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THEMES IN THE REAGAN BUDGET:

1982 AND BEYOND

The subject of tonight's meeting is the budget and the question of cutting the total versus changing the composition. Given the location, we might well be talking about the budget for the State of Maryland. Speaking for myself, however, I know very little about that subject and am constrained to speak about the Federal budget.

[All budgets]-no matter who prepares them or the level of government for which they are prepared-reflect two, very different elements. They represent [a financial plan and] they represent [a statement of political objectives and political philosophy.] [Usually those two elements are so intermingled, however, that it is impossible to determine which consideration gave rise to which budget decision.]

[The Reagan budget proposals are no different.] Notwithstanding our inability to say why a particular decision was made, however, I think it is possible to discern some underlying themes which appear consistently in the pattern of decisions and in the rhetoric surrounding those decisions. Many of these themes have already been discussed at length in the press. Others have not, or in my judgment have been misinterpreted in the public discussion.

Let's talk for a moment about a few of these themes. First, [the Administration is clearly saying that one of its dominant budget priorities is to change the trend line of

total Federal spending.) The Administration has said, and its budget proposals are consistent with that statement, that it wants to slow down dramatically the rate of growth in spending. If successful, these proposals would reduce that growth rate from about 13% annually to about 6%. If inflation is considered, this means a shift from real growth to real decline. [The Administration estimates that this will yield a balanced budget in 1984 at \$770 billion.]

[A second priority is to increase the level of spending for defense. There, too, we have consistency between rhetoric and action. The Administration's budget proposals project a rise in defense spending from \$136 billion in 1980 to \$256 billion in 1984.] This represents almost a doubling in four years and a real growth rate (after accounting for inflation) of about 9% per year.

[A third priority is to reduce Federal involvement in the domestic economy and to reduce the Federal role in dealing with domestic social problems. Again, we find consistency between rhetoric and action.] While non-defense spending will continue to rise in absolute terms, the rate of growth will be less than the rate of inflation. [In some categories, such as grants to States and localities, there will be substantial absolute declines.] Indeed, this priority would be the implied consequence of the first two, even if it were not a specific objective of this Administration. I would like to return to this point a little later.

[A fourth stated priority is to reduce waste and inefficiency in government. Here I think we encounter some divergence between rhetoric and action.] I would like to spend a few moments on this item because it is one on which there has been a great deal of public discussion. Unfortunately, much of that discussion has been (in my judgment) rather badly misinformed.

The problem starts, I believe, from the fact that we speak of fraud, waste, and abuse as if they were a single entity. The terms are used interchangeably and imprecisely. In fact, however, the terms are not interchangeable and have relatively precise meanings, if we care to use them. Fraud, for example, is a criminal act, punishable under the criminal statutes and implying criminal intent. Abuse, on the other hand, implies turning to one's own advantage loopholes in the rules governing a program. It usually involves activities which, while not illegal, were obviously not intended by the program. Waste, at least as we in GAO use the term, usually implies simple inefficiency. Waste is involved if a perfectly legal and proper activity is being carried out in a less than efficient fashion. When GAO talks about waste, we are not commenting on the objectives of a program, but rather the means used to carry it out.

Others use the term quite differently. A program may be called wasteful, even though it is efficiently managed, if one disagrees with its objectives or its underlying premises. I

do not find this use of the term "waste" very helpful in the debate over the budget because it means that every program-- and I doubt if there are any exceptions--is wasteful in someone's eyes. It is equally true that every program is absolutely essential to someone.

Leaving this debate aside, however, [it is interesting to examine what actions the Administration has taken to reduce fraud, abuse, and waste] (as GAO defines the term). [The rhetoric is encouraging; the actions are less so. In our experience, the most effective defenses against fraud, abuse, and waste are good program design, competent and motivated managers, strong internal controls and aggressive internal auditors.] This is as true in government as in the private sector.

We were a little startled, therefore, to see among ^{was} the new Administration's first acts [^] the firing of the entire corps of Inspectors General and reductions in the staffs of internal audit units. We have also heard reports of intentions to reduce staff working on agency accounting systems.) For obvious reasons, this does not strike us as a very productive way to go about the process of reducing fraud, abuse, and waste.

There are other examples of the Administration's actions not yet matching its rhetoric. [GAO recently put together a package of actions ranging from more aggressive collection of delinquent debts owed the government to replacement of obsolete computers, for consideration by the Congress.] We estimated that, if these actions (all related to waste in government)

were taken promptly, the 1982 budget deficit could be reduced by nearly \$5 billion without any reduction in services.

For reasons which have not yet been explained, [the Administration opposed every item in the package, without exception.]

I might add that [arbitrary ceilings on the number of Federal employees,] another early action by this Administration, are not a fruitful way to root out waste and inefficiency. Often it has exactly the opposite result, [leading to shortages of people with critical skills, imbalances of workload, bottlenecks in operations and contracting for services at higher costs. It can mean the elimination of precisely the people whose job it is to identify and eliminate fraud, abuse, and waste.]

Similarly, [arbitrary ceilings on salaries are not a particularly effective way to assure competence among managers in the Federal service.] At present, people at five levels of responsibility receive the same salary. Far from motivating good people to do well in hope of advancement, it motivates them, rather, to leave government. [We were disappointed] therefore, [to see the Administration withdraw what we had understood to be its support for lifting the salary ceiling.] There is already substantial evidence of the extent to which continuation of that [ceiling is driving good people out of managerial positions into the private sector.] We cannot long afford that loss of talent if we are really serious about wanting efficiency in the Federal workforce.

Incidentally, in light of all the current rhetoric about the hordes of Federal bureaucrats, you might be interested in a few numbers. In 1952, there were 2.6 million Federal employees; in 1980, there were 2.8 million, hardly an example of mushrooming growth. In 1952, there were 16.3 Federal employees for every 1,000 people in the Country; in 1980, there were 12.7. In 1952, we had 38,400 Federal employees for every billion dollars in the Federal budget; in 1980, we had less than 5,000.

Recognizing that one-third of the Federal workforce is in DOD, and another third is in the Postal Service and VA, I rather

doubt that you will see enormous cuts in these numbers. What you may well see, however, is a significant decline in the number of State and local employees, many of whose salaries are financed with Federal grants.

On the surface, at least, the actions taken by the Administration so far might reasonably lead one to the conclusion that the commitment to dealing with fraud, abuse, and waste is more rhetorical than real.

But it is much too early to reach that conclusion. These problems are simply not amenable to global attack. Rarely can a single sweeping action eliminate large areas of fraud, abuse, or inefficiency. Occasionally one finds an item of this sort, such as more aggressive collection of debts or more rational procurement practices. But usually the inefficiencies, the abuse, and the fraud are found by detailed examinations of individual activities. This is grubby, tedious, unromantic, and time consuming work. It rarely gets headlines and the progress comes in small doses.

There is some evidence that the Administration understands this, and is preparing for a more concerted, fruitful attack on the problems. The recently announced Task Force on Integrity and Efficiency is a step in that direction. We can only wait and see whether or not it will be pursued aggressively.

The goal of minimizing fraud, abuse, and waste is always a noble objective, of course, though one which is more often

honored in the breach than in the observance. In the current context, however, it takes on an added measure of importance.

For purposes of discussion, let us postulate that there is substantial public support for the Administration's first budget priority--reducing the rate of growth in Federal outlays. Let us also postulate that there is substantial support for strengthening the Nation's real defense capabilities, for which defense spending is an accepted (though far from perfect) surrogate. Let us also postulate, however, that support for the third priority--reduced Federal support for domestic programs and services--is much less firm.

All other things being equal, however, the third priority is the inescapable consequence of the first two, whether people support it or not. Mirrors and budget gimmicks aside, the budget is the sum of its parts. If the total is reduced and defense spending is increased, non-defense spending must decline. But all other things are not necessarily equal. Each dollar saved through the elimination of fraud, abuse, and waste is a dollar available for another purpose. And those dollars will become increasingly important as time goes on, for I believe we have seen only the first stage of the ratcheting down of the Federal budget. Incredible as it may seem, what we have seen so far is the easy part. [If the Administration is serious about

-- the Kemp-Roth tax cuts;

-- a balanced budget in 1984; and
-- continued growth in defense spending;
next year's budget fight will make this year seem tame.)

I am not privy to the Administration's budget strategy, but the Administration's own projections for FY 1984 make this situation quite clear. In that year, the Administration projects a budget in balance at \$770 billion, including \$256 billion for defense and \$68 billion for interest. They project \$392 billion for payments to individuals (primarily the safety net programs), \$44 billion for other grants to States and localities and \$55 billion for everything else. Unfortunately, that adds up to \$814 billion, not \$770 billion. To reach the target, they must find additional cuts of \$44 billion, over and above the \$45 billion or so in cuts proposed this year. (If you prefer to believe the CBO projections, or if you expect less than 100% success this year, the problem is even more severe.)

The numbers seem large enough on the surface to absorb such a cut. Technically, they are. But you should look a little more closely at the composition of those numbers before assuming it can be accomplished easily. The \$392 billion in payments for individuals is only about 23% above the current estimate for 1981, barely enough to cover inflation under the Administration's rather optimistic economic assumptions. The

\$44 billion in grants to States and localities is already down \$10 billion from the current estimate for 1981. You can always find a little bit by nickel and dime cuts in that elusive category, all other, the obvious targets in that category have already been attacked.

Given this situation, some may be tempted to say that you cannot get there from here. You can, of course, if you are prepared to pay the price. (At least you can get to \$770 billion in 1984. Whether or not the budget would be in balance at that point is another question.) What is the price we are talking about? Again, I have no special knowledge of the Administration's plans, but I would submit that you cannot make another \$44 billion in cuts without

1. Further substantial reductions in aid to State and local government; and
2. A significant reduction in benefits under the "safety net" programs.

The latter would almost certainly have to include a reduction in the extent to which benefits under these programs, particularly Social Security benefits, are indexed for inflation.

These, then, are the themes I see as likely for the 1983 and 1984 budgets:

- Continued restraint in the budget totals;
- Continued growth in defense spending;
- More intensive retrenchment in domestic social programs, in the form of reduced intergovernmental

assistance and reduced support for the safety net programs; and, perhaps,

- More vigorous efforts to eliminate inefficiency. Success in the attack on inefficiency can moderate the degree of real retrenchment needed in domestic social programs, but cannot (in my estimation) eliminate it entirely. >

My crystal ball is at least as cloudy as everyone else's. I have no idea how successful the Administration's budget strategy will be this year, to say nothing of next year. If I am correct in my estimate of the situation, however, the next couple of years should be very interesting ones for those of us who observe the budget process. Unlike some forecasters, however, I will even offer to come back at this time next year and tell you why I was wrong.