offices: one for Budget Review, one for Legislative Reference, one for Management and Organization and one for Statistical Standards. Each of those is headed by a career Assistant Director. Below these are the five divisions which principally have to do with the budget process--the Commerce and Finance, International, Labor and Welfare, Military, and Resources and Civil Works Divisions. Each is headed by a career Chief of division. We have a total staff of about 420.

Many think the Bureau of the Budget is engaged solely in the business of budget making, which, of course, is the largest part of our duties. But it is only part, as you will see from this chart.

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CHART 1



**EXECUTIVE OFFICE OF THE PRESIDENT
BUREAU OF THE BUDGET**

ASSISTANTS TO THE DIRECTOR

ADMINISTRATIVE ASSISTANT TO THE DIRECTOR	
PERSONNEL SECURITY	BUDGET ADMINISTRATIVE SERVICES

OFFICE OF BUDGET REVIEW

OFFICE OF LEGISLATIVE REFERENCE

OFFICE OF MANAGEMENT AND ORGANIZATION

OFFICE OF STATISTICAL STANDARDS

COMMERCE AND FINANCE DIVISION

INTERNATIONAL DIVISION

LABOR AND WELFARE DIVISION

MILITARY DIVISION

RESOURCES AND CIVIL WORKS DIVISION

Now, the Office of Budget Review assumes responsibility for the complex technical job of planning, scheduling, and controlling the preparation of the budget, ranging from the preliminary economic analysis of conditions in the year to be covered, through the preparation of material for submission to the President and to the Cabinet for their decision, to the final printing of the budget document which is submitted to Congress.

I think you will be interested in these other activities too, because they do have an impact on your own activities.

One of the other duties of the Bureau is conducted by the Office of Legislative Reference. Proposals for new legislation are sent to the Bureau by all Government agencies prior to their submission to the Congress, so that they can be analyzed for budgetary implications and can be coordinated with other interested agencies, to prevent conflicting recommendations, and so that the President can determine the relationship of each proposal to his own general program.

The Bureau also reviews and coordinates agency comments on legislation proposed by members of the Congress, and furnishes advice to congressional committees on the relationship of all legislation to the President's program. So far this calendar year, for example, over 5,700 draft bills, congressional requests for Bureau views, and agency reports on pending legislation have been acted on by this office.

Legislation, when passed by the Congress and forwarded to the President, is handled by the Bureau in a similar manner. The Bureau supplies the President with the views of the interested agencies as to whether approval or veto is recommended, as well as any draft documents that may be required to carry out the legislation by executive action.

The next office, that of Management and Organization, develops programs designed to improve the organization and management of the executive branch, including the organization and relationship of executive agencies, and Government-wide management and service activities, such as personnel and accounting. For example, it develops and reviews reorganization plans and other proposals for placing Government functions where they can be administered most appropriately and most economically, such as the recent organization of the International Cooperation Administration (ICA), within the Department of State to take the place of the independent FOA.

Another principal responsibility of this office at the moment is the coordination of the views of all Government agencies on the recent reports of the Hoover Commission.

The fourth office, that of Statistical Standards, is responsible for improvement of the Government's statistical activities. It reviews statistical forms proposed by various Federal agencies, develops and improves statistical techniques and standards, and maintains surveillance over the publication of statistical data from the point of view of national security. For instance, when the unemployment statements published by two of the departments didn't agree, we had to go into the formulation of the basic assumptions and reconcile them. It also serves as the focal point for United States participation in statistical activities of international organizations.

Each Government agency, with very few exceptions, must obtain the Bureau's approval for each questionnaire which is to be sent out to more than ten persons. About ten or a dozen such questionnaires are proposed by the different agencies each working day of the year. You would be surprised how many people want information through questionnaires. Each new questionnaire is examined to make sure that the information it would obtain is necessary and is not already available in some other place, that the form is as simple as possible and conforms to business record-keeping practices, that it is sent to the smallest possible number of persons, and that it is collected no more frequently than is necessary.

This office reviews the release of statistical data by Federal agencies, to determine the need for restrictions in the interest of national security. In this activity the office is aided by a committee representing the security and intelligence agencies of the Government, and also by an advisory council of businessmen, which serves without compensation. This office has saved business and industry many unreasonable or unnecessary demands for information and the tremendous cost of developing the replies.

Now, every agency in the Government is assigned to one of the five divisions shown in the lower line of the chart. Each division has a staff of examiners, whose business it is continuously to analyze reports and operations of every phase of the agency's activities--this goes on throughout the year--and their relation to budget and legislative requirements.

Some divisions also have important nonbudgetary responsibilities. The Commerce and Finance Division, for example, has initial responsibility relative to the Bureau of the Budget's function of advising the President respecting international air route certificates. The Labor and Welfare Division has a continuing responsibility for coordination and review of the Federal hospital system. The Resources and Civil Works Division has responsibility for helping in the review and development of long-range plans for Federal public works and improvement projects, as well as for coordinating the Government's mapping and surveying activities.

With regard to the process of budget formulation, it is important to realize that the period during which the budget draws greatest public attention, that is to say, following the President's submission of his January budget message to Congress, and during the congressional review which follows that period, is comparable to that portion of an iceberg which is visible above water. There is a lot more to it than that. Many months of arduous work precede the President's budget message to Congress.

Leaving the military budget aside for the moment, the preparation of the budget for all the other departments and agencies follows this general procedure: In May and June--for instance, this last May and June of 1955, we started formulating guidelines for the preparation of the fiscal year 1957 budget, which will start next 1 July--well over a year ahead of the beginning of the fiscal year. First we develop the policies that will be applied; that is, the fiscal interpretations, the economic assumptions, and the domestic and international forecasts. Preliminary discussions are held with the heads of the principal agencies to determine what new programs, if any, will be required; what extensions of old programs are desirable or necessary; and what reductions or terminations of existing programs are possible.

We then develop and discuss with the President and the Cabinet a preliminary overall estimate as to the probable expenditure level as compared with the Treasury estimates of what the receipts, based on current legislation, are likely to be. An overall ceiling on controllable costs is then established for each individual agency, which is then advised of our decision and asked to submit a detailed estimate and justification for the ensuing fiscal year, based on the policies which have been set forth. The normal date for the receipt of these estimates is between the middle and end of September.

During this same period, between June and September, the Bureau of the Budget, as always, is working on the results of three fiscal years. During the past three months we have been compiling the final results for the fiscal year just ended 30 June 1955. At the same time we have prepared revised estimates for the fiscal year just commencing on 1 July 1955. And, as I have just indicated, we are working on preliminary estimates for fiscal 1957.

Now, during the months of October and November the Bureau of the Budget holds hearings with each of the agencies, at which top officials appear and present their detailed justifications for their proposed programs. The recommendations by the examiners as a result of these hearings and their own detailed reviews are then considered at what is called the Director's review. The Deputy Director and the Assistant Directors, together with the top staff of the Bureau, sit down together with the examiners to discuss the issues arising from the agency requests and the major questions of program and policy in the light of the appropriation requests from all the other agencies and the general budget policy.

Turning now to the military budget, we have a slightly different course, because of its size. In all three budgets with which the present Administration has had to deal, that is, the revised 1954 budget, and the 1955 and 1956 budgets, all decisions made with respect to governing military policies, such as force levels and procurement objectives, were thoroughly discussed with the National Security Council, with the Joint Chiefs of Staff, and with the President, and had his approval before budget action to carry them out was even formulated.

Because the objectives of the Secretary of Defense are essentially the same of those of the Executive Office, and in order to avoid duplicate demands within limited time periods, the Military Division of the Bureau of the Budget works with the staff and the Assistant Secretaries of the Department of Defense in reviewing the proposals of the three services. I understand that you have already had a talk from Secretary McNeil, and that he referred to this joint work.

After submission of the budget estimates by the Secretary of Defense, an evaluation is made in relation to existing policies and proposals; and possible modifications are discussed again in the Security Council, with the Cabinet, and the President. The budget is thus based on policies established by the President after consideration of recommendations by the Joint Chiefs of Staff and Defense officials.

It must be remembered that there is only one individual who can present a budget under the law to the Congress--the President of the United States. It is his budget and his recommendations to the Congress.

One other factor you might bear in mind when you consider military expenditures is that the President's decisions have been made not only as Commander-in-Chief, but also on the basis of his experience in his distinguished career in the military service. He has given especially close personal attention to the military section of the budget. The ultimate decisions have been his and, I think, can be accepted as authoritative.

In November and December, after consideration of the military and other budgets, the final estimates are prepared, and the budget document is sent to the printer. Under the law, the **budget must be** transmitted to the Congress, together with the **budget message**, within the first fifteen days after the session of Congress opens. That is why we have to be so exacting and have to bring so much pressure to bear on the various agencies to have their presentation and figures in on time.

The budget document itself serves not only as a budget estimate for the fiscal year beginning six months after the budget message, but also contains the revised estimates for the fiscal year then current, and the actual results for the fiscal year which has ended six months previously. Therefore it serves as an annual report on the operations of the Government and all of its departments, as well as containing the budget estimates for the coming fiscal period.

Now, before we go into the further charts and figures, there is one fact I might bring to your attention. While the budget is one document, it contains two different sets of figures, which are sometimes confusing--those relating to obligational authority and expenditures.

The budget, in the first place, shows how much money the President requests from Congress each year to carry out the present and proposed programs of the Government. These requests become the appropriation bills which Congress considers and acts upon. Appropriations provide the authority--usually called "NOA--New Obligational Authority"--for Federal agencies to spend money, but the money itself must be raised by the Treasury through taxes or by borrowing.

The budget also shows, in the second place, the estimates of how much money the Government is expected actually to spend each year

in carrying out those programs, and how much it will receive from taxes and other sources. Here we see whether the budget is balanced or unbalanced. If the amount received in revenues is greater than the amount spent, the budget is balanced and the Government has a surplus for the year. If the expenditures exceed receipts, the Government has a deficit.

Under our Constitution, no one in the Government may spend money until an appropriation law is first enacted by Congress. However, the amount of appropriations passed by Congress for any one year and the amount which the Government spends in that year may be very different. This is true because only part of the funds appropriated and obligated for a certain year are spent in that year. The balance may be spent the following year, or, in the case of long-lead-time items, several years later.

Funds spent in any one year, therefore, come both from appropriations voted by Congress for that year and from funds voted in earlier years. For example, money for Government employees' salaries is usually spent in the same year for which it is appropriated. On the other hand, most of the money for jet planes and aircraft carriers is spent several years after it has been appropriated. This delay, of course, occurs because of the time it takes to order, produce, and deliver the planes and ships.

In some years the dollar amount of appropriations will therefore be smaller than the expenditures. In other years it may be larger. The effect of this difference between appropriations and expenditures will show up a little more clearly in a chart I shall show in a minute.

Now, the present Administration took office on a platform which called for reduced Government expenditures, reduced taxes, and the achievement of a balanced budget. Our budgetary and fiscal policies, however, have been considered and must be considered in relation to the broad objectives of our national policies. I shall try to describe for you some of the steps we have taken to return to financial stability. We have tried to strike a balance between (1) wise fiscal and budgetary management, (2) a sound and effective program of national security, and (3) a strong and expanding economy contributory to the general welfare and readily convertible to the tasks of war should this prove necessary.

Taking our objectives one at a time, but remembering that a balance between these objectives is what we must attain, the principal

goals of our fiscal and budgetary management continue to be: (1) reductions in Government spending, (2) reductions in taxes, and (3) achievement of a balanced budget. The level of our total expenditures--64.5 billion dollars--the first figure on this chart is expenditures and the second figure is revenue--in 1955, you see, is greater, we feel, than our taxpayers are likely to be willing to provide over an indefinite period. The high rates of corporate and individual taxes take too large a proportion of our national income, and we must face that fact. But under present circumstances we cannot reduce taxes without reducing spending, because an unbalanced budget encourages inflation, which in turn creates hardships on many levels of our society and creates a larger debt for our children to pay.

The simplest way to indicate the measure of progress that we have made toward these goals is to compare the latest budget estimates for 1956, the current fiscal year, which just began last July, of 63.8 billion dollars, with the previous Administration's budget recommendation for 1954, which confronted the President when he assumed office.

Chart 2, page 11. --The actual expenditures for 1953 were 74.3 billion dollars, but they had budgeted 77.9 billion dollars for the following year, 1954.

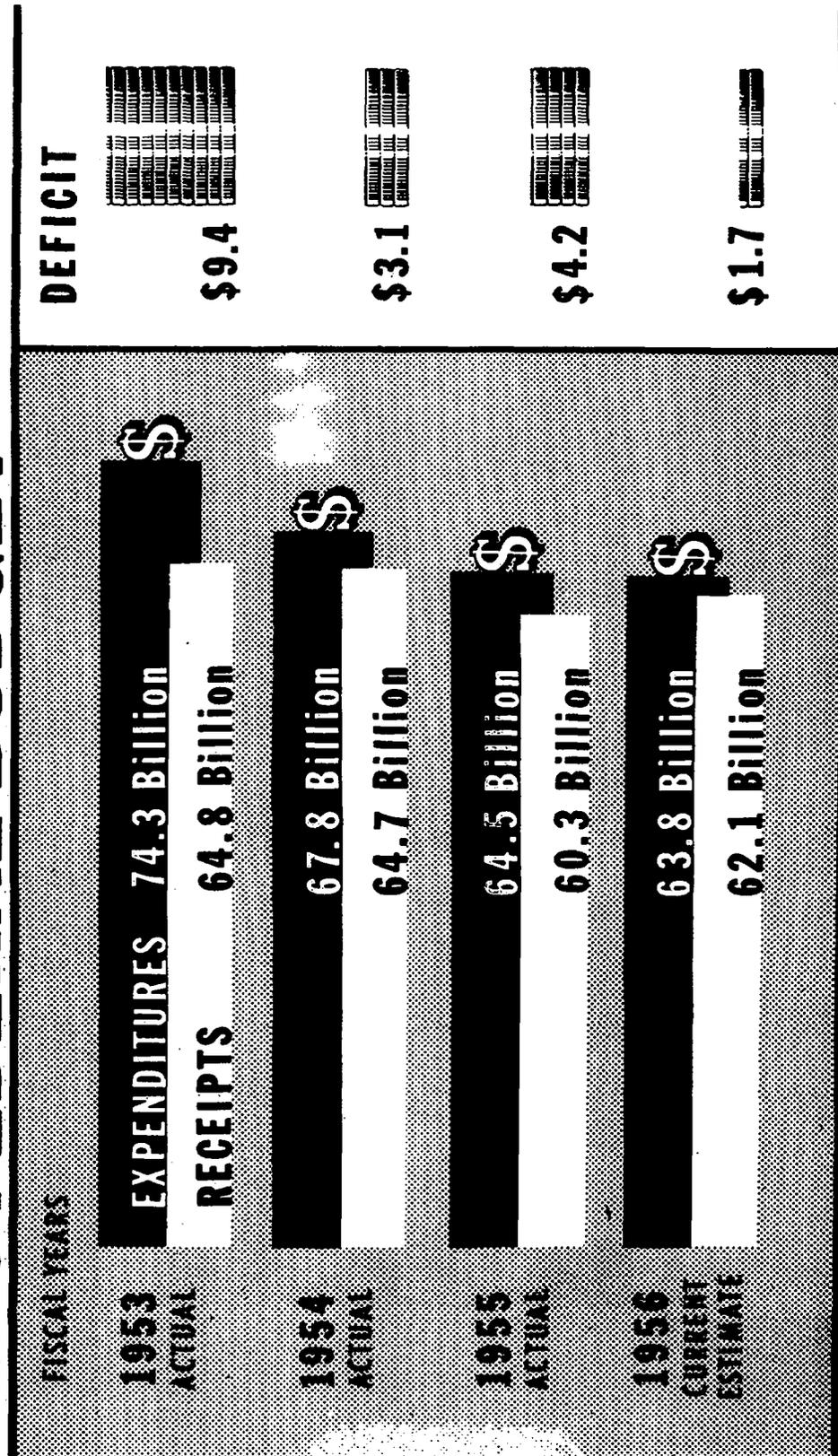
Now, Federal spending is being reduced for the third consecutive year. The net Federal expenditures for the current year are presently estimated to be 14.1 billion dollars less than the recommended 1954 budget of the previous Administration. On a per capita basis this has meant a reduction from 484 dollars per person to 383 dollars per person in the United States, or an expenditure reduction of about one hundred dollars for every man, woman, and child in the nation.

Equally as important as current spending is the trend of future expenditures. These are largely governed by two factors: the total of new appropriations for a given year, and the backlog of unexpended balances from appropriations of prior years.

The appropriations line (chart 3, page 12), starts above 90 billion, as you see, in 1952--that is after Korea--and has come down below 60 billion dollars in 1955, and has gone back a little in 1956. As anticipated for 1956, new spending authority is about 10.5 billion dollars less than recommended for 1954 by the outgoing Administration, about 18.5 billion dollars less than was enacted in 1953, and nearly 30 billion dollars below 1952.

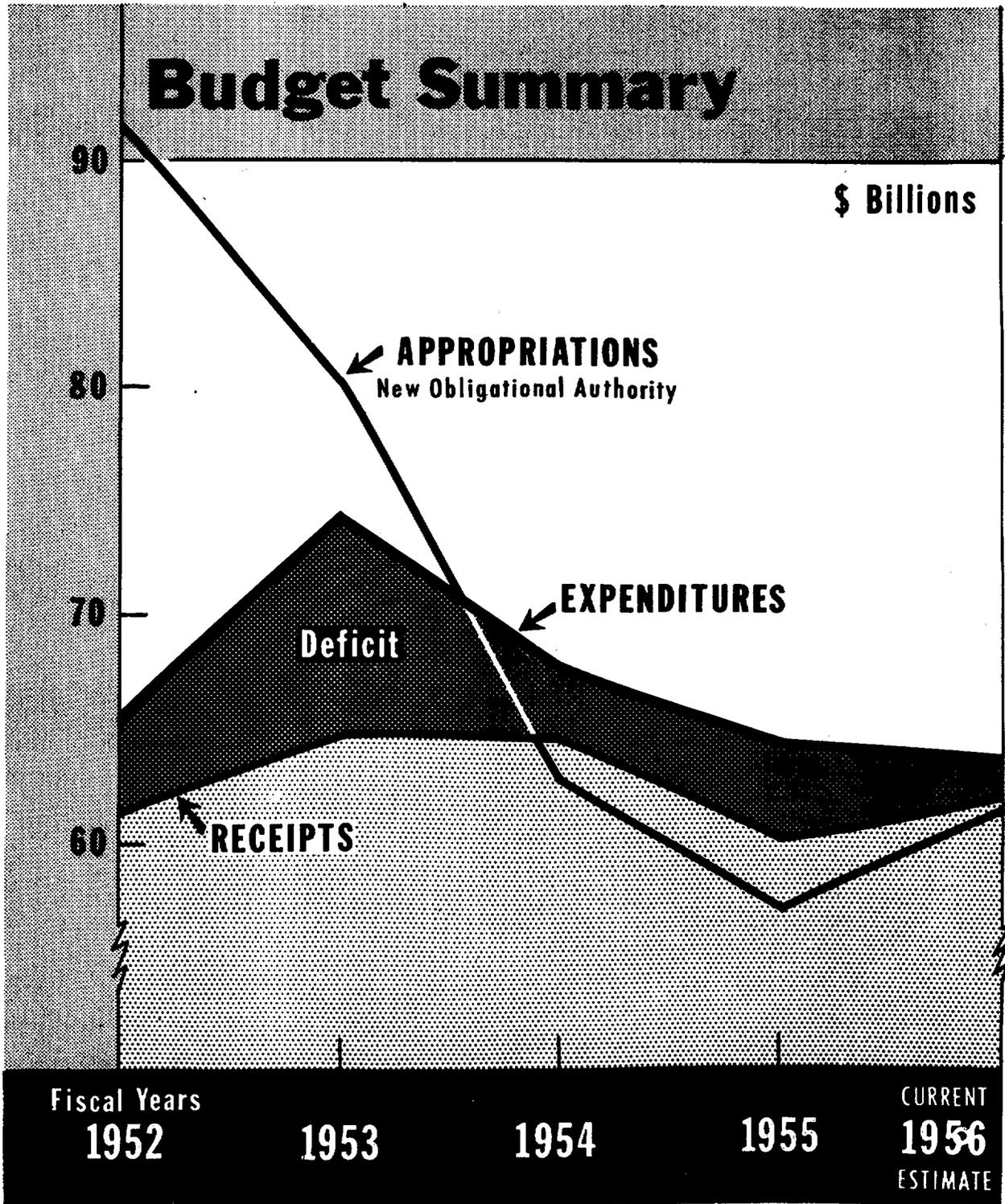
CHART 2

The FEDERAL BUDGET



Executive Office of the President • Bureau of the Budget

CHART 3



Executive Office of the President • Bureau of the Budget

New spending authority, therefore, has been kept below receipts and expenditures in each year since 1953, as you see. The receipts line is below the expenditures line in every year. But the appropriations line goes down below the receipts line between 1953 and 1954. In other words, we have been paying our way on the current basis; and the present problem arises primarily from the overhanging backlog of spending authority.

In the second place, the balances of appropriations carried over from prior years amounted to nearly 80 billion dollars when the present Administration took office. By the end of the current year it will be about 50 billion dollars, a reduction of well over one-third. This action, combined with the reduced levels of new spending authority, forecasts, I believe, lower expenditures in the future and an eventual balancing of the budget.

The deficit picture over the past few years can be seen in this chart at the top in red. Our present estimate of the budget deficit for 1956 is 1.7 billion dollars, which is the lowest estimate in five fiscal years. This, of course, is made in August, which is ten months before the end of our current fiscal year--next June 30th. You may be certain that, since an expenditure reduction of less than three percent could bring the budget into balance, we are doing all we can, without sacrificing our objectives of military and economic strength, fiscal soundness, and the welfare of the country, to reduce those expenditures and end up with a balanced budget. Our economy is strong and prosperous at the present, and taxes are high. We are determined not to dissipate our economic strength through inflationary deficits if we can possibly avoid them.

These reductions in Federal expenditures have been of such magnitude that they are not easy to obtain. They have been achieved by thrift and frugality, by a continuous effort to eliminate red tape, waste, and duplication, and to find better and less expensive ways of doing the things the Government must do.

In the Department of Defense last year alone, nearly 170,000 separate suggestions for improvements in operations were reviewed. Hundreds of examples of economies could be listed. I might just mention a very few.

The Air Force will save a million dollars a year by eliminating winter underwear as a mandatory item of issue.

The State Department estimates that it will save 40,000 dollars annually by reducing the number of blank pages in their passports.

The General Services Administration estimates substantial savings through standardization of office supplies. It is estimated, for example, that a million dollars a year will be saved by reducing the number of types of mimeograph paper from 172 to 17. Other comparable savings will result from reducing the present ten varieties of paper clips to four, blotting paper from twenty-four to five, and paper towels from eighteen to seven.

The use of commercial specifications instead of special Government specifications will lead to savings in several fields. GSA estimates substantial savings through the purchase of standard two-ounce bottles of ink instead of a special one-and-three-quarter-ounce, non-commercial bottle, which has been required for a couple of generations. The Army estimates annual savings of 246,000 dollars by the purchase of commercial-grade 50-grain vinegar instead of the 40-grain vinegar which had for years been especially manufactured just for the Government.

By revising its maintenance techniques and eliminating superfluous requirements for disassembly, the Air Force has reported that it will be able to get three aircraft of the same type repaired for the previous price of two. Resultant savings are estimated to exceed 100 million dollars a year.

Another significant achievement--in which it is presently difficult to estimate the exact dollar saving--is the outstanding progress made by the Army in developing financial accounting for its worldwide inventories. Since it has been estimated that Army inventories of supplies and equipment equal or exceed those of all United States retailers combined, the savings which can result from proper control and adjustment of excess inventories promise to run into hundreds of millions of dollars.

These and countless other examples illustrate ways in which it has been possible to reduce the cost of doing the things the Government is doing without sacrificing any programs. When costs are made an issue, savings multiply; and when costs are disregarded, expenses multiply. We must continue to make costs an issue, as we realize that there are thousands of other economies that can be achieved.

Equally as important as how the Government does things is what it is doing. It is here that the policy of reducing expenditures meets its sternest test. Perhaps the simplest overall summary from a budgetary standpoint is to discuss the three principal categories of expenditures as we classify them from the standpoint of controllability: (1) major national security, (2) relatively uncontrollable civil programs, and (3) all other Government programs.

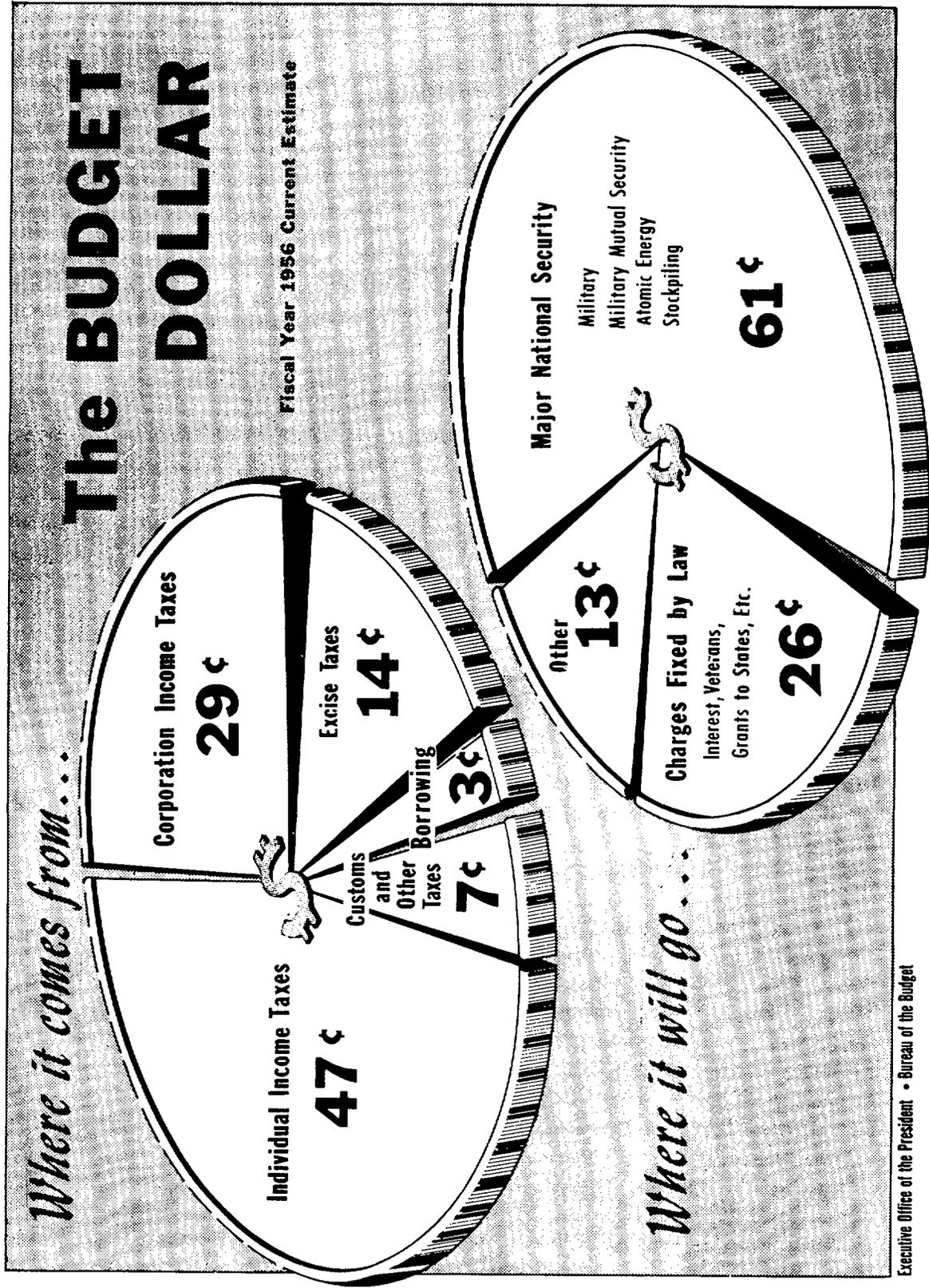
As you will see from chart 4, page 16, this year's national security programs will require approximately 61 percent, or 61 cents out of every dollar, of the total Government expenditures; the relatively uncontrollable programs approximately 26 percent, or 26 cents out of every dollar; and all other Government activities 13 percent.

Take the middle 26 percent category first--those expenditures which by law permit little or no administrative discretion through the budget process, including farm price supports, veterans' pensions, interest on the public debt, and grants to states for various programs--items of that category. Unless Congress revokes the basic legislation, whatever expenditures are required must be made. Year after year, as we approach the budget-making process, we must therefore arbitrarily allot, before we even consider our national security expenditures, a substantial part of our budget for these mandatory programs which are embedded in the law.

By and large, the only likelihood for appreciable change downward in this category of mandatory expenditures would result from revision of the basic legislation. Some future savings, for example, may be possible as the result of congressional action in the last session providing for flexible farm price supports.

Now, budget expenditures for "other Government activities" will have been reduced by about seven percent during the fiscal period from 1953 to 1956, although within the overall category there have been selective increases in some programs and larger decreases for others. This category of expenditures represents less than one-seventh of the total Government expenditures, but includes the great majority of individual budget items, such as civil public works, expenditures for international affairs and finance, and the cost of most of the regular operations of the Government, such as law enforcement and administration, the postal service, and tax collection. The recent recommendations of the Hoover Commission, which are now undergoing intensive study in the executive branch, will be extremely helpful to us in further improving operations.

CHART 4



Now, the expenditures for major national security programs include the military functions of the Department of Defense, military assistance to our allies, atomic energy, and stockpiling of strategic materials. These together comprise three-fifths of the budget. The expenditures in these categories dominate the results for the year.

Coming to the second of the three policy objectives I mentioned earlier--a sound and effective program of national security--it is quite clear in our own minds, and it has been publicly announced by the President, that we will not commit aggression, but that we must always be ready to defeat it. The threat to our security is a continuing and many-sided one; but there is, so far as we can determine, no single critical date and no single form of enemy action to which we can soundly gear all our defense preparations. As you will know, the many radical new inventions and discoveries of recent years seem to have seriously altered the balance between attack and defense. At the present it seems as if a surprise attack with nuclear weapons could throw any nation off balance, as well as seriously damage its war potential. However, I am confident that our research is developing and will produce adequate defensive weapons which, together with the threat of devastating counter-attack, will prevent a potential aggressor from deciding to risk another total war. Our objective, therefore, must be intensified research and a well-balanced defense, which within the concept of collective security will deter war and provide the strength necessary to fight back if war should ever be thrust upon us. We are placing this establishment on a level of expenditures which we hope can be maintained over an extended period of uneasy peace without undermining our economy or our fundamental institutions. We propose to defend a way of life as well as lives and property.

Substantial reductions in total national security expenditures have been possible during the past two years. However, the approach has been selective. Expenditures in some programs in this category, as you doubtless know, will be reduced this year, but others will be increased. Total expenditures by the Atomic Energy Commission are higher than in any previous year. We expect to spend more on our own air power and related programs this year than in any year in peacetime history. We will spend more on continental defense and on guided missiles than in any year in our history. Research and development activities in the Department of Defense will continue at a level which utilizes the services of about half the research scientists and engineers in America.

That we have been able to grow in strength, while still reducing total defense expenditures, over the past two and a half years has

resulted from a number of factors. We have, for example, set aside the former concept of the "fixed date of maximum danger," which was moved forward from time to time, under which planning was designed to achieve maximum readiness for each such date. This was not only an extremely costly process, but made it impossible for the services to plan realistically on a stable long-term basis. Expenditure reductions have also been made possible by the introduction of new weapons and techniques in our military planning, which enables us to make maximum use of science and technology and minimum use of numbers of men. Other reductions in military expenditures reflect the growing strength of our allies, the termination of active hostilities in Korea, and the increased emphasis on our reserve forces.

As I have already pointed out, more businesslike procedures have also played an important part. Substantial reductions have resulted from more orderly and better-balanced procurement, from improved organization and management, from curtailment of unnecessary personnel movements, and from the elimination of duplication--or the reduction, at least, of duplication--overstaffing, and activities of marginal value. Other avenues will continue to be explored, for many more savings can be achieved without jeopardy to our security.

We must remember that during the last five years the United States has expended over 200 billion dollars on major national security programs. These expenditures have made possible substantial improvement in our military effectiveness, and the accumulation of "hard goods" which has brought our stock of many of these items to the point where it is possible to taper off our procurement. Since such supplies are not now being consumed in combat, the bulk of the material now being produced is adding to our capacity to defend ourselves. Mobilization stocks of key military items have thus been built greater levels of preparedness than ever before in peacetime.

The truly massive effect of nuclear weapons on military requirements and planning is vividly illustrated by the fact that one airplane with a three-man crew can carry more destructive energy in a single mission than all the air forces of all the nations of the world carried during the whole of World War II.

Today's defense expenditures are thus bringing about a steadily growing military capability. The free nations are now collectively stronger than at any time in recent years. The land, sea, and air forces we are proposing to maintain during this period of uneasy peace

represent by far the largest and most powerful military establishment this country has ever maintained in peacetime.

I might say in this connection that recent statements in the papers to the effect that the Administration has initiated a new round of drastic reductions in military expenditures are entirely without foundation. The President's budget message last January estimated that this year's expenditures for the military functions of the Department of Defense would be 34 billion dollars. Our last official budget estimate--five weeks ago--was still 34 billion dollars, and it remains our goal. We shall, of course, continue to make every effort--as we have for two and a half years--to reduce expenditures by further efficiency and economy wherever these can be achieved without jeopardy to our national security.

Now, the third of the principal objectives to which I referred at the outset is to keep our economy strong and growing. We have been determined to avoid the nightmare of inflation, and to bring to an end the upward spiraling of prices and wages, and the steady depreciation of the dollar with which we have become familiar in recent years. We are convinced that establishment of a healthy economic climate for free competitive enterprise and the substitution of the judgment of the marketplace for controls represent the best way to encourage sustained economic growth and productivity.

This confidence has been justified by the events of the past three years. 1955 is a year of unprecedented prosperity, with the major economic indicators now running at their highest levels in history, in war or in peace. Americans are producing, earning, and spending more, and hold more jobs today, than ever before.

Furthermore, since the armistice in Korea we have made the adjustment from a wartime to a peacetime type of economy, and our present growing prosperity has solid foundations, free from the artificial stimulations of war or inflation.

After the summary that I have given, I hope that you will feel that we have been able to strike a reasonable balance between our three principal objectives that I mentioned earlier--(1) a wise fiscal and budgetary management, (2) a sound and effective program of national security, and (3) a strong and expanding national economy. We are looking forward to a time when world tensions will gradually lessen and it will be possible to channel a much greater proportion of our resources into projects of lasting public benefit.

As we continue to approach a position of reasonable protection against unprovoked attack, it will become increasingly possible for the United States to release more of its energies towards the further improvement of national living standards. As we are able to make further reduction in expenditures, we will be able to make further reduction in taxes; and that will release additional funds for selective spending by the taxpayers according to their desires rather than by the Government. This in turn should enable us to achieve an even better balance between our defensive capacity, our expanding economy, and the increased welfare of our citizens.

We have a little adjournment, I understand, before we have further discussion.

CAPTAIN GERWICK: Ready for questions, gentlemen.

QUESTION: Mr. Brundage, after the budget is balanced, what are your thoughts about reduction of the public debt? How fast should it be reduced, and should it be reduced at all?

MR. BRUNDAGE: I will have to speak from my own personal ideas rather than for the Administration. But I personally think that we should scale down our present debt slightly during good years, and expect it perhaps to go up a little in bad years. I don't think our economy can keep going quite at the pace that it has been going this year or since the war. I think it is going to level off, to drop a little. I would like to see the debt cut, if possible, to about 250 billion dollars over the next five years, with the idea that it might go up again after that. I don't think that we ought to cut it very rapidly, because I think that taxes ought to come down. I think that taxes are at a higher rate than we can count on our people being willing to continue to pay over a generation.

QUESTION: My question is concerned with the Hoover Commission report on budget accounting. What is the thinking in the task force on the Bureau of the Budget operation with respect to the Bureau concerning itself with budget accounting rather than involving itself with the policy of budgeting? Have we given proper heed to accounting in matters of that type? Could you briefly indicate what changes are to be expected in the Bureau's operations, particularly as affecting the Department of Defense, as a result of the Hoover Commission's report?

MR. BRUNDAGE: We are just studying that now. Ever since the Hoover Commission report came out I have been going over it and discussing it with the chairman of the Hoover Commission task force. It would involve quite a lot of changes if we were to adopt the whole of their recommendations. We have also discussed it with Joe Campbell of the General Accounting Office, because it would involve changes in his present operation.

I am inclined to think that we have to have an accounting officer for the Government as a whole. Whether he should be in the Bureau of the Budget I am not so sure. But I think we should have an Accountant General. The Comptroller General is more of an auditor general than he is controller in the ordinary commercial sense.

I think there should be an Accountant General in some way, who could have a staff and who would be able to coordinate accounting in all the different departments, including Defense. I think it would help. I think that the individual comptrollers and budget officers in the services and in the other departments should be responsible for their own accounting; but I think it would be helpful if there were an Accountant General to whom they could go for help, where they could go for advice as to improvements and changes--perhaps a greater use of machines, for electronic accounting, which I think is going to have to come in the next few years.

I think we have seen tremendous changes in accounting in the last ten years since the war, but I think we are going to see even greater changes in the methods of accounting and control over the next ten years. I can't say as to just how it will come about, because we are wrestling with it right now.

QUESTION: In our course in theoretical economics we learned that in a period of strong and expanding economy, with a large national debt, in theory we really ought to raise taxes instead of reducing them. I realize that the question of taxes has a great many political implications, but wouldn't it be sounder fiscal policy to at least keep the taxes where they are today without trying to reduce them?

MR. BRUNDAGE: Well, I don't think we are going to reduce taxes until we have a balanced budget. I think that is what the President has said in connection with the 1956 budget--that he isn't going to cut taxes unless we can see a balanced budget in sight.

The present Council of Economic Advisers, I think, is the soundest that we have had for a great many years. I think they are all extremely capable people. They have had wide experience in Government and in business. Their theory is, as I understand it, to try to keep the Government balanced on this narrow ledge between deflation on the one side and inflation on the other side. It is a difficult balance. I think they believe in leaving the free play of competitive enterprise as much as possible, with only a guiding hand. Of course we have seen the effect of the raise in the discount rate, which was part of their policy of trying to control the inflationary tendencies.

I think you are quite right--that if the economy had gotten out of control, the theoretical economists would have suggested an increase of taxes rather than cutting taxes; and I don't think that we will cut taxes if there is a serious inflationary danger next year. At least I wouldn't advocate it. I don't know what Congress may do, but I wouldn't advocate it. But I do think that they are working very hard, through the rediscount rate and by cutting Government expenditures, to avoid the inflationary effects of the wage increases, which were the biggest inflationary dangers in these last six months.

QUESTION: This is not intended as a loaded question, but it is directed at the 1.7 billion dollar fiscal deficit. In view of Congress' review of programs, and particularly in relation to Mr. Wilson's statement that he didn't see how we could reduce expenditures without weakening our defense, can you give us some idea of how you propose to reduce this deficiency?

MR. BRUNDAGE: I think the Budget Bureau has tried to avoid telling any department or agency how it could cut. I think we have suggested here and there minor possibilities. But I think, in the Department of Defense particularly, we have refrained from making any suggestions.

I have received a whole lot of suggestions from various members of the armed services. One that I received only yesterday was that, if the services would be willing to merge their hospital service, it would save a good deal in harrassment to the men and to the doctors. I understand that if each of the hospitals would receive and give service to members of each of the other services, there could be a considerable saving even in the Washington area. I don't know about it personally, but that is one suggestion I have received several times. I think that there are a tremendous number of savings that can be obtained

without reducing the forces and without reducing the programs--in procurement, in stock handling--those kinds of things.

I think that our Secretary of Defense has the will--I am not sure that any one person could conceivably have the way--to do it. I think it has to be a cooperative team effort. He has been working very strenuously on this problem of getting down to 34 billion dollars, I know. I know that it came out in a public statement that he didn't see how he could get it down below 34.5 billion dollars. I didn't refer to that in my remarks, because I am trying to keep away from that side of it.

QUESTION: The Hoover Commission report laid a good deal of emphasis on the advantages of an expenditure-type budget rather than the obligation-type budget. Some of us have difficulty understanding what real advantage there would be. Does the Budget Bureau see any particular advantage in the expenditure-type budget as against the obligation-type, and can you explain what that might be?

MR. BRUNDAGE: There is another part of the operation which I didn't refer to in my comments, and that is the authorization. You originally have to obtain congressional approval of your general objectives. That is called authorization. Then you have to go to the Appropriations Committee and obtain the approval of that committee and of the Congress before you can actually obtain new obligational authority, which is what I referred to as NOA. Then the next step is the actual obligation, as to making the contract or giving the order. Then the fourth step is the actual payment or expenditures.

Now, our expenditures in certain of the departments are on the ordinary commercial basis. That is, when the bill is received and the merchandise is checked, it is set up as a liability. Then the Treasury reports annually on the checks issued by the Government. That is the actual expenditure.

I think you would have to get into electronic accounting before you can do this, but I would like to see Government accounting improved and go on an actual accrual basis, as practically all businesses now do. But that wouldn't mean that you would have to set up a liability at the time the merchandise is received or the bill is delivered and title passes.

Now, part of the trouble with Congress, particularly the Appropriations Committee, is that they are very worried by this overhang

of obligational authority. There are still unspent authorizations of about 50 billion dollars that have been approved by the Congress. Part of that has been obligated and part has not been obligated and is still unobligated. Mr. Cannon, the present chairman of the Appropriations Committee of the House, and Mr. Taber, the minority leader, are both very much concerned with that, and they would like to wipe it out.

Now, if they wipe that out, the trouble is that we have to substitute something else, because when we come back for another airplane or aircraft carrier, you are not going to pay for that for a long time. It is going to extend over into another year. So if you don't have obligational authority, you are going to have to have something else. You are going to have to have some kind of authority.

If we ended the obligational authority, we would still have to have an authorization. I think that part of the difficulty arises from the hard-to-understand four phases of the operation. Actually our budget balance is on the expenditure basis and not on the obligation basis.

QUESTION: I would like to ask about this management and organization portion of your overall structure. It just struck me that it might get you into the inner workings of other people's business. Am I wrong?

MR. BRUNDAGE: I think we have to go into the inner workings of all the departments and agencies in order to understand their budget requirements. Our Management and Organization Office has been cut down too much, I think, out of budgetary limitations. I spoke of our staff being 420. When the present Administration came in two and a half years ago, the Bureau's staffing plan called for about 520 employees. We have reduced it about 20 percent. I personally think that we have lost considerably by so doing, in benefits which could be obtained by a little more study of the accounting of the different departments and suggesting some improvements.

About all that Management and Organization has been able to do in the last year has been to deal with proposals, management studies, that have come to us. I mean, where the Department has said: "We are not satisfied with the way this is operating." We have to look at these. We look at them and we say, "You need a management survey" or "We think it can be done this way or that." But we haven't been able to initiate the actual study ourselves of the different departments. We don't have the staff for it.

QUESTION: On this management phase, we have had much financial management imposed on us. Personally I just wonder how much attention is given to the conversion of this system, which has been imposed for peacetime operation, to wartime operation.

We have heard it said, facetiously maybe, but there is some feeling behind the statement, that if the next war is lost, we can take comfort in the fact that the best business methods were used. Now, I just wonder about that. These changes of procedures require changes in our procedures all up the line, and some of them aren't very adaptable to wartime operations. Could you comment on what thought is given to that aspect of the process by the Bureau of the Budget?

MR. BRUNDAGE: I am afraid that I can't from my own knowledge. I know that it is being considered. I think that most of the improvements that have been made would lead to more efficient operation in wartime as well as peace.

Several people who were in Korea told me they could have operated better if they had had less supplies. They told me that the supplies cluttered up the docks and receiving stations; and that actually, if they could have had a smaller supply operation, they could have conducted a more efficient war. I don't know, because I have never had experience in that field. But I think that it is something that has to receive very important attention. And if it isn't, I think perhaps more attention ought to be given to it. But it is something that I think the services themselves would have to arrange, because no one in the Budget Bureau would pretend to offer suggestions on that phase of the work. That would have to be done by the services.

QUESTION: We have heard quite a bit in the past two years about how much taxation the American people could stand. I believe that it has been mentioned that our budget expenditure is based on what we think the American people will stand in the way of taxation. You mentioned the figure of 20 percent, that right now our level of Government expenditure is approximately 20 percent of the gross national product. I am interested in how our tax level here compares with that of other countries that have recently emerged from the war, Great Britain for example, and how our national expenditures compare with their national expenditures, each to his own, that is, their expenditure as against our expenditure, and their level of taxation as against our level of taxation.

MR. BRUNDAGE: Well, our level has been higher. It has been 25 percent of the national income. It is just getting down. Expenditures are still around 20 percent--about 21 percent last year. But as we get above the 300 billion level, the percentage becomes less.

I think that the opinions of the economists vary. There is one economist who put 25 percent, or a quarter, as the top limit on taxation. But I think that the country that has had practically the highest level over an extended period of years without any serious decline is England. Many of the other countries that have tried a higher level lost their Governments and have been absorbed. But the English level has been high for a great many years, probably twenty or thirty years, since about 1914. It has been practically 40 years.

But I think you do see the effect of that on the resiliency of their economy. Their economy did not bounce back near as fast after World War II as ours did, or as the German economy did or the Belgian or the Dutch economy, I think that it has a very serious deadening effect on initiative and on investment, on the kinds of things that we value here so highly.

I don't think there is any exact line that can be drawn. But I think that we have been on the borderline. I think that the reduction of taxes last year was very beneficial. I don't think the effect would be too serious on our economy if we don't cut taxes next year, but I think it would be helpful. I think if we do cut them, it will encourage our economy, because people would rather spend their own money their own way than let the Government decide how they shall spend it.

CAPTAIN GERWICK: I am afraid our time is up. That was a splendid job of pinch hitting. On behalf of the Commandant and the rest of us, thank you very much.

(20 Dec 1956--100)B/ibc