The Evolution of Federal Budget Rules and the Effects on Fiscal Policy

How Informal Norms Have Trumped Formal Constraints

Peter T. Calcagno and
Edward J. López

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Abstract

Today's fiscal policy challenges are rooted in the way that fiscal policy rules have evolved over the history of the United States. This paper demonstrates that two shifts of informal norms occurred in the decades surrounding the turn of the 20th century. First, public expectations shifted from requiring a balanced budget to instead using the federal budget to promote economic security at the household level and economic stability at the macro level. Simultaneously, norms for elected office shifted from temporary service to careerism, and the federal government became increasingly professionalized. Both shifts increased demand on the expenditure side of the federal budget while creating fiscal commons problems on taxation and appropriations. Through a series of legislative milestones, Congress codified both shifts into entitlement programs and macroeconomic objectives. The combined effect has been to exert relentless pressure to increase public expenditures through debt finance. Despite four decades of legislative attempts to constrain spending relative to taxes, the informal norms have trumped the formal constraints. Viewed through the lens of public choice economics, fiscal policy rules have evolved into a complex system of incentives that instill a strong bias toward systematically greater deficit spending, whether or not policymakers intend for that outcome to result. Furthermore, by creating intergenerational redistribution, the pattern of deficit spending is morally suspect. Reform discussions must recognize that today's fiscal policy challenges can be met only by addressing these deep changes in federal budget rules.

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Author Affiliation and Contact Information

Peter T. Calcagno
Professor of Economics and Director
Center for Public Choice & Market Process
College of Charleston
calcagnop@cofc.edu

Edward J. López
Professor of Economics
BB&T Distinguished Professor of Capitalism
Western Carolina University
edwardjlopez@gmail.com

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> The most elementary prediction from public choice theory is that in the absence of moral or constitutional constraints democracies will finance some share of current public consumption from debt issue rather than from taxation and that, in consequence, spending rates will be higher than would accrue under budget balance.
>
> —James M. Buchanan, "The Ethics of Debt Default," 1987

1. Introduction

This paper seeks to understand the mechanisms underlying the epigraph above, in particular by demonstrating how constraints on fiscal policy have been gradually relaxed, on net, over time. We build our case on an analytical framework in which the proximate causes of fiscal policy outcomes are the incentive structures facing relevant decision makers, and incentives are in turn a function of the formal and informal institutions that constitute the rules of the fiscal policy process. In short, the analysis here rests on the general claim that formal and informal rules ultimately determine outcomes and that prevailing norms in political society are a component of the informal rules. The pioneering work in this vein is Buchanan and Wagner (1977), which applies public choice reasoning to analyze how rules determine the incentive structure of fiscal policymakers. However, Buchanan and Wagner's book is almost entirely theoretical, and at nearly four decades old it cannot address today's fiscal policy circumstances. In this paper, we provide an empirical history of US fiscal policy that documents how the long-term evolution of federal budget rules renders today's fiscal policy challenges predictable. The underlying causes of today's challenges are not the result of which political party is in power or whether the economy is in crisis. Instead, chronic deficits and fiscal crises have deeper causes. This paper argues that two fundamental shifts that have gradually occurred in federal budget rules—one occurring among the polity, the other within government—have had a profound effect on the size and frequency of fiscal deficits. We first present a clear understanding of how budget rules evolved over the history of the nation, and we then relate this evolution of rules to the incentive structure facing today's fiscal policymakers and to the observed fiscal policy outcomes. By implication, reform discussions must recognize that policymakers can systematically improve fiscal outcomes only by addressing these deep shifts in federal budget rules.

In section 2 we document and describe today's fiscal policy challenges, including chronic deficits caused by overspending rather than insufficient taxation, mounting and unsustainable levels of public debt, and a fiscal process that has become increasingly complex and myopic to the point of dysfunction. As we will show, this heightened complexity is itself a predicted outcome of the shift of informal norms. Furthermore, under such complexity, fiscal policymakers and voter-taxpayers can be unaware of the systematic biases driving them toward fiscal unsustainability.

Section 3 documents the shifts of informal rules to which this paper draws attention. The decades surrounding the turn of the 20th century brought about two important shifts in the norms that shape the scale and scope of fiscal policy. Among the general public there was a shift away from expecting a balanced budget to expecting the federal budget to be used as a policy instrument. This shift created new demands on the federal budget to provide both economic security at the household level and stabilization and growth at the macro level. We describe this evolution of informal rules as a shift from a balanced-budget norm to a deficit-as-policy norm, which we carefully define. Also during the decades surrounding the turn of the 20th century, an important informal rule was shifting within the federal government. During this time, elected office transformed from a short-term activity into a career pursuit—a professional activity with intense competition among people representing parochial interests. The combination of professional politicians responding to the public's new fiscal demands would come to exert steady upward pressure on federal expenditures, to the point that the government's long-term obligations would surpass its ability to generate revenue. The evidence of this development would emerge later in the form of chronic deficits and unsustainable levels of debt.

Next, section 4 documents the evolution of the formal fiscal rules in response to the earlier shifts of informal rules. Since the early decades of the 20th century, the shift from a balanced-budget norm to a deficit-as-policy norm has been codified into the formal rules. Specifically, we discuss legislation that formalized the economic policy objectives of full employment, price stability, GDP growth, trade balance, budget balance (macromanagement), and, most importantly, economic security through entitlement programs, all while mandating use of the federal budget as a policy instrument in pursuit of those objectives. Additional legislative changes have sought to hone and modernize the fiscal policy process, including the methods of analysis brought to bear on it. Thus, the long-term evolution of fiscal policy rules has been an underlying shift of informal norms, followed by a series of organizational and legislative changes in the formal rules. Our theme in this paper is that the informal norms that promote greater spending have trumped formal attempts to constrain spending, thus generating the observable adverse fiscal outcomes.

Section 5 presents our set of explanations that tie those adverse outcomes to the shifts of informal and formal fiscal rules. The sum effect of this institutional evolution has been to create strong rewards for policymakers to approve greater spending, to finance that spending out of debt, and to increase the complexity of the budget process to obscure the political and economic costs of systematic deficit finance. As a byproduct, the fiscal policymaking process has become increasingly dysfunctional and myopic. These outcomes are not due to mistakes or having the wrong kind of people in office. They are instead the predictable outcomes of a process that combines the response of professional politicians to an incentive structure created by systematically increasing public demands for spending under a deficit-as-policy norm.

Finally, in section 6 we use the foregoing analysis as a basis for thinking about fiscal policy reform. Successful reforms must be fundamental in the sense of addressing the underlying fiscal policy rules, both formal and informal. The objective involves, most fundamentally, a shift of American political culture away from a federal government whose scope and scale encompass all the economic activity that results from the deficit-as-policy norm.

2. Today's Fiscal Challenges

US fiscal policy faces serious challenges. As figure 1 (page 54) shows, federal debt held by the public as a percentage of GDP has reached peacetime highs after increasing sharply beginning in 2008. Despite a move toward fiscal balance in 2013–2014, the fiscal outlook is not a healthy one, as figures 2A and 2B (page 55) show. Under conservative assumptions, the Congressional Budget Office (CBO) projects that annual deficits will shrink for two years but then increase annually to 150 percent of their current magnitude by 2023. CBO also projects that the federal debt held by the public will exceed $18 trillion within the same decade (2013–2023). The outlook is even worse under the more realistic assumptions shown by the alternative fiscal scenario projections.

Overspending is driving the fiscal problem more than inadequate taxation is. Figure 3A (page 56) shows government spending as a percentage of GDP for the 19th century and for the first third of the 20th century. Large and rapid increases occur during national emergencies, most notably wars. During World War I, federal government spending as a share of GDP reached its highest level at nearly 24 percent. In figure 3B (page 56), which presents federal spending from 1930 to 2013, spikes are similarly evident during national emergencies; however, from 1952 onward, federal spending settled into an average level of about 19 percent of GDP, well above its pre–World War II trend. In fact, federal spending has been greater during "normal" times in the post–World War II era than in its peaks during genuine national emergencies in the 19th century and early 20th century.

By contrast, figures 4A and 4B (page 57) show total direct revenue as a percentage of GDP for the periods 1792–1929 and 1930–2013, respectively. As with the spending side, there were spikes in federal revenue surrounding genuine national emergencies. There was a similar-level shift after World War II, when revenues averaged about 3 percent of GDP before the war and settled into about 16 percent of GDP since. Even though spending and taxes experienced permanent shifts after World War II, the increase in federal spending was of greater magnitude (3 to 18.5 percent compared with 3 to 16 percent). Since the Great Recession, fiscal imbalance has been due to a combination of falling revenues and rising spending, but the overall post–World War II pattern of fiscal imbalance, during both normal and emergency times, is more attributable to spending increases than to revenue shortfalls.

In addition to chronic deficits and unsustainable debt, the fiscal policymaking process has become more complex and myopic since the brief period of surplus late in the Clinton administration. As Rubin (2007) explains, after 1998 the federal budget became less predictable and more fragmented, and policymakers became less accountable and more partisan, with commonplace use of earmarks and pork barrel, even for national security (Rubin 2007) and even during the spending cuts of the fiscal cliff (Yandle 2013). As deficits spiked again in the first few years after 2000, fiscal policymakers increasingly began to rely on emergency and supplemental bills, which evaded spending limits and the formal budget process. On the tax side, policymakers increasingly used temporary tax provisions that raised uncertainty in the marketplace and compromised economic growth. In general, in recent years, the process has given way to a climate of multiple crisis episodes and general dysfunction. For example, the president and Congress failed to enact a formal budget for six years from April 2009 to 2015 (Bendavid and Hitt 2009; Howell 2015). All the while, as record deficits ensued each year, increasing burdens accumulated on the liabilities of future taxpayers.

Even more troubling are the mandatory spending requirements for entitlement programs and the burden of debt service. Figure 5 (page 58) presents discretionary, mandatory, and net interest spending as percentages of the total federal budget from 1962 onward. Mandatory spending increased from 25 to 65 percent of the budget, whereas discretionary spending dropped from 68 percent in 1962 to 34 percent in 2014. The Office of Management and Budget (OMB) projects discretionary spending will drop to 24 percent by 2020, as net interest spending and mandatory spending increase. During the 1980s and 1990s, net interest occupied 10–15 percent of the budget. Net interest decreased to less than 7 percent in 2014 but is projected to exceed 11 percent by 2020, crowding out discretionary spending even if mandatory spending does not increase. The decreasing share in future budgets of discretionary spending poses serious problems for Congress to be able to respond to changing circumstances in the short term. The steady creep of mandatory spending also poses increasing obstacles to meaningful fiscal reform.

In brief, therefore, the US fiscal policy situation is characterized by chronic deficits and mounting debt, driven largely by increases in spending rather than decreases in taxes, especially increases in mandatory spending on entitlement programs. In the absence of meaningful entitlement reform, the outlook for these measures is projected to become even more challenging. Furthermore, as we document, the fiscal policymaking process has become increasingly complex. Through the course of this paper, it will become evident that these fiscal challenges are the predictable consequences of the long-term evolution of fiscal rules, especially the two shifts of informal rules to which we now turn.

3. The Evolution of Fiscal Policy Rules: Key Shifts in Norms

The evolution of fiscal policy rules in the United States has featured two gradual shifts of informal norms. First, the general public has shifted from expecting a balanced federal budget to expecting that the budget will be used as a policy instrument that provides household economic security and macroeconomic stability, even at the cost of deficit finance. We call this replacing the *balanced-budget norm* with a *deficit-as-policy norm*. Note that the deficit-as-policy norm is not a public preference for deficits—that is, it is not the inverse of the balanced-budget norm. Instead, the deficit-as-policy norm reflects new and steadily increasing demands for federal expenditures, even at the cost of fiscal unsustainability.[1] Second and consequent to the first, norms have shifted from viewing elected office as a temporary duty of public service to a career-long endeavor of personal ambition.

3.1. Shift of Norms, Part 1: From Balanced Budget to Deficit as Policy

From the time of this country's founding through the 19th century, voters and politicians predominantly shared the view that the federal government's budget ought to be in balance,

[1] Wagner (2012) refers to this change as one from sound finance, in which deficits occur during times of national emergency and surpluses are generated to pay down the debt during normal times, to one of functional finance, in which the condition of the budget is of no concern and spending occurs to maintain full employment.

much like a family's finances.[2] During times of genuine national emergency—defined as war or severe economic depression—it was viewed as acceptable for the federal government to increase spending through deficit finance. At the end of an emergency period, it was also expected that government spending would then be restrained, so that surpluses could be used to rapidly pay down the recently accumulated debt.

Figures 6A and 6B (page 59) show annual deficits and gross federal debt for the periods 1792–1857 and 1858–1914, respectively.[3] In these data, we can see how the balanced-budget norm was adhered to in fiscal policy decisions. In the 1790s, Revolutionary War debt levels remained elevated as military spending continued to increase, owing to conflicts along the American frontiers and the Barbary Coast. By 1801, Congress had restored surplus to the federal budget, and debt levels had begun to decline sharply, until the War of 1812 interrupted this trend. Deficit spending increased sharply in 1812 and 1813, and the federal debt reached $125 million. Following that war was a long period of fiscal discipline, as large deficits during the war were followed by large surpluses, and federal debt levels soon began to decline sharply. For 50 years starting in 1816, only two years of low deficits occurred, and by 1835 the federal debt had been entirely paid down.[4] The next genuine national emergency occurred in the wake of the 1837 financial panic, which ushered in a severe economic depression that lasted nearly a decade. A seven-year stretch of mostly large deficits led to an accumulated $33 million debt. However, surpluses again followed the emergency period, and debt levels began their sharp decline. The Mexican–American War (1846–1948) repeated the pattern, with the federal debt rising to $68

[2] For greater detail and background on fiscal discipline in the 19th century, see Buchanan and Wagner (1977), Hansen (1941), and Lane (2014).

[3] We have deliberately divided the data at 1857/58 to emphasize the vertical scale difference between the two periods. Had we presented the data in a single chart on the same vertical scale, none of the variation in the earlier periods would have been visually detectable.

[4] For a more recent accounting of the view of 19th century fiscal discipline, see Lane (2014). He argues that several political leaders and the public alike favored debt freedom.

million by 1851, followed by a sharp decline to $29 million by 1857. As figure 6B shows, the pattern of fiscal discipline continued from 1858 to 1914, albeit on a larger scale. In the first year of the Civil War, the federal deficit was $30 million, exceeding all previous years except 1845. By 1863 the deficit had increased 20-fold to $600 million, and by 1865 it was $963 million, leaving the federal government with a debt of $2.7 billion at the end of the Civil War. Yet what followed were 28 consecutive years of budget surplus and a near halving of the debt to $1.5 billion by 1894.

Overall, the pattern of fiscal policy in the 19th century exhibited adherence to a balanced-budget norm. Deficits were tolerated during times of genuine national emergency, but surpluses were expected in normal times to pay down the federal debt. Although the lingering effects of this balanced-budget norm could be detected in the early decades of the 20th century (e.g., when World War I debt was paid down from $27 billion to $16 billion by 1930), by the 1880s the balanced-budget norm had begun to crumble. By the time of the New Deal and World War II, the American polity had established a new fiscal norm, and deficits would shift from being the exception to being the rule.

During the decades surrounding the turn of the 20th century, there was increasing pressure by citizens and interest groups to spend federal dollars on safety net and economic insurance programs.[5] For instance, cash payments to Civil War veterans set a precedent that would exert significant pressure on the federal budget (by the end of the Hoover administration in 1932, veterans' benefits accounted for one-quarter of federal spending). The precedent would encourage other parochial interests to seek group transfers from the federal government (Holcombe 1999). As a parallel example, Congress passed a bill in 1887 that would have sent

[5] Higgs (1987, 113) argues that "all shared a willingness, often an eagerness, to expand the scope of effective government authority over economic decision-making."

$10,000 in disaster aid to drought-stricken citrus farmers in the West. President Cleveland vetoed the bill, explaining that he could find no authority in the US Constitution to use taxpayer money in that way (Higgs 1987, 83–84). Despite the veto, it is noteworthy that Congress agreed on the proposal, presumably in response to constituent and interest group demands, thus indicating ongoing shifts in the predominant views about the expected role of the federal budget. Throughout the latter decades of the 19th century, interest group competition intensified around the federal budget as agriculture, railroads, industry, and other groups vied for subsidies and regulations (Higgs 1987). Meanwhile, advocacy groups pushed for federal dollars to fund local aid, basic services, and an administrative state to manage a new structure of economic regulations. In short, the period saw a proliferation of ways to use the federal budget to finance labor and consumer regulations plus safety net and economic security programs in the form of transfer payments to well-defined groups. As we will discuss in section 4, this new spending would become codified in the form of entitlement programs beginning in the 1930s.

The decades surrounding the turn of the 20th century also saw increasing pressure to elevate macroeconomic management as a policy objective to be achieved through the federal budget. Although the idea of stimulus spending is often attributed to John Maynard Keynes and his 1936 book, *The General Theory of Employment, Interest, and Money*, stimulus arguments were, in fact, being widely proposed and debated as early as the Hoover administration. As the economics historian William J. Barber (1985) describes the Hoover years, there was much discussion of expansionary public spending, multiplier effects, and toleration of deficits:

> Hoover believed that human manipulation could triumph over any alleged "laws" of economics. As he stated his position in 1923: "We are constantly reminded by some of the economists and businessmen that the fluctuation of the business cycle is inevitable; that there is an ebb and flow in the demand for commodities and services that cannot

> from the nature of things be regulated. I have great doubts whether there is a real foundation for this view." (Barber 1985, 16)

Hoover thought that deficit spending could help the country out of the Great Depression (Powell 2003). He was channeling the work of pre-Keynesian scholars such as Hobson and Durbin (1933), who developed the theory of underconsumption. With a focus on optimal taxation, Mirrlees (1971) argues that the federal budget is a tool to maximize social welfare.

In summary, from 1776 to the early decades of the 20th century, norms gradually shifted away from, and eventually abandoned entirely, the expectation of a balanced budget. In its place emerged a different norm under which the general public expected the federal budget to be used as a policy instrument to promote the public interest, both by underwriting a stronger safety net for economic security and by promoting macroeconomic performance. Taken together, these two sets of expectations began to exert pressure for increased federal spending, not only during times of genuine national emergency but also during ordinary conditions.

3.2. Shift of Norms, Part 2: From Voluntary Rotation to Professional Politicians

In the decades surrounding the turn of the 20th century, norms were also shifting within the government itself. The elected class was transforming from a high-turnover group of political amateurs who served temporarily into a body of professional career politicians. The organizational structures of Congress, the political parties, and the executive branch were prompting more division of labor within the federal government. In addition, the rising value of holding elected or appointed office began to draw intense competition that favored individuals with comparative advantages in responding to the deficit-as-policy norm.

From the time of the country's founding through most of the 19th century, elected officials adhered to the norm of voluntary rotation. This circumstance partly reflected the belief that service in office should be short term. George Washington famously endorsed this belief by declining a third term as president of the United States—a norm that subsequent presidents upheld voluntarily until Franklin D. Roosevelt ran for a third and then fourth term in the 1940s. Similarly, members of Congress would typically serve two terms and not seek subsequent reelection. Abraham Lincoln entered the House of Representatives under this norm, when his predecessor adhered to voluntary rotation. One term later, Lincoln paid it forward, allowing another person to take his Illinois district seat (Miller 2011). Voluntary rotation also made good sense under that period's prevailing politics and election procedures. Because congressional districts overlap several counties and municipalities, officials from local governments used rotation as a means of giving each other a turn at representing the district in Congress (Kernell 1977; Miller 2011). Despite these reasons, rotation broke down in the late 19th century as the party-line ballot was replaced with the candidate ballot and, perhaps more importantly, as the career value of holding national office began to increase (Rusk 1970).

The rising value of holding congressional office was driven by several concurrent factors, starting with pay. In 1855, the per diem stipend system was replaced with annual salaries, which increased dramatically between 1855 and 1925, from $3,000 (approximately $78,000 in 2013 dollars) to $10,000 (about $131,000 in 2013 dollars) (Brudnick 2014, Taylor 2013). With greater pay also came increasing staff allotments, perquisites such as franking, and benefits from increased lobbying, as discussed previously. Finally, incumbents began increasing their advantages over challengers, in part because of convergence toward the two-party system (López 2003). As the value of holding office rose and politicians began abandoning the norm of voluntary rotation, there was a dramatic decline in congressional turnover. As figure 7 (page 60) shows, the proportion of new members in each Congress went from above 40 percent in the 19th century to less than 20 percent in the 20th century. Most pronounced was the stretch from 1883 to 1910, when turnover declined by an average of 2.1 percent every year.

As members of Congress became more experienced and tenured, the organizational structure of Congress became more professionalized. The number of committees and subcommittees flourished, accommodating and further creating the need for greater specialization within Congress (Polsby 1968). Internally, party leaders began adopting the seniority system for allocating valuable committee assignments. Congressional staffs began to grow in number and prestige. In addition, the perquisites of elected office began to reflect the demands of a professionalized position that had begun assuming greater responsibility over human affairs great and small. As discussed in section 4, these shifts were codified through several legislative changes to the organizational structure of Congress.

In sum, from about 1880 to 1930, the general public began to view the federal budget through the deficit-as-policy norm rather than the balanced-budget norm. Meanwhile, the value of holding a congressional seat was increasing, which gave an advantage to candidates who were politically ambitious over those who approached office as temporary amateurs, all of which led to the abandonment of voluntary rotation in favor of increasing careerism in Congress. As a prominent scholar of Congress has said: “From the Civil War through the 1920’s . . . there appears to have been near linear growth of congressional careerism” (Kernell 1977, 671). This period ushered in a professional political system that began to favor and select policymakers who could respond to interest group and public demands to use the federal budget for purposes of microeconomic security and macroeconomic stability, in emergency as well as normal times, and at the expense of federal deficits if necessary.

4. From Codifying Deficits to Constraining Overspending: Evolution of the Formal Rules

In the long-term aftermath of the two informal norm shifts discussed here, the evolution of fiscal policy rules continued, with numerous changes to the formal rules of fiscal policy.[6] In several aspects, new legislative changes went on to simply codify earlier changes in informal norms. In other respects, legislation introduced wholly new rules. The salient theme in the evolution of formal rules has been the struggle to balance the need for fiscal discipline against the fiscal demands of a professionalized government that is expected to use its budget to promote economic security and macroeconomic management.

Table 1 (page 61) presents the key legislative changes discussed in this section, listed chronologically with brief summaries. This section of the paper groups legislative changes into four main areas: (1) codifying the deficit-as-policy norm, (2) modernizing the fiscal policy process, (3) attempting to constrain overspending through formal institutions, and (4) arriving at complexity in budget analysis. We detail each of these categories in turn.

4.1. Codifying the Deficit-as-Policy Norm

The past century saw enactment of new legislation through which the federal government has taken on increasing responsibility for economic outcomes, both at the household and economy-wide levels. At the household level, the single change with the greatest long-term impact on the federal budget was the 1935 Social Security Act (SSA). At its enactment, the SSA provided old-age insurance, welfare assistance, and unemployment insurance in the event of economic downturns. However, the long-term fiscal effect of the SSA would be to centralize responsibility for public assistance and social insurance programs and to create a permanent demand for

[6] Hou and Smith (2010) explain how informal rules affect formal rules and outcomes at the state level regarding balanced-budget rules.

increased spending on entitlements. An important aspect of this development was to expand coverage for old age, welfare, and unemployment to a comprehensive range of social insurance and public assistance programs. Survivors, children, and disabled people were gradually made eligible, and programs were expanded to cover health care, supplemental income, housing, and food.[7] Further expansion continued with the creation of Medicaid in 1965, the Children's Health Insurance Program in 1997, and prescription drug coverage under the Medicare Modernization Act of 2003. Over time these programs evolved into today's system of entitlements, putting steady pressure on the federal government's annual budget.

At the macro level, the Federal Reserve Act of 1913 centralized responsibility for financial stability and the supply of liquidity during financial crises. The 1946 Employment Act set the objectives of stabilizing unemployment, output, and inflation. The 1978 Humphrey–Hawkins Act extended macrogoals.

The economics profession arguably played a key role in codifying the deficit-as-policy norm. With the experience of the Great Depression and World War II, the profession began to support greater expansion of the federal government's role, specifically the use of budget deficits as a policy tool for achieving macrostability and avoiding a repeat of the Great Depression.[8] It was during this era when John Maynard Keynes articulated the macroeconomic case for countercyclical fiscal policy, sparking a revolution of thought in the economics profession (Keynes 1936). As the ideas of experts and intellectuals shifted toward a deficit-as-policy mind-set, the discourse

[7] The early social insurance programs expanded to encompass more and more benefits and groups. In 1935, Social Security paid retirement benefits only to the primary worker in a married couple. In 1939, the law was changed to include survivor's benefits and benefits for a retiree's spouse and dependent children. Social Security added disability benefits in 1956. Medicare parts A and B were passed in 1965, providing health insurance coverage for individuals over the age of 65. President Nixon allowed individuals with long-term disabilities under the age of 65 to be covered in 1972. The 1990s saw two introductions: Medicare Part C, which provides supplemental private health insurance, and the Children's Health Insurance Program. The year 2003 brought Medicare Part D, which provides prescription drug benefits. See http://www.medicareresources.org/basic-medicare-information/brief-history-of-medicare for the history of Medicare.

[8] For analyses of the gradual shifting of ideas within the economics profession, see Hansen (1941), Buchanan and Wagner (1977), Yergin and Stanislaw (1998), Boettke (2012), White (2012), Burgin (2012), and Leighton and López (2013).

surrounding fiscal policymakers began to change. By midcentury the mainstream positions in academia, the news media, and the intelligentsia had become predominantly Keynesian. Ultimately, this shift in ideas began to manifest in the formal rules of the game.[9] By the end of World War II, the Employment Act of 1946 codified, for the first time, the federal government's responsibility for stabilizing unemployment, output, and inflation. The act also gave economists a formal role in making economic policy by founding the President's Council of Economic Advisors and Congress's Joint Economic Committee. Furthermore, the act initiated the annual *Economic Report of the President*, through which economic policy advisors would forecast employment and other macroconditions, use these diagnostics to set goals for the macroeconomy, and then recommend fiscal and monetary policy actions for achieving those goals.

While the postwar economy was generally prosperous for two decades, the late 1960s began an extended period of high unemployment, combined with high and volatile inflation, plus chronic budget deficits and mounting debt. Amid the economic malaise of the 1970s, Congress and the president enacted the 1978 Full Employment and Balanced Growth Act, also known as the Humphrey–Hawkins Full Employment Act. The act further extended the federal government's responsibility for macroeconomic management, requiring federal policy to pursue the goals of full employment, output growth, price stability, balance of international trade accounts, and balance of the federal budget.

With the SSA of 1935 laying the foundation for entitlements, plus the Federal Reserve Act of 1913, the Employment Act of 1946, and the Humphrey–Hawkins Act of 1978 formalizing the objectives for macroeconomic performance, the definition of the federal government's economic responsibilities was set, and the deficit-as-policy norm was codified into law. The

[9] For analyses of ideas shaping institutions, which in turn shape incentives, see Buchanan and Wagner (1977) and Leighton and López (2013).

balanced-budget norm, which had been adhered to from the time of the country's founding through most of the19th century, had been officially stamped out.

4.2. Modernizing the Structure of the Fiscal Policy Process

The evolution of the formal rules has included changes to organizational structure, both within and external to Congress, and changes to the budget process. These changes were intended to modernize Congress for the professionalized era, yet they also had the effect of shaping fiscal policymakers' incentives toward creating systematic deficits. Similar to the codifying legislation discussed previously, these changes have their roots in the events of the late 19th century.

First, the structure of the Appropriations Committee changed in ways that led to a diffusion of spending authority within Congress. Throughout most of the 19th century a single committee in each chamber made nearly all the spending decisions (Cogan 1994). Created in 1794, the House Ways and Means Committee originally had authority to initiate both taxing and spending bills.[10] In 1865, Congress separated these functions, vesting the newly created House Appropriations Committee with the authority to originate spending bills and leaving the power to originate tax law with the House Committee on Ways and Means.[11] With fairly strict rules on new spending proposals, the Appropriations Committee began to draw increasing jurisdictional competition from other committees seeking to secure authority for their own spending projects. In 1877, Congress gave the Commerce Committee jurisdiction over appropriations for rivers and harbors, thus completely sidestepping the Appropriations Committee. By the mid-1880s, the structure of the

[10] The Senate has a similar but shorter history. The Senate Finance Committee was first created in 1816, consolidating power from other committees. In 1867, two years after the House, the Senate introduced more diffusion by separating the Finance Committee and the Appropriations Committee. By 1922 the Appropriations Committee consisted of 10 subcommittees; as of 1971, there were 12 subcommittees. For more details, see Committee on Appropriations (2008).

[11] For the changing committee structure during this period, see Committee on Appropriations (2010), which offers historical details and a partial review of the scholarly literature on this history.

Appropriations Committee had been expanded to feature 12 subcommittees, each of which took control of spending in distinct policy areas. As a prominent historian of the Appropriations Committee described its structure during this period, "They are the lords with their fiefs and their duchys [*sic*] each with power over his own area of appropriations. . . . There's a power elite on this Committee. And these subcommittee chairmen are as powerful as other legislative chairmen" (Fenno 1966, 168). Under this diffusion of budget authority, Cogan (1994) reports that federal spending increased by 50 percent between 1886 and 1893. In the years following the First World War, the centralizing of the budgetary process was gaining prominence. In 1921, Congress passed the Budget and Accounting Act, which restored centralized spending authority to the Appropriations Committee and its newly gathered 13 subcommittees.[12] However, by the end of the 1920s, the committees again began to diffuse budget authority, both inside and outside the Appropriations Committee. Through the mid-1970s, the number of subcommittees varied between 10 and 15, as the diffusion of budget authority within Congress continued (Tollestrup 2013).

In addition, the diffusion of budget authority extended outside Congress. In 1932, Congress created the Reconstruction Finance Corporation, an entity vested with the authority to borrow directly from the US Treasury. Congress soon created several other entities, including the Tennessee Valley Authority, the Homeowners Loan Corporation, and the Rural Electrification Administration. These entities could avoid the appropriations process, instead introducing tax-financed trust funds, which enabled the tax-writing committees to use trust fund revenues in place of general fund revenues (Cogan 1994).

[12] Specifically, "the House reorganized its Appropriations Committee by establishing for the first time a set of subcommittees to consider appropriations bills based on the administrative organization of the executive branch" (Saturno and Tollestrup 2015, 1). In addition, the act created the Bureau of the Budget (now OMB) and called for an annual executive budget submission by the President. It also created the General Accounting Office, now called the Government Accountability Office.

Changes to the broader congressional structure also affected fiscal policymaker incentives. The 1946 Legislative Reorganization Act (LRA) consisted of 10 components that attempted to modernize the congressional committee structure while also formalizing the professionalization within Congress (Galloway 1951).[13] The LRA reshuffled the congressional committee structure, reducing the number of overall committees in both chambers and increasing the average number of seats on each committee. The new structure narrowed the jurisdictional scope of many committees, thus creating greater specialization of duties within Congress. The LRA indirectly encouraged the professionalization of Congress by increasing the size and pay of congressional staffs, increasing the pay and benefits for members themselves,[14] and requiring lobbying organizations to register and file quarterly financial statements. The last was an effort to create more transparency; however, revealing the identity of special interest groups and how much they were spending only further increased the value of holding a congressional seat. Meanwhile, the expanded committee structure established in the decades from the 1930s to 1970s, and the diffusion of budget authority within and beyond Congress, allowed members to spend on their pet projects, an attractive option for those competing as professional officeholders.

On the fiscal policy side, the LRA was supposed to strengthen the powers of Congress by establishing a legislative budget, standardizing the appropriations classifications, requiring greater analysis by the comptroller general, and providing regular studies on the permanent appropriations of both chambers. Galloway (1951, 62) claims that "many of the fiscal reforms embodied in the Act have been virtually ignored or failed to work." The dramatic growth in spending and deficits during the 1960s and early 1970s gave rise to a standoff between President

[13] For a detailed description of all 10 components of the LRA, see Galloway (1951).
[14] Members received a pay increase of $2,500, to a new level of $12,500 ($148,810 in 2013 dollars); a tax-exempt expense allowance of $2,500; and optional retirement benefits through the Civil Service Retirement Act.

Nixon and Congress over how to curtail spending, which led to the 1974 Congressional Budget and Impoundment Control Act (Hogan 1985), which was a further attempt to return greater power of the purse back to Congress.

Commonly known as the Congressional Budget Act (CBA), this act put the final touches on the modern-day federal budget process. Most of the LRA's expanded committee structure would remain, but a newly created Budget Committee in each house would supervise and facilitate the formal budget process. The CBA created the Congressional Budget Office (CBO), which gave Congress the ability to have its own annual budget analysis separate from the executive branch. The CBA tasked CBO with generating five-year projections of outlays, revenues, and surplus or deficit figures. CBO works under the assumption that existing levels of government activity will continue, absent express changes. These projections became the origins of modern baseline budgeting (Cogan 1994). In addition, the CBA changed the start of the fiscal year from July 1 to October 1. Thus, the CBA added layers of complexity and bureaucracy to the existing organizational structure and formal budget process (Cogan 1994, Kamlet and Mowrey 1985).[15] Within 10 years of the act's passage, Congress was failing to pass appropriations bills on time, leading to greater use of omnibus bills as stopgap measures (Hogan 1985).

The evolution of the formal rules that we have highlighted—both the codifying of the deficit-as-policy norm and the changes to the organizational structure of Congress and the budget process—had the effect of raising the political gains to policymakers of providing more durable and lasting expenditures to constituents and interest groups. Being able to deliver a one-time

[15] In addition to the LRA, Congress made several attempts to create a formal budget process before passing the CBA, including the Omnibus Appropriations Act of 1950, the President's Commission on Budget Concepts in 1967, statutory spending limits and reductions for 1967–72, and the Joint Study Committee on Budget Control in1972–1973 (Committee on the Budget 2006), all of which failed.

allocation of spending is one thing; however, a long-term or even permanent flow of spending each year is of much greater value to professional politicians fielding offers from organized interests. In particular, entitlement programs with built-in claims on the stream of future budgets became more politically feasible under the twin forces of a codified deficit-as-policy norm and a diffusion of budget authority. Persson and Tabellini (2000) argue that the diffusion of power in the congressional appropriations structure creates a dynamic commons wherein each subcommittee increases its spending but has no control over the aggregate. These effects can be seen in the shrinking portion of the overall budget that remains directly in the hands of the Appropriations Committee, combined with a growing share of automatic spending increases for entitlements. In 1974, spending outlays for appropriations controlled only 44 percent of the federal budget; by the early 1980s, the share was down to 40 percent. Meanwhile, seven other committees shared 55 percent of the budget (Cogan 2008). As discussed, figure 5 shows the changes in discretionary, mandatory, and net interest spending from 1962 to the present, including OMB's projections through 2020. In 1962, discretionary spending was just under 70 percent of the federal budget and mandatory spending just over 25 percent. OMB estimates that by 2019 these values will be reversed, with discretionary spending down to just under 25 percent and mandatory spending at approximately 65 percent. These values have been decreasing and increasing, respectively, over the past 50 years. As with chronic deficits and mounting debt, the inversion of discretionary and mandatory spending began in the late 1960s and became more pronounced in the 1980s. Consequently, proponents of fiscal discipline have been trying to reform and constrain an ever-smaller portion of the overall budget.

4.3. Constraining Overspending

The evolution of formal fiscal rules has included various legislative reforms explicitly intended to constrain spending. As noted, Congress largely ignored the fiscal components in the 1946 LRA. With the emergence of systematic deficits, the 1974 CBA was then the first comprehensive attempt to restrain federal spending. The CBA limited the borrowing authority of the commodity corporations established in the 1930s. In addition, it introduced restrictions on creating new entitlements but left the existing programs intact (Cogan 1994). The overall effect of the CBA on budgetary outcomes was modest to nonexistent, partly because of the vague language of the act, which created fiscal policy debates but not actual fiscal restraint (Kamlet and Mowrey 1985). This led to passage of the Omnibus Budget Reconciliation Act in 1981. The 1981 act had the explicit goal of reducing government spending; however, CBO and OMB had separate baseline projections, so the degree of spending reductions became dependent on which estimates Congress evaluated (Ellwood 1982). Thus, there is debate over whether the 1981 act actually cut spending (Hogan 1985).

In 1985, Congress passed a bill that increased the debt ceiling by over $2 billion, which included as an amendment the Balanced Budget and Emergency Deficit Control Act. Known as Gramm–Rudman–Hollings (GRH), the act attempted to create a balanced budget within five years by using deficit-decreasing targets, with the plan of passing a balanced budget by fiscal year 1991. Leloup, Graham, and Barwick (1987) argue that it was the rise of entitlement spending and the decline of discretionary spending (i.e., the pattern seen in figure 5) that led to the emergence of GRH. Congress had been increasingly presenting authorizations and appropriations in omnibus bills, threats of government shutdowns were becoming a common way to deal with gridlock, and basic control of the budget process was beginning to prove difficult for individual congresses to achieve. For example, fiscal policymakers began violating House and Senate rules by enacting increases in appropriations without formal authorization (Leloup, Graham, and Barwick 1987). By contrast, GRH's intention was to add discipline to the process and hold future congresses accountable for overspending. If Congress did not meet a given year's deficit goals, automatic spending cuts (sequestration) would occur, cutting half from domestic discretionary spending and half from defense discretionary programs.[16] However, entitlement programs and interest on the debt were exempt from the automatic cuts. In addition, the automatic budget cuts would not occur if the country entered a period of recession or in time of war (Lynch 2011).[17] Finally, GRH allowed for a cushion of $10 billion over the deficit reduction target (Leloup, Graham, and Barwick 1987). Lynch (2011) notes that exempting certain programs from sequestration created incentives to not even attempt budget reductions on those protected areas. In short, GRH had something of a loud bark, but its teeth were removed because of built-in loopholes combined with the difficulty of one congress to constrain overspending by subsequent congresses. Indeed, GRH was challenged on constitutional grounds. In *Bowsher v. Synar* (1986), the US Supreme Court ruled that GRH violated the separation of powers doctrine. In response, Congress passed the Balanced Budget and Emergency Deficit Control Reaffirmation Act of 1987 (known as GRH II). Yet in 1990 the Budget Enforcement Act (BEA) made further modifications that formally repealed GRH (Wagner 1992).

The BEA created two avenues to control spending: Pay-As-You-Go (PAYGO) and discretionary spending caps (Lynch 2011). The intention of PAYGO was to offset any increases

[16] U.S. Congress House, *Balanced Budget and Emergency Deficit Control Act of 1985*, title II of P.L. 99-177; 2 U.S.C. 902 (99 Stat. 1037), http://www.ssa.gov/OP_Home/comp2/F099-177.html.

[17] A recession is determined when the joint deficit and sequestration report of OMB and CBO projects two quarters of negative growth consecutively, or when the Commerce Department reports actual growth to be below 1 percent for two consecutive quarters (Lynch 2011).

in spending with spending cuts or tax increases, thus not adding to the deficit. OMB would assess the PAYGO scorecard on an annual basis to determine if it would have to trigger sequestration. The BEA allowed Congress to adjust the limits set on discretionary spending up to three times in a fiscal year.[18] As was the case in the previous bills, emergency spending was exempt. The Omnibus Budget Reconciliation Act of 1993 extended PAYGO and discretionary spending caps to apply through 1998. All the while, the steadily increasing fiscal pressure of entitlement programs remained untouched. In other words, at every turn the demands on the budget under a deficit-as-policy norm consistently thwarted efforts to constrain spending.

4.4. Arriving at Complexity in the Budget Process

In first codifying the deficit-as-policy norm, then modernizing the budget process through organizational changes, then enacting explicit attempts to constrain overspending, evolution of the formal fiscal rules has incrementally added layers of complexity to the fiscal policy process. Complexity in fiscal policy raises the difficulty for individual voters, taxpayers, and policymakers to grasp or control the policymaking process and to perceive the actual consequences of fiscal policy. Individuals can grasp, control, and perceive only pieces of the whole but not the process in its entirety. Hebert and Wagner (2013) argue that policymakers and the public often treat macrolevel polices as though there is a central agent making orderly decisions. But faced with complexity, it is more realistic instead to treat fiscal policy as a process of dispersed decision making among the various voters, taxpayers, and policymakers who each control a small piece of the whole and who each have their own political objectives (Hebert forthcoming). Focusing on

[18] The three adjustment periods were: "(1) in a sequestration preview report included in the President's annual budget submission; (2) in a sequestration update report, issued in August; and (3) in a final sequestration report, issued 15 days after the adjournment of Congress" (Lynch 2011, 9). Congress could make adjustments for the following reasons: accounting for changes in budget concepts and definitions, credit subsidies, inflation, emergency appropriations, and IRS tax compliance funding.

the tax side of government budgeting, Hebert and Wagner (2013, 16) argue that a process of multiple decision makers with conflicting objectives and limited information creates “a certain degree of incoherence” in the tax code. Similarly, the complexity of the expenditures side of fiscal policy makes it difficult for people to understand or control systematic deficits.

The evolution of the formal rules that we have highlighted fits this analysis. Starting with organizational changes to the Appropriations Committee structure, the creation of trust fund corporations with borrowing authority, continuing with passage of the CBA and its creation of chamber budget committees, and on through the whole list of subsequent budget reforms that followed, layers of organizational complexity were incrementally added, and multiple methods of analysis were made part of the formal process. Several authorities now examine and review the federal budget. The Employment Act of 1946 created the President’s Council of Economic Advisors, which provides economic forecasts and advice that influences the president’s budget. OMB reviews the budget and provides reports for the executive branch. Once in Congress, the Budget Committee is given agenda-setting power to shepherd the appropriations bills through both houses. CBO reviews the budget for the legislative branch. OMB and CBO work independently; thus, their methods and assumptions of analysis have historically differed. GRH gave the trigger authority for sequestration to the comptroller general upon review of OMB and CBO reports, but GRH II gave the authority to OMB and the executive branch. Only since 1987 have OMB and CBO used the same set of assumptions as a baseline. With the introduction of the PAYGO scorecard, OMB would use this report, along with the discretionary spending caps, to determine whether it should enact sequesters. The composition of discretionary spending caps and other constraints has also been changing and has involved various methods of analysis by various committees, agencies, and branches of government. The evolution of fiscal rules has morphed into a process that requires expertise to grasp and that carves vast space for opportunistic distortions.

Complexity of formal rules is itself an outcome of the shifts in informal rules that we have highlighted. Consider the example of baseline budgeting, which Schick (1982) argues was an outgrowth of partisan politics. Originally, the Senate Budget Committee wanted a neutral baseline that would allow a distinction between discretionary and "automatic" spending decisions. Each side of the aisle came to recognize its own advantages of this proposed new baseline method. Democrats on the Budget Committee realized they could "cut" the budget while actually increasing expenditures. Republicans on the committee, after years of arguing that this method had a built-in expansionary bias, began to favor the method by 1981 because it could be used to overstate cuts. To see how this works, first note that CBO's baseline budgeting assumes growth in discretionary spending by the annual rate of inflation, yet growth in mandatory spending is tied to inflation and the growth of caseloads (as with Social Security, Medicaid, and Medicare). Suppose that Social Security spending was $768 billion in 2012. The 2013 baseline would have increased this by 1 percent for the anticipated increase in caseloads and 2 percent for the expected inflation rate. Therefore, the 2013 baseline would have been $791 billion; this would have been the expected outlay for the 2013 budget assuming nothing else changes. If Congress instead allocated only $783 billion, this change in the baseline could be reported as a 2 percent increase in spending relative to 2012 levels, or as a 1 percent decrease based on the projected baseline of $791 billion. Again, both sides of the aisle could claim to have been acting in ways that benefited their constituents. Thus, Democrats and Republicans found common ground on this procedural issue because Democrats wanted the actual cuts to be lower than they appeared to be and Republicans could claim the cuts were deeper than in reality

(Schick 1982, 31–32). It was politically expedient, under the deficit-as-policy norm, to add these layers of complexity.

The heightened complexity has interacted with increasing party polarization to create myopia and dysfunction in recent decades. As Republicans and Democrats have diverged, particularly on fiscal policy (López and Ramírez 2008, Poole and Rosenthal 1991), policymakers have increasingly gamed the formal process, often through parliamentary and political tactics, such as closing the Washington Monument and manufacturing phony crises or emergencies. Recall that the GRH and subsequent attempts to reduce deficits exempt emergency spending. Thus, to avoid the scrutiny of the formal budget process, both Congress and the president benefit by introducing emergency or supplemental spending bills that are not subject to the budgetary restrictions of PAYGO or deficit spending caps. Congress missed every deadline set by GRH, in part because it left enforcement to the use of parliamentary procedures. GRH II and the ensuing series of budget reforms all had shortcomings, loopholes, and exemptions written into them (Leloup, Graham, and Barwick 1987).[19] Every reform exempted emergency and entitlement spending. Congress eliminated PAYGO procedures in December 2002, setting all PAYGO balances to zero and thereby avoiding sequesters after 2003 (Lynch 2011). In parallel, supplemental spending and emergency spending, which are both excluded from ordinary budgetary rules, began increasing, especially after 1998 (de Rugy and Kasic 2008). The tide receded somewhat in 2010, when Congress reinstated PAYGO and sequestration under 5- and 10-year scorecards to be prepared by OMB. Yet off-budget entitlements, such as Social Security and Medicare, as well as emergency spending, were once again exempt.

[19] Specifically, GRH II allowed the House and Senate to avoid the sequester if the majority leaders in both houses could produce a joint resolution within 10 days of the OMB sequester report, which would then go through an expedited procedure (Lynch 2011).

As a result, CBA, GRH, and subsequent attempts to control chronic deficits have all failed. Responding to the expectations of the deficit-as-policy norm and working within the structure of expanded budgetary authorities, congressional spending committees have found ways around virtually every new constraint and procedure designed to limit spending. In the 1970s, it was baseline scoring tactics; in the 1980s, it was omnibus bills; in the late 1990s, it became earmarks; more recently, it has been supplemental and emergency spending.[20] The complexity of the overall process has contributed to avoidance of the formal rules, thus legitimizing an environment of government shutdowns, partisan and interbranch standoffs, an effectively permanent crisis mode, and routine reliance on temporary tax and spending measures filled with political tactics instead of actual on-time passage of proper budgets. The shift from a balanced-budget norm to a deficit-as-policy norm, followed by the codification of those norms and attempts to constrain spending, has created a level of complexity that may not be obvious to taxpayers or even to members of Congress but nonetheless shapes the incentives for fiscal policymakers and thereby renders predictable the fiscally unsustainable outcomes of their decisions.

4.5. The Sum Effect

Given the penchant for subsequent congresses to undo the constraints attempted by previous ones, and as entitlement spending marched on, in time the fiscal reality began to feature chronic deficits and mounting debt. Figures 8A and 8B (page 62) show deficits and accumulated debt for the periods 1915–1973 and 1974–2014, respectively. As with figure 6, we purposefully divided

[20] It is worth noting that much of the emergency spending is not for genuine national emergencies, a fact betrayed by the many earmarks and pork barrel projects that have accompanied these measures in recent years. See de Rugy and Kasic (2008) and Yandle (2013) for examples of earmark spending included in supplemental spending bills. As de Rugy and Kasic (2008, 24) put it: "The political effect of the word 'emergency' is to increase public pressure for quick passage of the bill. In this charged atmosphere, effective oversight is even more important, yet the 'emergency' label actually weakens congressional oversight."

the data at 1973/74 to emphasize the vertical scale difference between the two periods and to permit the variation in the earlier period to be visually detectable. The 1915–1973 interval, in particular, reveals the transition from the balanced-budget norm to a deficit-as-policy norm. In the early years of this stretch, the federal budget resembled 19th-century patterns under the balanced-budget norm. The largest deficits surrounded national emergencies, namely World War I, World War II, and the Korean and Vietnam Wars. Following World War I, the pattern resembled that of the 19th century, as the federal budget showed surpluses anywhere from $450 million to $950 million each year from 1920 to 1930 and total debt decreased from $2.6 billion to $1.6 billion. Since 1930, however, there has been a change in the pattern. Deficit spending began in 1931 and continued in much larger magnitudes through World War II. After the war, however, there were only minor decreases in accumulated debt (beginning in 1948), and the budget began alternating between periods of deficit and surplus. From 1953 to 1973, there were only four years of surplus, despite the absence of war or severe recession during that 21-year stretch.[21] Recall that in the late 1940s and 1950s the federal government began exercising more macroeconomic management, pursuant to the 1946 Employment Act. In parallel, entitlement spending continued to expand as well. By 1973 the stage was set for chronic deficits and mounting debt to become the nation's new fiscal reality.

Moving to figure 8B, we see that deficits and debt have become the dominant pattern of the modern budget era—starting almost exactly with passage of the CBA in 1974. This modern period has featured a long span of peacetime activity with a relative absence of any genuine national emergency until 2001. Yet despite three decades of new legislation to constrain

[21] The business cycle dating committee of the National Bureau of Economic Research lists four recessions during the 1953–1973 years: 1953–1954, lasting 10 months with a 2.6 percent decline in real GDP; 1957–1958, lasting eight months with a 3.7 percent decline; 1960–1961, lasting 10 months with a 1.1 percent decline; and 1969–1970, lasting 11 months with a 0.2 percent decline.

spending and reform the budget process, every annual budget since 1974 has experienced a unified budget deficit, with the exception of 1998–2001. Total debt has increased in every year during the modern budget era, with a few exceptions of insubstantial decline. In sum, by the time Congress began to take serious steps to rein in the budget, these systematic tendencies toward deficit-financed overspending were already cemented into place.

5. Why the Deficit-as-Policy Norm Trumps Formal Spending Constraints

Suppose the federal government seeks to finance an additional dollar of spending. It can do so in one of three ways: raise current taxes by one dollar, borrow a dollar, or print a new dollar.[22] Under a balanced-budget norm (as in the 19th century), it would not be politically feasible for policymakers to use debt to finance the additional dollar of spending except during a period of genuine national emergency or war, and then only with the expectation of future surpluses to quickly pay down the debt. On the other hand, under a deficit-as-policy norm, it is politically acceptable (in fact, expected) for fiscal policymakers to utilize any of the three finance methods. Viewed through the lens of public choice economics, the connection between the evolution of fiscal rules and the adverse outcomes of overspending through debt finance becomes clear.

5.1. The Spending Side of the Fiscal Ledger

Under the deficit-as-policy norm, the federal budget becomes susceptible to being overused, much like a property commons. In standard property rights analysis, when little or no rights of exclusion are attached to a scarce resource, the resource is owned in common. The "tragedy of the commons" demonstrates how the lack of exclusion rights leads toward the resource being

[22] By framing the question as an *additional* dollar of spending, we omit the option of financing a proposal through spending offsets elsewhere in the budget.

overutilized and allocated inefficiently. The academic literature has produced arguments that the federal budget is vulnerable to becoming a fiscal commons. Velasco (2000) demonstrates theoretically that, when fiscal authority is fragmented, a fiscal commons emerges and the macroimplications are higher transfers, deficits, and debt than would emerge with a single source of decision making. Wagner (1992; 2012) argues that three groups compete for the budgetary commons. Each committee maximizes spending, but interest groups and worthy causes put continued pressure on funds from these committees, as do their respective government agencies. All three groups understand that, if they do not fight for their share of the funding, it will go to other committees, interest groups, or agencies. The result is that each committee allocates funds for its segment of the budget—for example, agriculture, defense, commerce—but when the several appropriations are aggregated, the sum is greater than anyone intended and more than the available revenues can afford. Thus, the federal government generates deficits as a matter of routine, regardless of whether emergency conditions are at hand.

The shift to a deficit-as-policy norm, its codification, and the overall complexity of the budget process that has evolved all contribute to a fiscal commons problem in Congress. As noted, Cogan (1994) argues that since the 1930s Congress has expanded the number of committees that have spending authority. Yet the power to exclude must be delegated alongside the diffusion of access rights—otherwise the resource extraction rate will soon exceed its natural replacement rate, and a commons problem will come about. When a single committee had the appropriations decision, budget authority was concentrated in Congress, essentially providing a stronger ability to exclude access to the additional dollar of federal spending. A relatively small number of legislators (those on the appropriations committees in their respective chambers) had effective property rights over the budget. But as more committees, finance corporations, and trust fund authorities emerged—each with a constituency—from the 1930s to 1970s, this served to expand budget authority within and even outside Congress. Each additional decision maker with budget authority and his or her constituency could now receive the benefits of allocating an additional dollar of federal spending while spreading the costs among taxpayers. None of the attempts to constrain spending discussed in section 4 effectively address this fundamental fiscal commons aspect of the budgetary process. The attempts set targets for better outcomes but with too little attention to the process that generated those outcomes.

Outside Congress, the federal budget has also become a fiscal commons among the general public. Some interest groups are highly effective at requesting funds for their cause. As explained in section 3, safety net programs for the elderly, children, and unemployed persons have evolved into permanent entitlements that now occupy two-thirds of federal spending and for which even a suggestion of budget cuts has become politically taboo. Defense spending has become similarly untouchable, as the sequester debate of 2013 showed, even though defense appropriations have doubled in the past decade (de Rugy and Friedman 2012). The financial sector urged Congress in 2008 to inject liquidity to avoid systemic risk and has continued to press for ongoing injections under the Federal Reserve's new monetary policies. Relief of economic hardship has motivated historic expansions of unemployment benefits, food assistance, and other safety net programs. Economics experts argue that increased deficit spending is needed to promote economic growth and that more spending carries minor tradeoffs because Treasury yields and debt service levels remain low.[23] In general, the deficit-as-policy norm has effectively granted federal budget access to any group with a good cause. Groups have the further incentive to tout their causes as critical and

[23] Krugman (2009) claims, "If we have a reasonably responsible government a decade from now, and the bond market believes that we have such a government, the debt burden will be well within the range that can be managed with only modest sacrifice."

as being in states of emergency. The cacophony of these pleas exacerbates the fiscal commons problem and promotes a general climate of urgency, if not crisis, surrounding the federal budget.

Certain groups in the general public do advocate for more fiscal restraint. Watchdog organizations represent taxpayer interests, some of which have their roots in the tax revolts of the 1930s (e.g., the National Taxpayers Union). A number of organizations advocate for future generations, arguing that it is unfair to impose the costs of current spending on tomorrow's taxpayers. These groups do have some representation in Congress, with a minority of policymakers working to varying degrees toward fiscal discipline. On balance, however, the groups that advocate for fiscal restraint have been no match for fiscal commons under the deficit-as-policy norm, both in Congress and among the general public.

5.2. The Finance Side of the Fiscal Ledger

Just as there is intense political competition to secure the benefits of an additional dollar of federal spending, there is intense competition to avoid the burden of financing additional expenditures. This competition can take the form of supporting tax rate cuts, for renewal of temporary targeted tax breaks, for raising taxes on competitors, and so on. These modes of political competition have the common trait of putting future taxpayers at a disadvantage, simply because at any point in time future taxpayers have no political representation in current fiscal decisions. This relative underrepresentation is a driving force behind the fiscal commons argument to systematically push spending upward. It also introduces a second bias toward financing current spending through future rather than current taxes—that is, a bias toward debt finance (as noted in the epigraph). Later, future taxpayers have the incentive to propagate debt-financed overspending once they can vote themselves into becoming recipients of current spending. This gives future taxpayers some degree of recourse, so long as the deficit-as-policy norm still prevails once they become current voters. If so, then once their day comes, they can choose to debt finance their round of then-current spending, including service of past debt. Therefore, the deficit-as-policy norm creates dynamic biases toward chronic deficits and greater debt accumulation in each period; it also encourages each generation of voter-taxpayers to continue the pattern of intergenerational redistribution, a pattern that is detectable in the modern budget era, as shown in figure 8.

5.3. Incentives of the Policymaker

The public choice analytical lens shows how the evolution of fiscal rules shapes policymaker incentives. In the era of professional politics, politicians have a career motivation to win reelection (or be elected to higher office); therefore, they have a professional interest in taking credit for the benefits of additional budget outlays. Because of the fiscal commons problem, this incentive creates a systematic tendency toward increased spending, both in good times and in bad. Buchanan and Wagner (1977) argue that elected officials willingly spend public funds on projects that will deliver obvious benefits to their constituents. The deficit-as-policy norm allows those elected officials to benefit from that spending by offering constituents public services without increasing their taxes. Furthermore, because future taxpayers are only weakly represented in any current time's fiscal policy decisions, this norm creates a systematic bias toward financing current spending out of debt instead of current taxes. These forces overpower the opposition when arguing for fiscal discipline, thus reducing the frequency, likelihood, and power of attempts to constrain overspending. Instead, policymakers have the professional incentive to engage in nominal fiscal discipline—passing powerfully named legislation with targets to balance the budget by certain dates in the not-too-distant future, only to preserve flexibility to continue the debt financing of overspending through loopholes and exemptions. This is the observed pattern in the evolution of formal rules documented in section 4.

Those unproductive policymaker incentives are reinforced by voter perceptions of fiscal discipline, known as fiscal illusion.[24] A complex tax and budget process makes it difficult for voters to imagine the benefits of deficit reduction. Policymakers have professional interests in further blurring the connection between a dollar of deficit spending today and its eventual tax price tomorrow. They do not want people to think about the tax price at all. An effective strategy for blurring this connection is to make the tax code and budget process more complex—so complex that ordinary people cannot fathom the way federal tax and budget processes work, much less how the two interact. Public choice economics allows us to see that professional politicians, operating under a deficit-as-policy norm, can benefit from the set of fiscal policy rules becoming more and more complex over time.

In summary, elected officials have an incentive to support current interest group and constituent demands for spending, as doing so will increase their chances of reelection. Similarly, current voters and interest groups have the incentive to support deficit-spending proposals, partly because the benefits are clear and present while the costs are opaque and distant and also because they can shift the costs to future taxpayers, who do not now have a seat at the table.

[24] Oates (1988) reviews the fiscal illusion literature. A recent survey and empirical treatment based on a fiscal sociology approach is that of Houdek and Koblovský (2015). Cowen (2011) argues that for holders of Treasury debt it is "time to face the fiscal illusion."

5.4. Perceptions of the Voter-Taxpayer

Suppose the benefits of real deficit reduction (as opposed to nominal signaling) consist of better long-term economic performance, a more sustainable fiscal policymaking process, and perhaps an overall improved political climate. These benefits can be real and significant, yet under a deficit-as-policy norm, there would still be little incentive for the electorate to demand a move toward deficit reduction. This is partly driven by how current voters perceive the tradeoffs associated with deficit reduction.

The academic literature has established this line of reasoning. For example, Buchanan and Wagner (1977, chapter 8) and Wagner (2012) portray today's voters as associating both costs and benefits with deficit reduction proposals. On the cost side, deficit reduction either means there are fewer current benefits of federal spending or greater burdens on current taxpayers. They perceive these costs as being direct and certain consequences of any deficit reduction proposal. These costs are also perceived as being incurred in the present time and by individual groups and special interests that either receive less spending or have more taxes imposed on them. Next, compare those perceived costs to the perceived benefits of deficit reduction. Again, even if those benefits are real and substantial, they will be perceived as accruing indirectly, at some time in the future, perhaps the distant future. Furthermore, it will be difficult to say that the future economy will have been performing better because of past fiscal discipline and not because of some other set of reasons. Finally, unlike the current costs of real fiscal discipline, which are borne by specific groups that receive less spending today, the benefits of fiscal discipline are going to be widely shared across the whole future population. It is difficult to enact any reforms with diffuse benefits and even more difficult when those reforms have concentrated costs.

When voters are presented with clear benefits of spending against vague, uncertain, and shared costs of fiscal restraint, there will always be a systematic bias toward greater spending. This voter perception problem is exacerbated by the complexity of fiscal policy. This problem reinforces the fiscal commons and intergenerational biases toward greater spending financed by debt to meet the demands of the deficit-as-policy norm.

6. Lessons for Reform

We argue throughout this paper that the current fiscal policy scenario faces serious challenges that are driven by the long-term evolution of fiscal policy rules. The shift from the old balanced-budget norm to the modern deficit-as-policy norm, coupled with the professionalization of elected office, has trumped four decades of legislative attempts to constrain federal spending. The overarching reform lesson is that systematic improvements to the fiscal health of the nation can be achieved only by addressing these deep shifts in institutional rules. We now direct that general point toward suggesting useful ways of thinking about fiscal policy reform.

6.1. The Need for Reform

The economics of the current fiscal path are unsustainable in the sense that the federal government's existing spending obligations exceed its long-term ability to raise tax revenue. Recall that figure 2A presents CBO debt projections using the 2013 baseline and an alternative fiscal scenario. The projections by CBO suggest that neither deficits nor debt will decline over the next decade. In both scenarios, deficits increase to between 150 and 200 percent of their current magnitude. Accumulated debt is projected to increase between $18 trillion and $22 trillion by 2023.

A number of estimates in the academic literature attempt to calculate the magnitude of all current and future spending promises.[25] Measuring all future spending promises plus all existing debt obligations yields a fiscal gap estimated to be approximately $211 trillion, which is about 16 times the $13 trillion of actual debt held by the public in 2014 (Kotlikoff 2013). The current tax system would have to increase tax rates across the board by an average of 57 percent just to meet these obligations (Kotlikoff, 2013). Insofar as that is unrealistic, systematic spending cuts are a mandatory part of serious reform proposals.

A moral dimension reinforces the economic case for fiscal reform. The shift of norms that we have identified in this paper—from the old balanced-budget norm to the modern era's deficit-as-policy norm—is a change in the moral constraints imposed by the general public on fiscal policymakers. The benefits of deficit spending accrue to people in the current generation.[26] The costs of deficit spending are borne not by today's bond holders but by tomorrow's taxpayers, who will service public debt at its maturity.[27] There is little gain to future taxpayers unless one argues that the economy they inherit will be a more prosperous one because of current deficit spending (which requires at minimum that current deficit spending be directed to sound, productive uses). As Buchanan and Wagner (1977, 12) surmise, "Put starkly, debt finance enables people living currently to enrich themselves at the expense of people living in the

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[25] Kotlikoff (2006) offers a brief introduction to fiscal gap accounting. For greater depth on generational accounting, see Auerbach, Gokhale, and Kotlikoff (1994).

[26] "The primary real burden of a public debt is borne by members of the current generation only insofar as they correctly anticipate their own or their heirs' roles as future taxpayers, and take action to discount future tax payments into reductions of present capital values. Insofar as the time horizons of individuals are not finite, that is, insofar as future individuals are considered to be separate conceptually from present individuals, there must be some shifting of the primary real burden to future generations" (Buchanan 1958, 36–37).

[27] "If an individual freely chooses to purchase a government bond, he is, presumably, moving to a preferred position on his utility surface by so doing. He has improved, not worsened, his lot by the transaction. . . . The economy, considered as the sum of the individual economic units within it, undergoes no *sacrifice* or *burden* when debt is created. . . . The fact that economic resources are given up when the public expenditure is made does not, in any way, demonstrate the existence of a *sacrifice* or *burden* on individual members of the social group. . . . It is not the bond purchaser who sacrifices any real economic resources anywhere in the process. He makes a presumably favorable exchange by shifting the time shape of his income stream" (Buchanan 1958, 28–32, emphasis in original).

future." In short, there is lack of reciprocity in the intergenerational deal that the deficit-as-policy norm has wrought. Furthermore, there is no mutual consent to this one-way deal. Since future taxpayers do not have a seat at today's political bargaining table, they are not able to resist political decisions that will impose financial burdens on them. Reciprocity and consent are two basic standards of fairness. By lacking both, the intergenerational deal created by the deficit-as-policy norm is morally suspect. After being awarded the 1986 Nobel Prize in economics, Buchanan (1987b, 527) summarized this problem as such:

> The financing of current public consumption by debt issue is unjust because it shifts income from those who are not and cannot be beneficiaries of the outlay and who do not and cannot participate in [the] complex political process that generates the observed results. "Taxation without representation" is literally descriptive of the plight of those who will face the debt-burden overhang in future periods.

The old balanced-budget norm effectively recognized this moral dimension to the problem, and policymakers were politically constrained from entering the morally suspect territory of intergenerational redistribution. However, as the deficit-as-policy norm gradually took hold, and as the policymaking class gradually became career professionals, the old moral constraint began to crumble and is now largely gone.[28] In short, the evolution of fiscal policy rules has brought federal fiscal policy to an unsustainable and unjust set of policy outcomes. Both of these realities call for meaningful reforms that restore America's fiscal policy to economic sustainability and intergenerational fairness.

[28] "The explosive increase in debt or deficit financing of public consumption outlays can be explained, at least in part, by an erosion of previously-existing moral constraints. The political decision makers did not 'discover' a new technology of debt financing midway through this [20th] century. Their rational self-interest has always dictated resort to nontax sources of public revenues. What happened in this century was that debt financing ceased to be immoral" Buchanan (1985, 1).

6.2. Thinking about Fiscal Reform: A Focus on Institutional Rules

Strong as the economic and ethical cases for meaningful fiscal reform might be, the political obstacles to reform are daunting. The deficit-as-policy norm and the professionalization of politics have become ingrained in American politics. Attempting to reverse them is at best a long shot. Even so, the public choice approach taken here points to effective ways of thinking about how to instead constrain the deficit-as-policy norm. In general, public choice emphasizes that underlying institutional rules define and shape the incentive structure of any decision-making environment and thereby determine subsequent outcomes. Thus, serious reform discussions must focus on the fundamental, underlying institutional rules of the fiscal game. Only then will the people with a seat at the table have the incentive to act systematically to promote fiscal discipline.

A widely studied idea is to implement some form of balanced-budget rule, which would require fiscal policymakers to restrict spending to amounts no greater than revenues. There are many variations on the essential idea. For example, would the budget need to be balanced in each fiscal year or over some other interval instead? Would the balance requirement be binding at the stage when budgets are initially proposed or at some later stage, such as when budgets are passed or actual revenues and outlays are realized? What would be the consequences of violating the balanced-budget rule? A voluminous literature has taken shape around the particulars of these questions and more. One strand of this literature argues that a limit on spending—perhaps as some percentage of GDP—would be better than a balanced-budget requirement, partly because the latter could simply give policymakers the political leeway to raise taxes rather than decrease spending. The essential question that this paper poses to supporters of a balanced-budget rule is this: Can the idea of a balanced-budget rule or a spending limit be implemented in a way that structures policymaker incentives to systematically avoid debt-financed overspending? Let's consider the prospects.

The balanced-budget and spending limit ideas are both hard constraints, and in this sense they are similar to the attempted legislative constraints discussed in section 4. As hard constraints, they do not alter the underlying reasons that policymakers have incentives to overspend. Instead, they operate analogously to price or quantity controls on markets. A price control on some good does not change the supply or demand conditions for that good; as a hard constraint, it only prohibits market participants from trading at certain prices. For this reason, market traders typically find ways to adjust to a price control, neutralizing its real effects over time. For example, rent controls may lead to reduced maintenance by landlords and minimum wages to greater use of capital instead of low-skilled labor. In an analogous way, fiscal policymakers can be predicted to find, create, and exploit loopholes in hard constraints like balanced-budget and maximum-spending requirements. If anything, our focus here on the informal norms suggests that hard constraints can be a useful part of the fiscal reform discussion, but they are not sufficient on their own to generate meaningful progress. Instead, we emphasize the need to address the underlying fiscal policy conditions—the supply of revenue available to fiscal policymakers and the demand for spending that is largely shaped by the deficit-as-policy norm.

Doing something about the fiscal commons problem is a good starting point. Within Congress, this translates into organizational changes that promote clear and enforceable exclusion rights to budget authority. Persson and Tabellini (2000) argue that centralization of the appropriations committee structure could reduce the problems of the fiscal commons. One example of this could be a concentrated veto or gatekeeping power within Congress, such as a strong appropriations chair or perhaps a deficiencies subcommittee, as was used in the 19th century and through most of the 20th century.[29] That subcommittee served a gatekeeping purpose, examining supplemental appropriations bills for programs that already had funding and alternatives for those without funding. Every time it has been eliminated, the responsibilities of this subcommittee have returned to the full committee, thus diffusing access to spending authority. Restoring the deficiencies subcommittee may help minimize the fiscal commons problem and its many symptoms that we discussed above. Outside Congress, reversing the fiscal commons problem requires a focus on changing public attitudes and expectations about the scope of government. This is a greater challenge that requires a more gradual approach, a point we will analyze further.

Entitlement spending, as figure 5 shows, is the area in which reform is most needed. In general, institutional rules need to make current policymakers more accountable for entitlement spending increases that create long-term fiscal imbalance. As one example, applying PAYGO offset requirements to the unified budget could create this kind of accountability because current policymakers would be required to decrease appropriations spending for every dollar of unfunded increase in entitlement spending. These constraints would make current policymakers more likely to devise permanent solutions to unfunded entitlement spending, which is where the real heavy lifting is needed to restore long-term fiscal balance. These constraints will not work, however, unless the public begins to change its expectation that spending on these programs, especially Social Security and health care, is an *entitlement*. Again, this is a huge challenge that requires gradual changes in attitudes, but the reality is that meaningful fiscal reform does not stand a chance without some shift away from the deficit-as-policy norm.

[29] Congress abolished and created the deficiencies subcommittee several times during the 20th century. It was first discontinued in 1950 in the Senate and in 1952 in the House. The subcommittee returned to the House from 1959 to1964 and to the Senate from 1962 to1970. Since 1970, there has been no deficiencies subcommittee in either chamber.

6.3. Prospects for Reform

The question that naturally arises is how likely the discussed sorts of reforms are to come about. Any significant reform can be defined as a supplanting of the status quo. In fiscal policy, reform efforts face a powerful status quo because the shift to the deficit-as-policy norm has led to an expansion of the power of Washington, coupled with a transfer of wealth to current recipients of spending. The expanded scale and scope of the US government has created a powerful incentive structure for politicians, interest groups, and voters to oppose spending cuts and therefore resist attempts to restore fiscal discipline. As detailed in section 4, attempts to control spending have come with built-in exemptions and loopholes, and the increasingly complex budget process actually works in politicians' favor by obfuscating the costs to the American economy of increased debt-financed spending. The status quo is a formidable one.

Several factors can each serve to weaken the status quo, though, and the confluence of these factors could create the political opportunity for implementing a new set of ideas. Milton Friedman famously articulated the first of these factors in the preface to the 1982 edition of his classic, *Capitalism and Freedom*:

> There is enormous inertia—a tyranny of the status quo—in private and especially governmental arrangements. Only a crisis—actual or perceived—produces real change. When that crisis occurs, the actions that are taken depend on the ideas that are lying around. That, I believe, is our basic function: to develop alternatives to existing policies, to keep them alive and available until the politically impossible becomes politically inevitable. (Friedman 1982, ix)

In the *perceived* sense, a crisis might be neither necessary nor sufficient for meaningful reform.[30] After all, the fiscal cliff drama ended in 2013 with a compromise bill that did not alter fiscal rules but did include conventional pork barrel spending. However, a *real* crisis could pressure

[30] See Leighton and López (2013, 8), who argue that major reforms often emerge slowly after repeated attempts but absent a crisis and that many crises come and go without leading to major reforms.

Congress into meaningful reform. For example, unless the projections in figure 2 are averted, there is rising potential for a sovereign debt crisis, or a near-crisis like that in Canada in the early 1990s (Henderson and Anderson 2011).

Turnover of politicians and ideologies is another factor that could create a favorable climate for reform. In the past, significant tax and spending reforms have followed changes in governing-party power—for instance, the Reagan tax cuts and the Clinton tax increases. Also, federal spending grows at slower rates under periods of divided government than under unified government (Calcagno and López 2012). Movements toward fiscal discipline can occur within party membership as well, over the long term (Poole and Rosenthal 1991) and even without turnover in response to short-term fluctuations of the business cycle (López and Ramírez 2008). Shifts in political control on their own are likely not sufficient to create the circumstances in which the powerful status quo can be defeated. However, regime change can be a contributing factor, especially when occurring alongside the emergence of a crisis and, perhaps most important, a shift in public attitudes regarding the appropriate scale and scope of government spending.

Toward that end, fiscal policy outcomes will improve only when the American political culture moves away from the deficit-as-policy norm. This amounts to a shift in the public's views about the proper scale and scope of government. The federal government has only a limited ability to successfully manage the complexities of a modern economy. The urge to "do something" in response to an economic emergency usually results in policy decisions that offer little benefit but carry large costs.

7. Conclusion

The main argument of this paper is that fiscal policy rules in the United States systematically encourage greater debt-financed spending, both in good times and in bad, whether policymakers realize it or intend for it to happen. The fundamental dynamic that we identify is the shift from a balanced-budget norm to a deficit-as-policy norm between 1880 and 1930, which was then codified during the middle of the 20th century into entitlement programs and the responsibility for macroeconomic management. In parallel and in response to the shift from a balanced-budget norm to a deficit-as-policy norm, the view of elected office as a temporary duty of public service shifted to that of a career-long endeavor of personal ambition, giving a competitive advantage to career politicians who know how to read and respond to professional incentives. Culminating in the 1974 Humphrey–Hawkins Act, this institutional dynamic ushered in the modern budget era, a period in which deficit-financed overspending firmly became the predominant pattern. Under the deficit-as-policy norm, fiscal institutions shape the incentive structures of career professionals in elected office such that they are politically punished for saying *no* to a cacophony of worthy sounding proposals, they have easy access to a cheap source of financing, and they are politically rewarded for making spending promises that are durable in the sense that they cannot easily be undone by future policymakers. Whether policymakers intend or realize it, chronic deficits have led to mounting debt, a dizzying complexity of tax and budget procedures, blurred lines between fiscal and monetary authorities, and unsustainably large unfunded obligations, all leading toward an overall bad and worsening fiscal outlook. In recent decades, attempts to constrain spending have been written into the formal rules, but in predictable fashion these formal constraints have not accounted for the circumnavigating forces of the deficit-as-policy norm. In short, informal norms have trumped formal constraints.

Reform discussions must start with the recognition that current fiscal challenges are rooted in these deep institutional changes. Effective reforms must focus on the institutional rules, both formal legislation and informal norms. Fiscal policy rules should be applied with permanence, to the unified budget, and without exemptions. Most importantly, changes in public attitudes are needed to move the American political culture toward a balanced-budget norm—recognizing that the abilities of the federal government are limited and so should be its spending authority.

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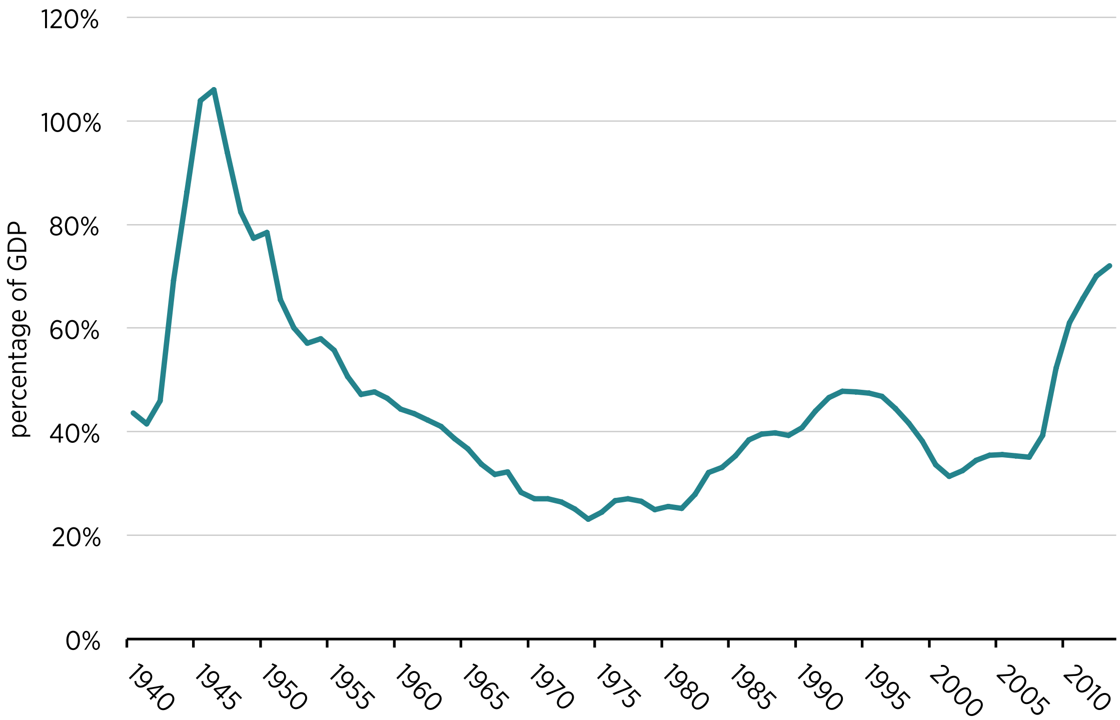
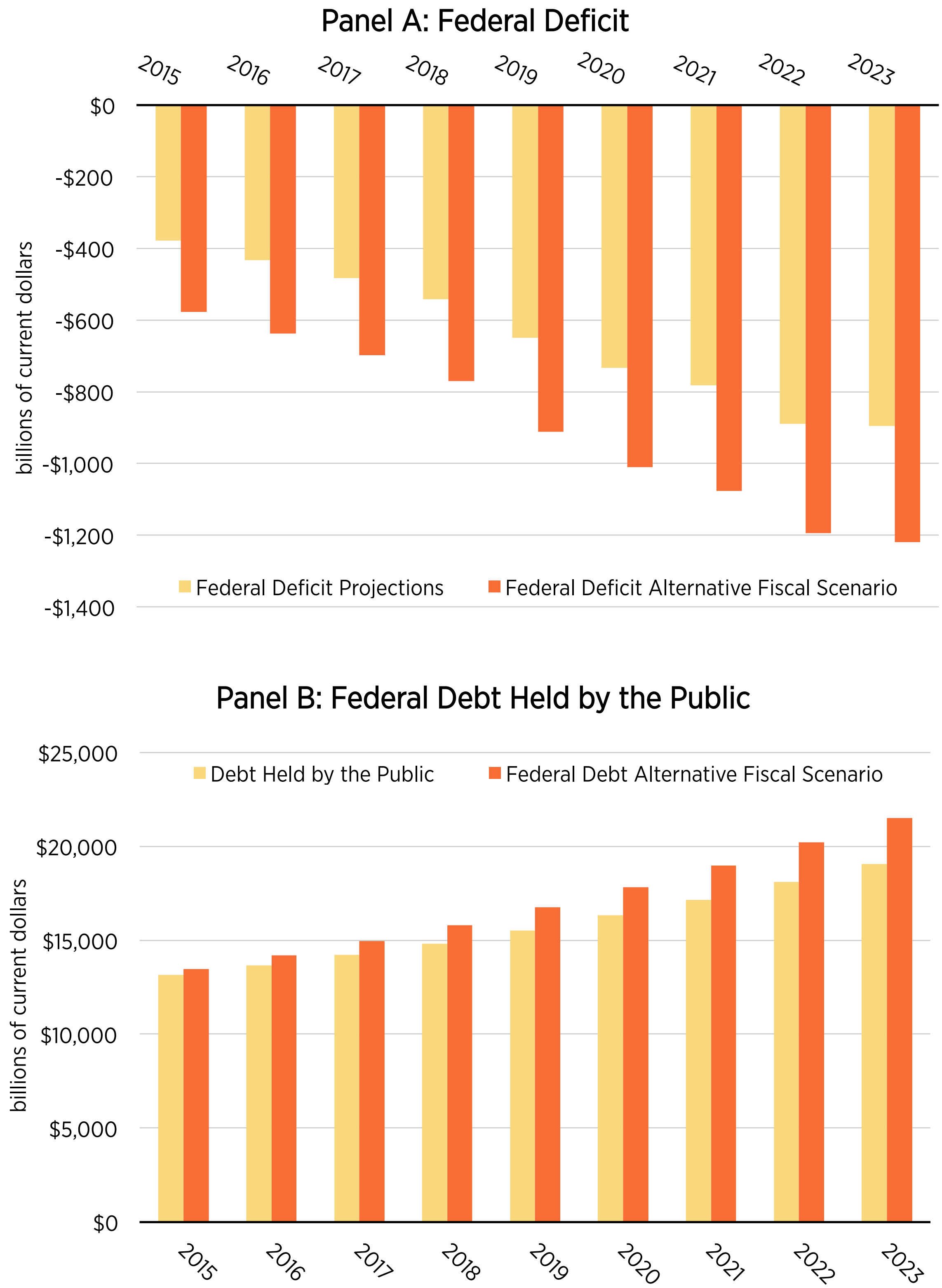
Figure 1. Federal Debt Held by Public, 1940–2013



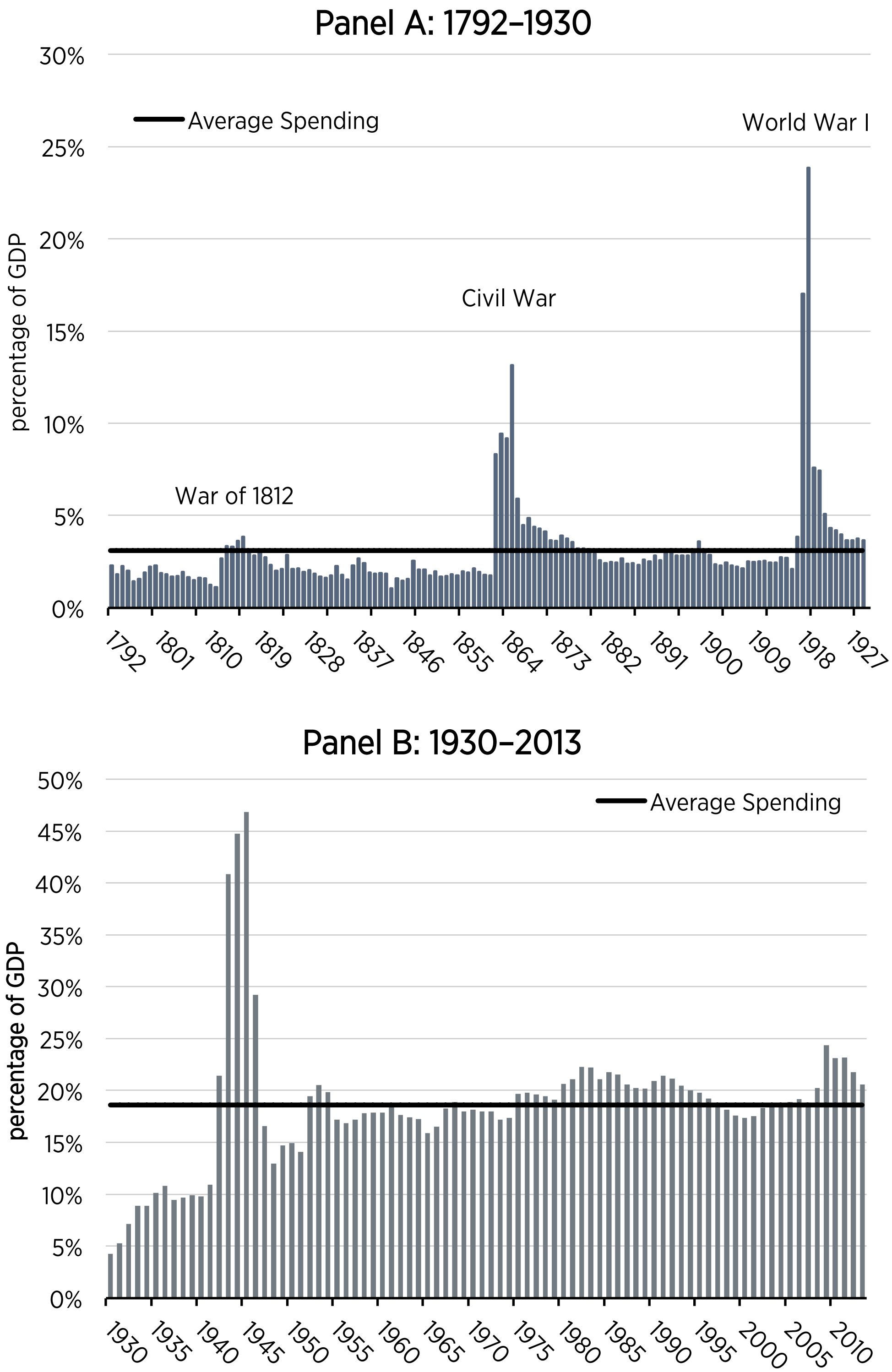
Source: Authors' calculations using data from Government Printing Office Historical Table 7.

Figure 2. Federal Deficit and Debt Held by the Public, 2015–2023



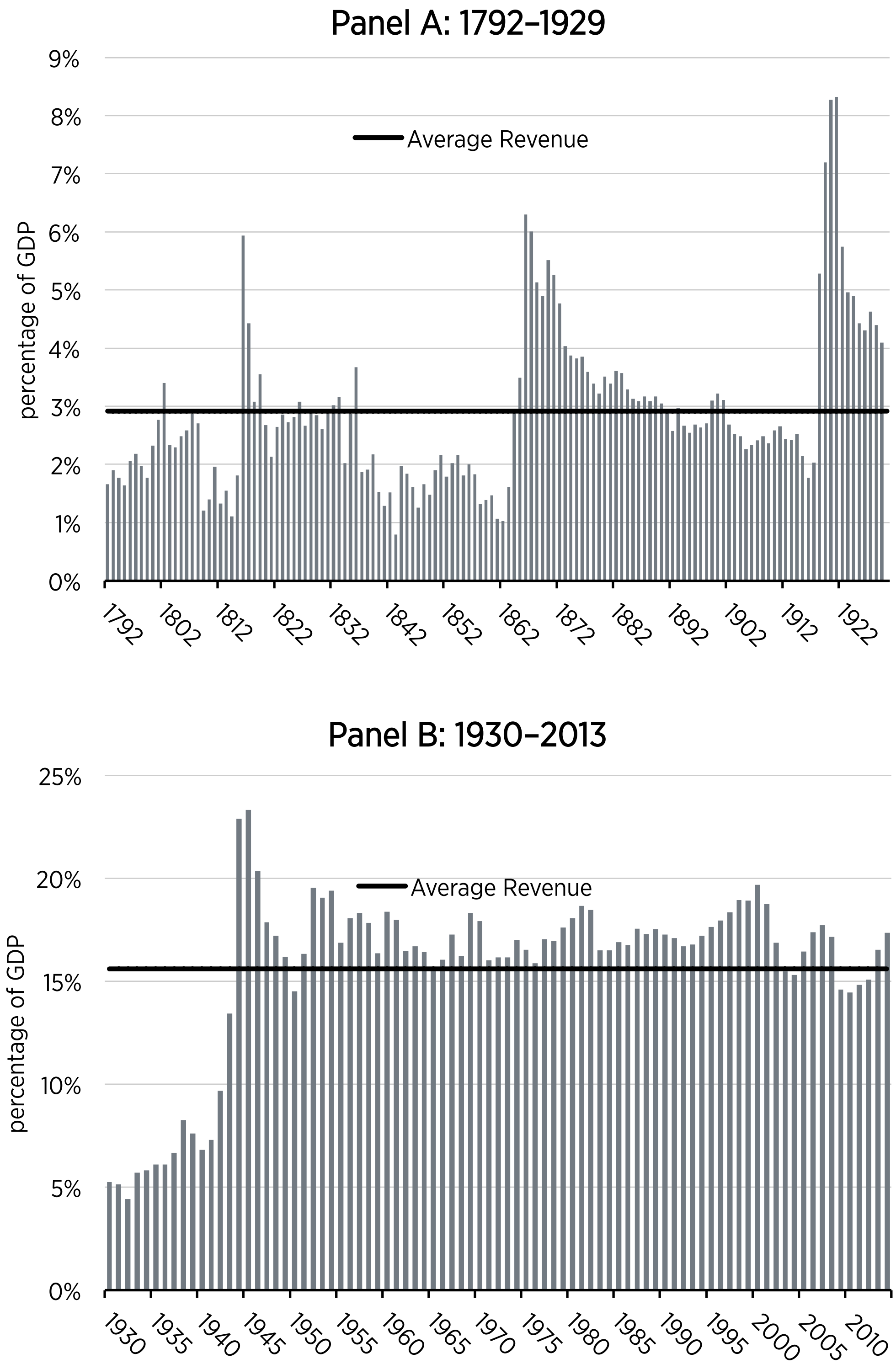
Source: Authors' charts using data from Congressional Budget Office, *Updated Budget Projections: Fiscal Years 2015 to 2023* (Washington, DC: US Government Printing Office, 2013).

Figure 3. Total US Federal Spending, 1792–2013



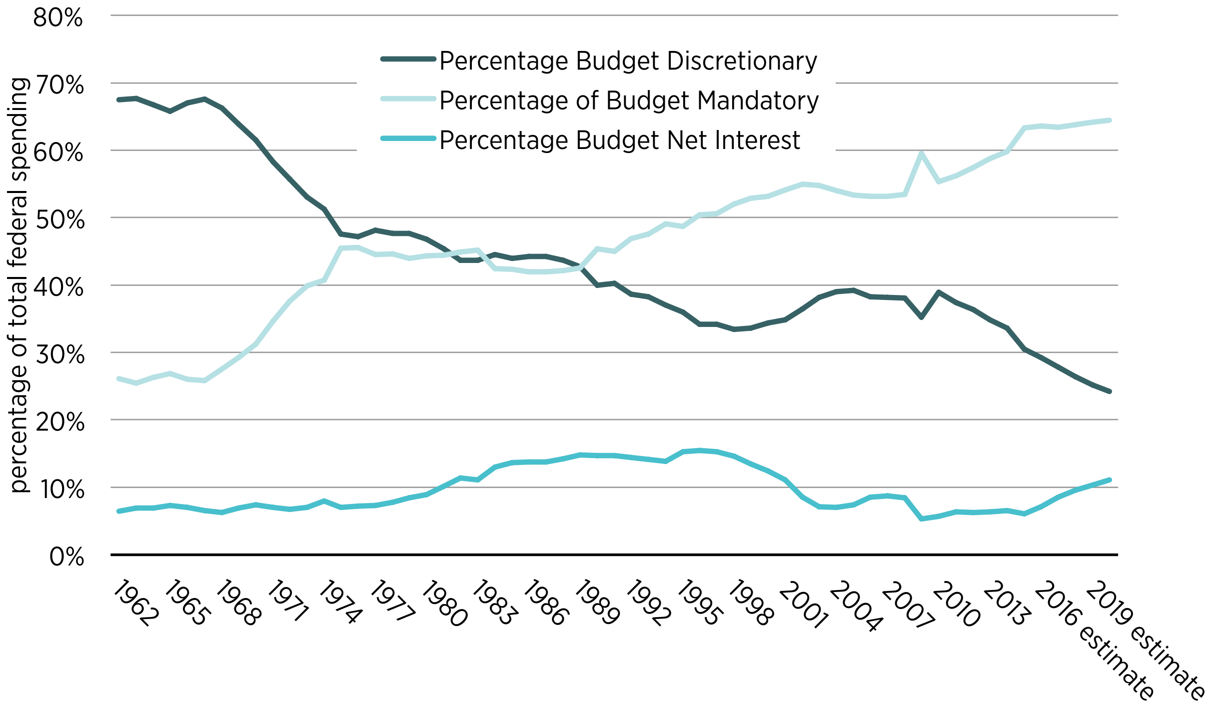
Source: Authors' calculations using data from *Historical Statistics of the United States, Colonial Times to 1970* and Bureau of Economic Analysis.

Figure 4. Total Federal Direct Revenue, 1792–2013



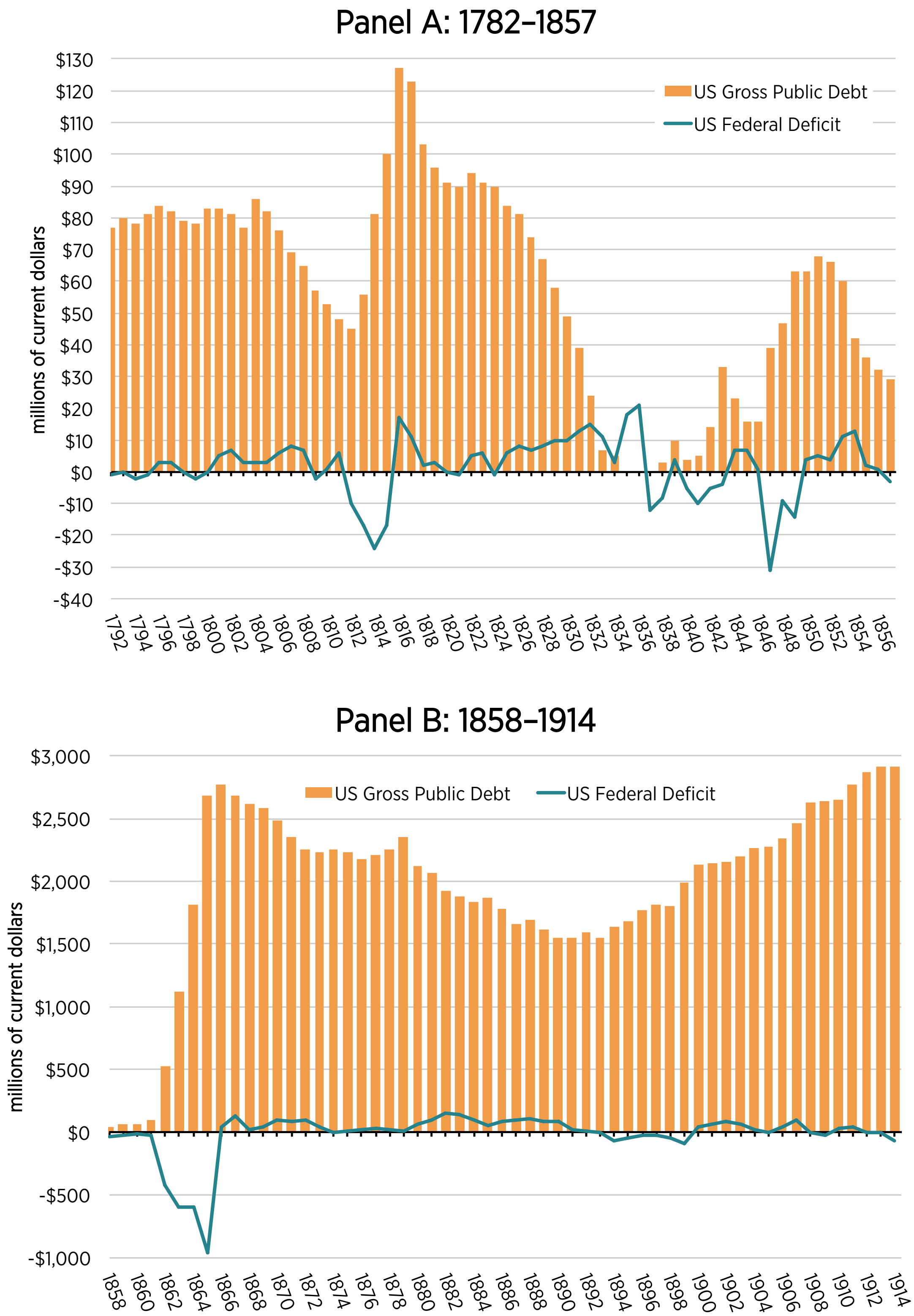
Source: Authors' calculations using *Historical Statistics of the United States, Colonial Times to 1970*.

Figure 5. Discretionary, Mandatory, and Net Interest Spending as a Percentage of Total Federal Spending, 1962–2019 Projection



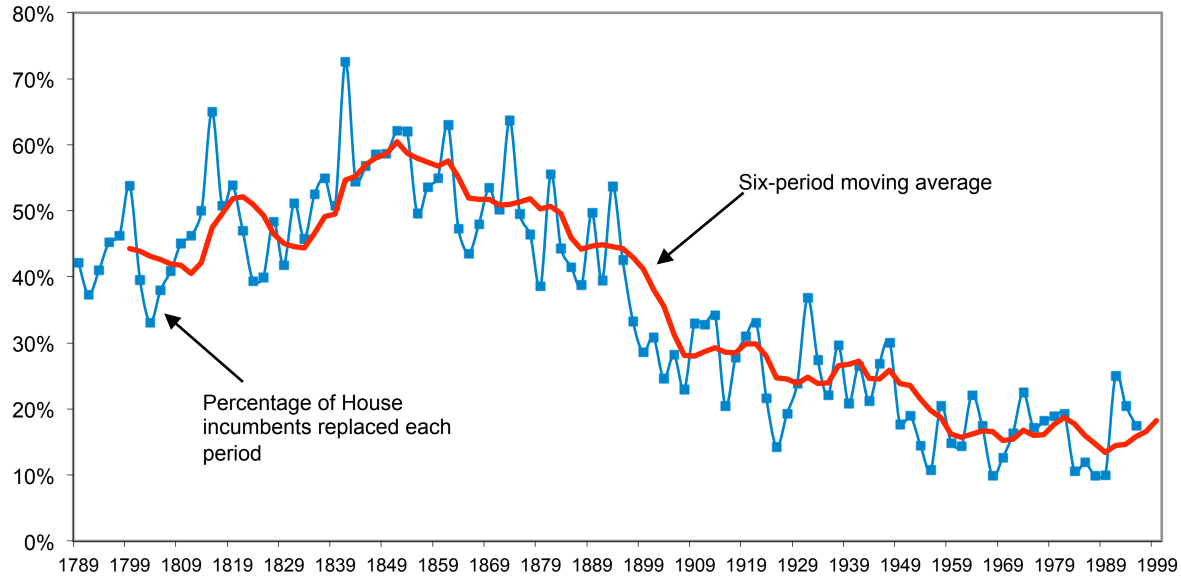
Source: Authors' calculations using data from Office of Management and Budget Historical Tables.

Figure 6. Federal Deficit and Debt, 1792–1914



Source: Authors' calculations using *Historical Statistics of the United States, Colonial Times to 1970*.

Figure 7. Turnover Rate of the US House of Representatives, 1st–104th Congresses

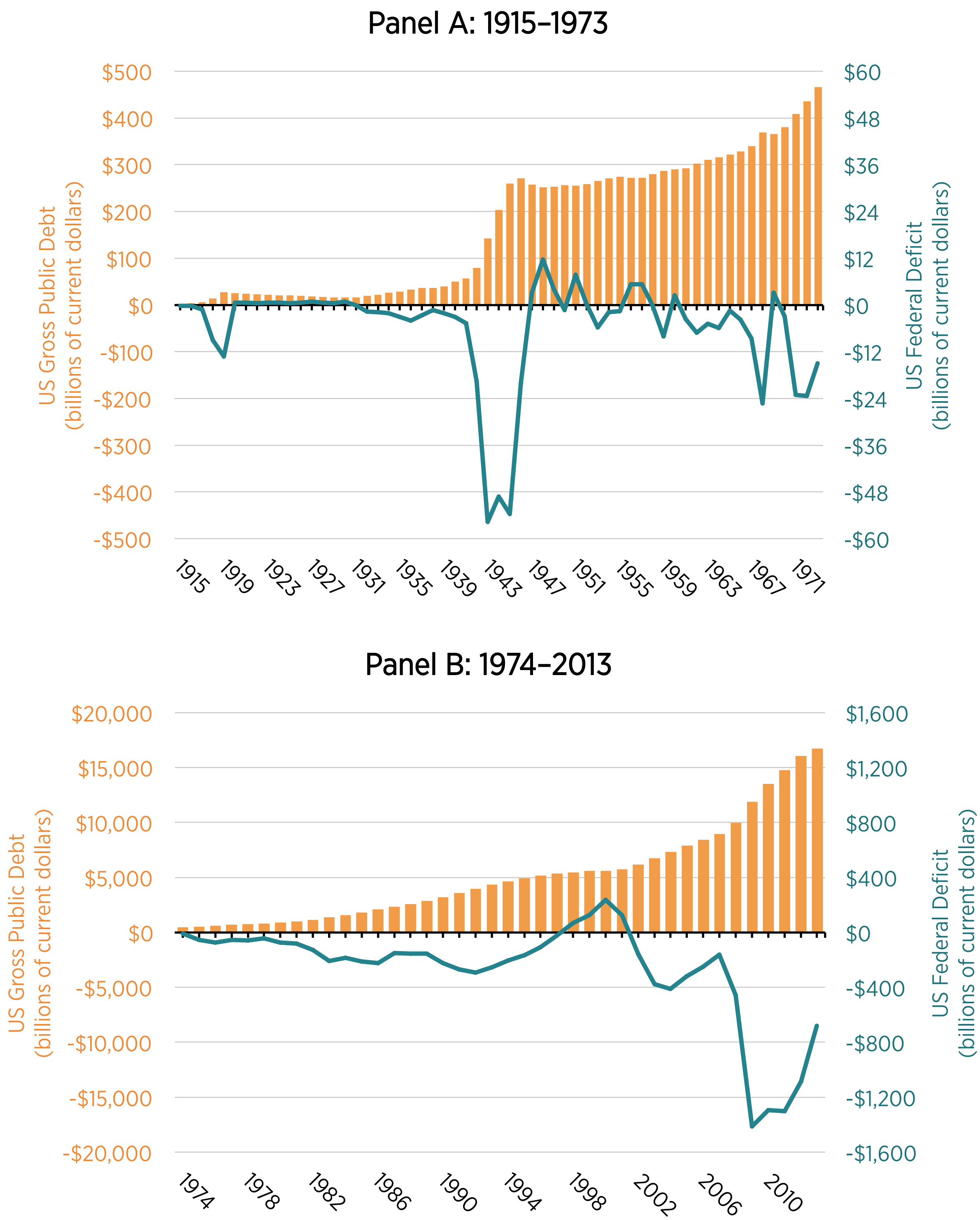


Source: Edward J. López, 2003, "Term Limits: Causes and Consequences," *Public Choice* 114 (1): 1–56.

Table 1. Major Legislative Changes to Formal Fiscal Policy Rules

Year	Act	Highlights
1913	Federal Reserve Act	Centralized responsibility for financial system stability and supply of liquidity during financial crises
1921	Budget and Accounting Act	Restored spending authority to Appropriations Committee, now centralized into chairs of 13 subcommittees
1935	Social Security Act	A significant and lasting step to legislate the federal government's responsibility for unemployment relief and social insurance programs that would become entitlements
1946	Legislative Reorganization Act	Changes to congressional organization, special relevance of changes affecting distribution of budget authority within Congress
1946	Employment Act	A key legislative change through which the federal government became officially responsible for using its budget to improve economic performance (e.g., to reduce unemployment)
1974	Congressional Budget and Impoundment Control Act	Altered the balance of budgetary power between Congress and the presidency; created standing budget committees in both the House and the Senate; originated modern budget reconciliation process; established the Congressional Budget Office; moved the beginning of the fiscal year from July 1 to October 1
1978	Full Employment and Balanced Growth Act (also known as Humphrey–Hawkins Full Employment Act)	Expanded the federal government's official responsibility for managing economic performance to include full employment, growth in production, price stability, balance of international trade accounts, and balance of the federal budget
1981	Omnibus Budget Reconciliation Act	Accompanied President Reagan's first budget; first major implementation of changes made to the 1974 act
1985	Balanced Budget and Emergency Deficit Control Act (also known as Gramm–Rudman–Hollings Act)	Created a series of deficit targets meant to constrain the spending decisions of future Congresses toward budget balance by 1991; otherwise, a series of across-the-board spending cuts (sequestration) would automatically ensue. Largely ignored by future Congresses until 2012, when it was the basis for sequestration
1987	Balanced Budget and Emergency Deficit Control Reaffirmation Act	Modified Gramm–Rudman–Hollings in response to *Bowsher v. Synar* in which the US Supreme Court ruled certain provisions of the 1984 act unconstitutional
1990	Budget Enforcement Act	Created caps for discretionary spending and created Pay-As-You-Go (PAYGO) rules for taxes and certain entitlement programs
1993	Omnibus Budget Reconciliation Act (better known as Deficit Reduction Act)	Accompanied President Clinton's first budget; proposed the highest peacetime increases in income tax rates in US history; cut appropriations spending; renewed the framework of the Budget Enforcement Act of 1990
1997	Balanced Budget Act	Extended earlier caps on discretionary spending; set goal to eliminate current-year deficits by 2002
2010	Statutory Pay-As-You-Go Act of 2010	Reintroduced PAYGO and sequestration

Figure 8. Federal Deficit and Debt, 1915–2013



Source: Authors' calculations using *Historical Statistics of the United States, Colonial Times to 1970* and US Census Bureau Statistical Abstract of the United States.