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3 Party Governance and U.S. Budget Deficits: Divided Government and Fiscal Stalemate

Mathew D. McCubbins

The president and members of Congress have been grappling with runaway budget deficits for over a decade. The 12-digit budget deficits of the 1980s have been blamed for everything from a decline in private investment and personal savings to trade imbalances with Japan. Collectively, the nation's policymakers seem akin to credit-card junkies, hooked on living beyond their means, borrowing to pay the interest on their debt.

Federal budget deficits are of course not new. Every president in the postwar period has run on a platform that included a promise to bring federal spending under control. Indeed, in only 10 of the last 60 years have federal revenues exceeded expenditures. Recently, however, real debt more than doubled from 1981 to 1988. As shown in figure 3.1, the swift growth in the debt as a percentage of the gross national product (GNP) in the 1980s reversed the general trend of the postwar period in which the ratio of debt to GNP had been declining.[1] The debt as a percentage of GNP in 1981 stood at slightly more than 32 percent. This jumped to 45 percent by 1985 and to over 50 percent in 1987.

Whole forests have been felled by analysts sawing through the causes and consequences of the runaway deficits of the 1980s. Two explanations for the occurrence of these deficits have received widespread currency. First, though much pulp was pressed over the four-bit deficits of the late 1970s, the plunge into the deficit abyss that followed Ronald Reagan's entry into the White House was a clear break from previous policies.

While constant-dollar-valued revenues for fiscal years 1982–84 were less

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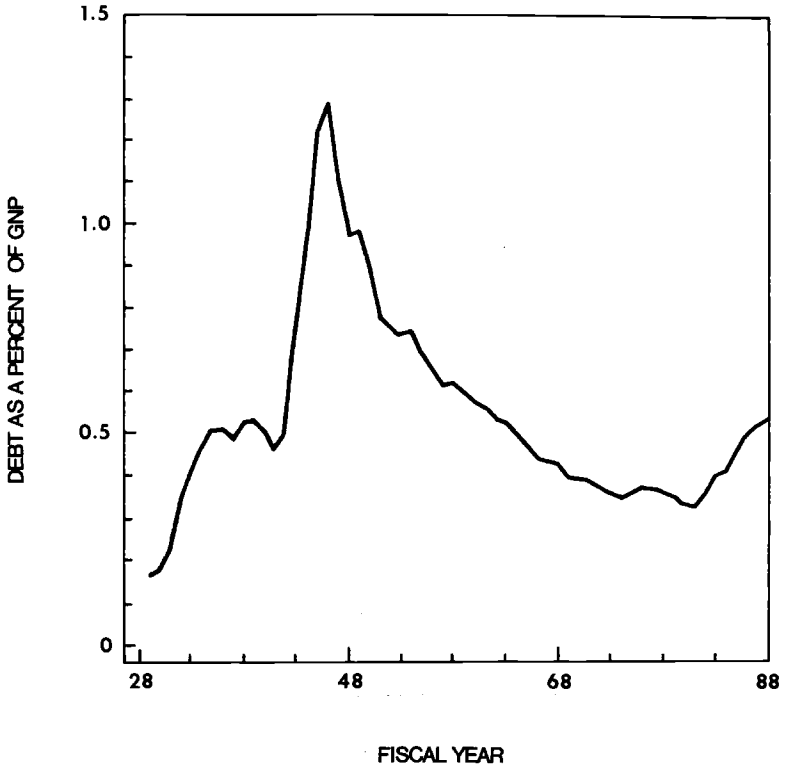

Fig. 3.1 National debt as a percentage of GNP, 1928–88

than the revenues collected under Jimmy Carter's last budget in 1981, constant-dollar levels of spending increased more than 8 percent. Indeed, over Reagan's first seven budgets, constant-dollar federal revenues increased by less than 21 percent, while constant-dollar spending increased by 25 percent. The discrepancy between spending and revenue in the 1980s led to constant-dollar federal deficits ranging from $50 billion to over $90 billion.

This explanation focuses on the central role of the president in budget policy. Presidents, it is argued, through their powers of persuasion, control of budgeting information, and use of the Office of Management and Budget (OMB) manipulate legislative outcomes, controlling the direction, if not always the magnitude, of policy change (Neustadt 1954, 1980; Wayne 1978).

Other analysts have seen the deficits of the 1980s as a consequence of a trend begun in the late 1970s. To them the deficits of the last decade arose from a change in the way Congress sets the budget. The Congressional Budget and Impoundment Control Act of 1974 (hereafter, Budget Act) prescribed new controls on presidential impoundments and it is important to note, established a new budget process in Congress. But the new process, instead of

balancing the budget, unleashed the spending profligacies of Congress from the restraining hand of the appropriations process.

Spending decisions, these scholars said, had been disciplined by the House Appropriations Committee, whose members saw as their role guarding the Treasury from the expensive tastes of their colleagues (Fenno 1966). The 1974 Budget Act, by reducing the role of the Appropriations Committee in determining spending, ruined the incentives for members of that committee to police the spending of their colleagues: members of the House committee, it is argued, no longer seek to cut executive spending requests, but instead seek to secure their own slice of the federal largess (Schick 1980).

These explanations represent two fairly common perceptions of American politics and the sources of American economic policy. The first is premised on the widely held belief that the president, in the twentieth century, has come to dominate policy-making. The second is based on a similar belief that congressional committees, in this century, have come to dominate policy-making.

The purpose of this essay, by way of examining the deficit crisis, is to examine these two views. I do so by questioning the basic tenets and inferences of each explanation. In so doing I also offer an alternative way to think about American politics, one that examines the relationships between the president and Congress and between Congress and its committees, within the institutional context of decision making. My central thesis is that congressional parties, to a greater extent than commonly thought, govern and determine public policy. I argue that divided partisan control of Congress in the 1980s, and divided control of government, led to rapidly increasing budget deficits, as the Democrat-controlled House and Republican-controlled Senate and presidency were unable to overcome the fiscal stalemate originally created in 1981.

3.1 Of Checks and Balances: The Thesis of Presidential Ascendency in American Politics

For much of the twentieth century, Congress has been seen to be in decline relative to the president. The greater efficiency of the executive branch and the inability of members of Congress to overcome their diversity of interests led members of Congress to "abdicate" their responsibilities in many key policy areas (Sundquist 1981, 28, 35–36).

Without presuming to undertake a full development of this thesis or my critique here, in the next few pages I reexamine the thesis of presidential dominance. My goal is to reexamine critically the thesis that the runaway deficits of the 1980s are the result of Reagan's policies.

3.1.1 Abdication or Delegation

The framers of the Constitution did not imagine that the president could attain a dominant position in federal policy-making. But it has become part of

the lore of American politics that the president has come to dominate national politics (Binkley 1962; Bryce 1924; Burns 1965; Laski 1940; Milton 1965; Neustadt 1980; Schlesinger 1973; Sundquist 1981). There is much evidence to support this thesis. The executive branch submits roughly 200 proposals to Congress every year, including budget requests, and legislative proposals relating to fiscal management, executive reorganization, and general policy. Congress frequently accepts these proposals without amendment (Pfiffner 1979; Peterson and Rom 1989) and, moreover, Congress almost never takes action on an issue until it has received a proposal from the president (Edwards 1980). Presidents also nominate several thousand people for federal posts. Rarely are these nominations rejected, and most receive only perfunctory review.

So how did this alleged transformation of national politics come about? Most of this increase in authority in the twentieth century has been the result of *congressional delegation* (Kiewiet and McCubbins 1991, chap. 7, 9). Congress, for example, in the 1921 Budget and Accounting Act redelegated the authority to transmit budget estimates from the various departments to the Bureau of the Budget and the President.[2]

The thesis of executive domination argues that in delegating, Congress actually has abdicated its authority to make decisions. The distinction here between delegation and abdication is more than semantic.[3] Many have argued, given the facts summarized above, that Congress no longer affects decision making on issues, such as the budget, that it has delegated to the executive branch.

But what can we actually infer from these stylized facts? They are entirely consistent with an interpretation that Congress, in delegating, actually has retained *all of its authority* over policy-making. The argument is as follows: Congress delegates to the executive branch its authority to make public policy. Members of Congress then use direct and indirect means (such as appointments, oversight, appropriations hearings, amendments to appropriations bills, etc.) to discipline those charged with carrying out this delegated authority (Kirst 1969; McCubbins and Schwartz 1984; McCubbins, Noll, and Weingast 1987; McCubbins, Noll, and Weingast 1989; Weingast and Moran 1983). Members therefore shape executive decisions as they are being made, thus largely relieving themselves of the need for the type of post hoc intervention that is the object of so many studies.

So how can we tell if Congress, in delegating, has retained control over policy-making? Evidence can be found in the ways Congress structures its delegations. Wherever Congress delegates to the executive branch or the president, we see the same attention to the details of structure, for the same reasons. The Budget and Accounting Act of 1921, for example, contains many provisions to control the revision, compilation, and transmittal of agency budget requests by the president (Kiewiet and McCubbins 1991, chap. 7).[4] These provisions have been amended and expanded many times in the intervening years (including the 1950 Budget and Accounting Procedures Act, the Gov-

ernment Accounting and Procedures Act of 1956, the 1958 Budget and Accounting Act, the 1970 Legislative Reorganization Act, among others; see Kiewiet and McCubbins 1991, chap. 7, for a complete discussion). Those who have argued that Congress has abdicated its responsibilities over policy-making have not ignored these facts, but they have missed their significance.

The question of whether delegation necessitates abdication can be asked in a somewhat different form. Others have admitted that Congress has the ability to exercise control; they ask instead whether its members lack the will to exercise control (Fiorina 1981).

At some times, of course, members of Congress do seem more willing to exercise control than at others. The efforts by Congress to restructure presidential discretion in the 1970s are prominent examples. Members of Congress take on the mantle of responsibility most often, however, when the president is from a different party than the one that controls Congress. Delegation is greatest, it seems, only when the president and the majorities in Congress share the same party label.

The abdication hypothesis, in its more subtle formulations, contends that the delegation of policy initiation, as in the budget, has tilted the balance between the branches toward the president.[5] And, it was the establishment of legislative clearance at the Budget Bureau that has been heralded as the principal source of presidential dominance in this century (Sundquist 1981). What must be remembered, however, is that "Congress created OMB. Congress can uncreate it—or change it" (quote found in Brand 1985, 1815; see also Kiewiet and McCubbins 1991; Wilmerding 1943). Even with an explicit delegation of authority to the president, as in the Budget and Accounting Act of 1921, Congress need not even consider the president's proposal. Referring to his troubled budgets at a press conference on October 22, 1987, Reagan observed that "every year under the law I submitted a budget program early in the year, and as they've done every year I've been here, they've put it on the shelf and have refused to even consider it" (*Congressional Quarterly Weekly Report* [24 October 1987], 2626). "When the delegation is not a power to act but only responsibility to recommend," Sundquist observed (1981, 12), "the executive budget, for instance—the Congress explicitly retains not only its full authority but also its responsibility to act."

Presidents do, nonetheless, gain some influence over outcomes through the recommendations they make. Because their electoral fates are partially linked, the president and his party in Congress will often find it in their best interest to cooperate. How much influence the president holds in this process is open to debate, particularly when his party is in the minority in both houses of Congress.

3.1.2 Presidential Power and the Veto

In contrast to the powers delegated the president by Congress, the veto conveys to the president a property right in the legislative process. The president's

proposal may matter on some occasions and not on others, but the veto applies to all acts of Congress.

Some people, in analyzing presidential vetoes, have inferred that it is ineffective because it is rarely used. Again, as in the thesis of presidential dominance, this is a mistaken inference. Members of Congress logically anticipate the president's reaction to their proposals. Their proposals, then, usually are designed to avoid a veto.

The influence that the veto gives the president is, however, asymmetrical. The president can use the veto to restrain Congress, to some extent, when he prefers to spend less than its members prefer. But it provides the president with no means of extracting *greater* appropriations (Kiewiet and McCubbins 1988). This asymmetry derives from inherent limitations in the veto power. The veto provides the president with only the power to reject; it does not provide him with the power to amend.

On spending bills, the president's position is even more precarious: on receiving a bill from Congress, the president can either accept the appropriations contained therein or veto it and let Congress write a continuing resolution.[6] Because of the emergency nature of continuing resolutions, they are virtually veto proof. Also, because continuing resolutions almost always contain less spending than is contained in the corresponding appropriations bill, the president is able to reduce spending (to the level contained in the continuing resolution) through the use or threat of the veto, but he cannot get increased spending from a Congress that does not favor it.

Again, the details of the situation did not escape Ronald Reagan's understanding:

> The President of the United States cannot spend a nickel. Only Congress can authorize the spending of money. And for six years now I have repeatedly asked the Congress for less money and they have turned around and given more—given more to spend, and done it in such a way that I can't veto it when they put it all together, instead of appropriations, in a continuing resolution—we haven't had a deficit—or, a budget since I've been here. No—the Congress is the one that's in command. . . . And every budget I've sent up there has been put on the shelf and I've been told that it's dead on arrival. (*Congressional Quarterly Weekly Report* [24 November 1987], 2628)

The limited and asymmetric influence conveyed to the president by the veto is illustrated by the budget debates in Reagan's second term. For fiscal year 1985, Reagan proposed a 13 percent real (inflation-adjusted) increase in defense spending for the following year. He coupled this with a proposal to slash Social Security and domestic spending and to eliminate cost of living adjustments (COLAs) for federal pension payments (including Social Security).

The political reality on Capitol Hill, however, did not favor a package of defense increases and domestic spending cuts. Reagan buckled to the pressure and reduced his defense request to a 5.9 percent inflation-adjusted increase.

On the other hand, he requested steep "cuts" in domestic spending totalling $34 billion in current dollars.

The package of domestic spending cuts and defense increases was still unacceptable to Democrats and liberal Republicans. In March 1985, the Senate Budget Committee voted to recommend an inflation-adjusted *freeze* on defense spending and a freeze on Social Security.

Faced with a projected deficit exceeding $200 billion (current dollars) for 1986 and trying to unite a fractured party, the Senate Republican leadership negotiated with Reagan a 3 percent real increase in defense spending. The package also included deep "cuts" in domestic spending. Reagan declared that a 3 percent real increase was the "rock-bottom level" he would accept (*Congressional Quarterly Weekly Report* [27 April 1985], 771).

But, Reagan was holding the wrong end of the veto stick. Despite Reagan's veto threat, the Senate rejected the Republican leadership's package. Ultimately, the Senate approved a budget resolution that only reduced, but did not eliminate, COLAs and that provided no real increase in defense spending.

On the other side of the Capitol, the House, voting along party lines, recommended more spending for domestic programs and less for defense than the budget passed by the Senate. Reagan pronounced the House budget resolution as "unacceptable" (*Congressional Quarterly Weekly Report* [25 May 1985], 971). In conference the House and Senate compromised on defense, but accepted much of the domestic spending increases advocated by the House. As expected, Reagan accepted the bills passed under this resolution.

In the final analysis, presidents do make numerous proposals to Congress. Congress generally takes no independent action on an issue prior to the president's request. This does not, however, imply congressional abdication or presidential ascendency. If presidential proposals are to succeed, the president must anticipate the reaction of members of the House and Senate to his proposals and accommodate their demands and interests. Presidents know this, so they rarely submit proposals that are likely to fail. Those who ignore this lesson have their proposals ignored.

3.1.3 The Reagan Revolution and the Determinants of Federal Spending Policy

The budget for fiscal year 1982 was heralded (or decried) as a victory by a powerful president over an institutionally weakened Congress. But what sort of victory was this for Reagan? The much-ballyhooed $36.6 billion budget "cuts" were measured not against the spending totals in the fiscal 1981 budget, but against Carter's proposed budget for fiscal year 1982 (in which he requested a whopping 17 percent nominal increase in spending relative to spending enacted for fiscal year 1981).

A vast majority of the programs and agencies that suffered cuts in Reagan's budget had previously suffered cuts by the Democrats and Jimmy Carter, and almost half had their budgets cut by Democratic Congresses when Gerald

Ford was president. Real spending in the commerce, energy, housing and urban development, interior, and labor departments, and in the Postal Service, had declined through most of Carter's administration. Spending on public works, other than sewage treatment plants and other environmental programs, had been declining since the late 1960s. Further, defense, expanded under Reagan's budget, also grew in Carter's last two budgets. Real spending on other federal programs, such as those in the Department of Education and Department of Transportation (DOT), declined in 1982, but then climbed steadily to new highs over the remainder of Reagan's first term.

Thus, though the 1982 budget may have accelerated an existing spending reallocation, it was not a radical change. Where Reagan did try to depart from the budgetary consensus of the previous administration, he was rebuffed. Almost all of the programs scheduled for termination by Reagan in fact survived his tenure in office.[7]

What responsibility, then, does Reagan bear for the runaway deficits of the 1980s? Constant-dollar spending grew at a faster rate during Reagan's administration (25 percent from 1981 to 1988) than during the Eisenhower (16 percent growth), Nixon (13 percent), Ford (3 percent) and Carter (12 percent) administrations. Annual changes in real spending varied from a low of *minus* eight percent in 1954 to a high of 13 percent in 1967. Reagan averaged a 3.3 percent annual increase (constant dollars) in spending.

On the other hand, Reagan, in his first three budgets, requested decreases for most domestic programs, whereas on average, most postwar presidents have requested nominal increases averaging close to 10 percent per year for domestic programs.[8] Expenditures for many domestic programs declined in the 1980s. Whereas nominal spending had grown, on average, between 8 and 11 percent per year (for the programs and agencies I examined) for each president from Truman to Carter, spending growth under Reagan was held to less than 1 percent per year. Thus, there is some reason to believe that a new direction in American politics was blazed by Ronald Reagan in his first term in office.[9]

But, Reagan did not have to contend with large Democratic majorities in both chambers of Congress, as did Eisenhower, Nixon, and Ford. Indeed, the Republicans owned a majority of seats in the Senate for the first time in over two decades during Reagan's first six years in office. In the 1980s with the Republicans controlling the Senate and the Democrats controlling the House, spending was cut, on average, for only 30 percent of the items in my sample of 69 agencies (which includes 63 domestic and six defense agencies). When the Republicans controlled both houses of Congress (1947–48 and 1953–54), by contrast, they cut over 42 percent of the items in my sample. In fact, the Republican Congress of 1953–54 cut spending for almost *two-thirds* of the programs in this sample, *more than twice the rate of cuts garnered by Reagan.*

The question becomes, what was the net effect on spending of Reagan's occupancy of the White House? Certainly, Reagan was no more successful,

under the circumstances in Congress, then expected.[10] Reagan was actually *less* successful than any other postwar president at pushing his spending cuts through Congress. Truman succeeded in getting Congress to enact cuts for all of the relatively few items for which he requested a cut in spending. Eisenhower succeeded 84 percent of the time. Reagan by contrast succeeded less than 60 percent of the time. Also, his batting average at getting spending *increases* out of Congress was *less* than any recent president. More generally, Reagan's success rate in influencing congressional votes for each of his eight years in office was less than that of Dwight Eisenhower in each corresponding year (Stanley and Niemi 1988, 220–21). Indeed, Reagan's success rate in 1987–88 was less than Richard Nixon's success rate *even during the period of the Watergate scandal* (Nixon won roughly 60 percent of his key votes that year). Thus, by this comparison Reagan was a weaker president than his predecessors.

3.1.4 Federal Expenditures in the 1980s

So what accounts for the budgets of the 1980s? In the first place, though there has been much talk of budget "cuts" in the 1980s, constant-dollar spending nearly *doubled* from fiscal year 1981 to 1989. And, whereas gross national product (GNP), valued in 1972 dollars, grew less than 24 percent from 1981 to 1988, real spending grew over 25 percent. As shown in table 3.1, real spending at the Department of Agriculture grew by more than 50 percent from 1981 to 1986; defense spending in constant 1972 dollars grew from $79 billion in Carter's last budget to $117 billion by 1986. At the same time, the Department of Health and Human Services grew by 35 percent in real terms, while spending at the Justice Department, the State Department, DOT, and the Treasury also grew quickly.

Second, those agencies and programs chosen for spending reductions in the 1980s were largely ones whose budgets declined throughout the latter part of the 1970s. The Great Society programs (especially housing programs) and the regulatory activities of the federal government started declining under Gerald Ford, and their decline accelerated under Jimmy Carter. The reduction of these programs was therefore begun under a Democratic Congress and was accelerated when both branches were controlled by the Democrats.

Real spending declined in Reagan's first budget (relative to the budget for 1981) for eight departments and programs: Commerce, Education, Energy, EPA, Housing and Urban Development, Interior, the Post Office, and DOT. Of these eight declining spending categories, two (Energy and the Post Office) were continuing declines begun under Carter's 1981 fiscal year budget. Carter had requested spending cuts for three others: Commerce, Housing and Urban Development and DOT. The remaining three departments and programs that declined in Reagan's first budget—Education, EPA, and Interior—constituted new spending reductions and can rightfully be attributed to Reagan and the Republicans in the House and Senate. For each of these three departments,

Table 3.1 **Constant-Dollar Appropriations for Selected U.S. Executive Departments, 1969–88**

Fiscal year	DoA	DoC	DoD	Energy	HHS	HEW	HUD	DoL	DoT
1969	8.5	1.4	92.1			65.8	3.3	6.0	9.0
1970	10.3	1.1	82.5			70.1	8.8	5.7	9.0
1971	10.3	1.2	74.2			73.6	3.6	6.9	12.0
1972	12.7	1.4	72.6			78.3	3.9	9.0	8.6
1973	12.7	1.6	72.6			85.0	4.1	9.1	6.7
1974	10.2	1.3	66.0			92.7	3.8	7.9	20.0
1975	11.5	1.3	66.8			92.2	40.0	20.9	14.9
1976	11.0	1.7	69.9	3.3		96.1	20.2	13.9	5.7
1977	9.5	2.7	75.1	4.4		106.5	13.6	18.2	9.0
1978	10.0	1.5	73.0	4.4		110.8	25.0	14.8	8.7
1979	15.4	1.6	72.4	6.4		111.7	19.2	11.9	10.1
1980	11.8	1.3	72.8	15.5		115.5	18.1	14.9	9.5
1981	12.4	1.4	79.4	5.2	113.9		17.9	15.5	12.5
1982	12.0	.8	93.3	4.2	122.6		10.3	14.8	8.6
1983	15.6	.8	102.8	4.6	125.0		5.2	15.1	14.7
1984	16.5	.9	106.5	4.8	132.6		5.6	21.5	11.3
1985	15.3	.9	115.2	4.9	146.3		5.2	13.9	11.6
1986	18.6	.9	117.2	5.0	153.9		6.7	13.6	10.8

Note: Abbreviations: DoA = Department of Agriculture; DoC = Department of Commerce; DoD = Department of Defense; Energy = Department of Energy; HHS = Department of Health and Human Services; HEW = Department of Health, Education and Welfare; HUD = Department of Housing and Urban Development; DoL = Department of Labor; DoT = Department of Transportation.

however, real spending *rose* quickly in fiscal years 1983–86, undoing much of the reallocation of 1982.

The budget story of the 1980s, then, is not the fiscal contractions so often advertised by Congress and the president. But several questions remain unanswered. Why should spending have grown during the administration of a fiscally conservative president supported by a Republican Senate? Should not the deficit have receded during Reagan's two terms? To answer these questions I must first discuss congressional politics and the effect of the budget process on spending decisions.

3.2 Party Governance in Congress

To some analysts of American politics, the runaway deficits of the 1980s are not the unintended result of the Reagan revolution, but rather a consequence of a change in congressional procedure. This perception is based on a well-accepted view that Congress is not so much a democratic institution as a "pluralistic leviathan" (for a model of congressional politics based on this

view, see Stigler 1971 and Becker 1983). Central to this view is the thesis that congressional politics is committee politics.

The "interest group liberalism" that purportedly dominates congressional politics, if true, has profound implications for budgeting. As Shepsle and Weingast (1984, 355) argue, "Legislators invent programs, seek funding, and are especially attentive to policy areas that create or maintain jobs within their electoral constituency. . . . Expenditure programs are, as a consequence, biased away from least-cost methods of production." As each subgovernment pursues its policies in the way Shepsle and Weingast describe, the end result could be that the government outspends its receipts.

To mitigate the effects of interest group liberalism, members of Congress purportedly have relied on members of the House Appropriations Committee to make the hard choices between supporting their colleagues' programs and the need to economize on spending (Fenno 1966). This system was supported by rules and procedures in Congress that separated authorization from appropriations. And the system appeared to work reasonably well, producing small but manageable deficits through the 1950s and 1960s.

This all changed with the Budget Act of 1974. By transferring authority for establishing overall spending limits to the budget committees, the act so weakened the House Appropriations Committee that it could no longer guard the Treasury. Instead, its members seemingly became claimants on the federal Treasury rather than its protector (Schick 1980).

Two assumptions underlie this explanation of the deficit crisis. First, that "power in Congress has rested in the committees or, increasingly, in the subcommittees," and thus, as a consequence, "throughout most of the postwar years, political parties in Congress have been weak, ineffectual organizations (Dodd and Oppenheimer 1977, 40). Second, that the House Appropriations Committee was once the "guardian of the federal Treasury" and now is only a subdued guardian. I examine these assumptions in turn, arguing that congressional parties and party leaders exercise more control and greater influence in congressional politics, and in budgeting in particular, than commonly has been perceived. I then seek to explain the budgetary decisions of the 1980s in light of this new understanding.

3.2.1 The Institutions of Agency: Parties and Committees

The common view of weak parties and autonomous committees in Congress, in its logical form, is identical to the view of presidential dominance presented in section 3.1 above. The membership of each house has delegated to the committees in each house wide-ranging authority to write legislation, hold hearings, and oversee the executive branch. This delegation, as was the case in interpreting delegation to the executive, has been mistaken for abdication.

Two factors underpin the importance and autonomy of committees and sub-

committees, according to this view: committees have jurisdictional monopolies, and thus an ex ante veto over proposed legislation; and committees honor each others' jurisdictional autonomy through a system of deference and reciprocation (Shepsle and Weingast 1984, 351, 353).

This view of committee and subcommittee power has been developed to explain a set of generalized observations on congressional behavior. It explains, for example, why coalitions within Congress are seemingly universal and nonpartisan—the reason is that all members face the same necessity, to bring home particularistic benefits, and the institutions are geared toward establishing and enforcing vote trades across projects and benefits. It also follows, for the same reason, that party discipline will be very lax—the vote trades cross party lines. Committees also use their powers, particularly their ex post veto, to ensure that amendments rarely get offered to their bills, and, when they are offered, few, if any, are successful.

These observations also are consistent with party control of committees. Indeed, none of the things listed above discriminate between the two views.[11] However, we do observe obvious violations of this cozy view of subcommittee autonomy. For example, multiple referrals, where legislation is sent to several subcommittees, are increasingly common in the House.

Members of Congress design their institutions to fit their purpose. Students of American politics have tended to focus on those aspects of congressional institutions that enable members to bring home private goods (projects or programs for their own districts). Studies of congressional behavior have focused largely on how members secure water projects, military bases, roads, and post offices for their districts, and the consequences of these activities for their political survival. These studies, of course, assume that voters appreciate projects in their district and that members can build reputations as good providers of federal pork.

But, party affiliations are also an important ingredient in voters' decisions: party labels signal information that is otherwise very expensive for voters to obtain about the policy positions of candidates. As a result, politicians, in seeking office, also establish reputations as partisans. Thus, politicians adopt a mixture of collective, that is, partisan, and individual, that is, district-oriented, activities in seeking reelection.

It follows that members will seek to structure Congress in such a way as to facilitate *both* of these activities. Party organizations, their leadership, and the committees that serve them, provide the institutional means for pursuing the collective goals of party members.

But these pursuits are not to the exclusion of individual district-oriented benefits. Thus, the majority-party leadership uses its agenda powers, in concert with the agenda powers assigned to committees, to secure the omnibus pork-barrel logroll so familiar to congressional scholars.

The congressional parties, of course, delegate much of the authority to make these kinds of decisions to the leadership and to committees, though the

Democratic caucus has at times sat down as a whole and made policy for the Democratic majority. In delegating, the congressional parties encounter the agency problems ubiquitous to human experience: for a variety of reasons, intentional or not, the person to whom authority is delegated may not carry out their authority in the best interests of those doing the delegating. So pernicious are these problems that their existence has led many scholars to conclude that the congressional parties have in fact abdicated their authority to the standing committees and subcommittees of Congress.

The abdication conclusion, however, ignores the efforts on the part of the congressional parties to mitigate delegation problems. In essence, like the separation of powers designed into the structure of the federal government, party organizations—in particular the party leadership—and the system of standing committees, form a separation of powers, a system of checks and balances. Party leaders use a hierarchical system of committees (capped by the "control committees," i.e., Rules, Appropriations, and Ways and Means in the House), control of committee appointments and procedural restrictions to steer policy outcomes in favor of the collective interests of the majority party (Rohde and Shepsle 1973; Shepsle 1988; Cox and McCubbins 1991; McCubbins and Schwartz 1984; McCubbins and Page 1987; McCubbins et al. 1987, 1989).

Some standing committees, of course, more closely involve the party label than do others. The actions of these committees affect everyone in the party, and, collectively, the party and its leaders have a greater interest in mitigating the agency problems that arise vis-à-vis these committees. Other standing committees, such as Post Office and Civil Service, Interior, and Merchant Marine and Fisheries, have jurisdiction over issues unrelated, or only minimally related, to the issues that voters identify with the party.

Delegation, in this case from the majority party caucus to the standing committees of Congress, in the conventional view of committees has been mistaken for abdication (Kiewiet and McCubbins 1991; Cox and McCubbins 1991). The transfer of authority has been recognized, the actions of the agents (i.e., committees) witnessed. What have not been appreciated, however, are the mechanisms used by the majority party to direct the actions and choices of their committees and the effect these mechanisms have on committee actions.

If committees are agents of party caucuses then we expect that most of the decisions in Congress would be made in committee—that is, after all, their function—and that committee members would acquire expertise in the committee's jurisdiction—that is after all why they were delegated the jurisdiction in the first place. We do not expect these functions to be uncontrolled, however, and we witness many and varied attempts by majority party caucuses and their leadership to control committees. Further, having anticipated the reaction of the majority party to its proposals, the committee can expect that few of its bills will be amended or rejected on the floor.

3.2.2 The Role of the House Appropriations Committee

In Richard Fenno's (1966) classic account, the House Appropriations Committee was depicted as a budget-slashing "guardian of the federal Treasury" (353), protecting the House from the budgetary excesses of its own committees and from budget-maximizing bureaucrats. Fenno reported that the House Appropriations Committee cut the amount requested by the president in 73.6 percent of the 575 cases in his data set (Fenno 1966, 353, table 8.1). For a set of 69 agencies and programs, including almost all of Fenno's 36 bureaus, for a period extending from 1948 to 1985, I found that the committee cut the president's requests for 70.4 percent of 1,983 cases.[12]

But, do these statistics constitute evidence that the "dominant pattern" (Fenno 1966, 353) for the House Appropriations Committee is to guard the Treasury? If the procedural restrictions on the Budget Bureau constrain the bureau's ability to revise agency budget estimates, and agencies compile estimates in accordance with authorizing legislation, then presidential requests will reflect, to a large extent, the level of funding preferred by the authorizing committees in Congress.[13] If many committees prefer more spending on items within their jurisdiction than preferred by the House majority party as a whole, and if the House Appropriations Committee is relatively representative of the majority party,[14] then House Appropriations will often *appear* to "guard" the Treasury.

In Fenno's account of the House Appropriations Committee, party politics plays essentially no role. I have argued here and elsewhere (Cox and McCubbins 1991; Kiewiet and McCubbins 1991) that the committee functions as an agent of the majority party, pursuing the collective policy goals of the majority party's membership. These goals may sometimes be to cut the budget, but they are not necessarily so. Consequently, the varying goals of the parties controlling the White House and the House of Representatives determine, for example, the treatment afforded the president's budget requests by the House Committee on Appropriations, with Democratic majorities favoring higher spending on domestic programs than Republican majorities. How often the committee cuts the president's requests varies with partisan factors.

The House committee is most likely to cut the president's requests when the president is a Democrat and the House is controlled by the Republicans (cuts amount to 93 percent of actions taken). The committee is somewhat less likely to cut the executive's requests when the same party controls both bodies—whether controlled by the Democrats or the Republicans, the committee cuts nearly 80 percent of the requests in my sample; but, a Democratic committee is far less likely to cut a Republican president's requests: only 57 percent of requests were cut by the committee under these circumstances. Under Reagan, the committee cut only 38 percent of the president's requests, and actually proposed *increases* for 55 percent of the items. Fenno described such changes as "mood" swings, where the committee would shift from an "econ-

omy mood" to a "spending mood." My data suggests that the mood toward executive budget requests by the House Appropriations Committee is determined by partisan differences between the House, Senate, and the executive.

Further, if the guardianship hypothesis is correct, I would never expect the House, in its amendments, to decrease the committee's recommendations. The committee, after all, is supposedly doing a job the House is incapable of doing, holding back spending. However, I found that more than 58 percent of individual, floor changes were decreases, and only 42 percent were increases. Of the appropriations bills amended by the House that I examined, 106, or 43 percent, reduced the totals recommended by the House Appropriations Committee.

Has the 1974 Budget Act changed the Appropriations Committee from the Treasury guardian it once was? There is no evidence that it was a guardian or that its function has in fact changed. It has been, and still is, a check used by the majority-party leadership to ensure that the policies pursued by the other standing committees in the House reflect the collective goals of the membership of the majority party (Kiewiet and McCubbins 1991, chap. 3).

3.2.3 The Congressional Budget Process in the 1980s

The budget process created by the 1974 act has three key components. First, it created budget committees responsible for setting guidelines for all aspects of federal spending and revenue. Second, it requires authorizing committees to "reconcile" spending policy within their respective jurisdictions with the guidelines. Third, if a committee fails to recommend legislation providing satisfactory reconciliation, then the budget committees can write the reconciliation legislation for them.

To ensure that the budget committees are responsible to the majority-party caucus and its leadership, the act also established a special relationship between the committee and the party leadership. Members are handpicked by the leadership, and tenure and seniority norms observed for other committees do not apply. The majority-party leadership, by these procedures, has relatively greater control, year in and year out, over the composition of the budget committee than it does over the composition of any other committee, allowing the majority party leadership to use the budget process to inject the majority party's priorities into the decisions of all committees.

Indeed, from the perspective of floor majorities in the House and Senate, the budget process has been strikingly effective in the 1980s. In 1981 the Republicans in the House and Senate, together with some conservative Democrats used the budget and reconciliation process to "cut" some $36.6 billion in spending for fiscal year 1982.[15] The first budget resolution called for the House Committee on Agriculture to write legislation bringing about "cuts" of $2.2 billion in fiscal year 1982 budget authority; required the House Committee on Banking and Urban Affairs to "cut" budget authority in its programs by $12.9 billion; the Committee on Education and Labor to cut $13.5 billion; the

Committee on Energy and Commerce, $6.4 billion; and the Committee on Public Works and Transportation, $6.6 billion. In this case a majority consisting of Republicans and conservative Democrats in the House rolled the House Democratic leadership in the budget process. This coalition's use of the process demonstrated how effective the process could be at submitting congressional committees to the will of floor majorities. It would also mark the only time the House Democratic leadership was rolled.

The first budget resolution in 1982, for fiscal year 1983, required "cuts" of $2.2 billion in budget authority. This time, the House Democratic party, using inventive procedures, such as the "King of the Mountain" rule,[16] managed to reestablish some control over the course of the budget process. The resolution required the revenue committees to recommend legislation to raise $20.9 billion in additional funds. The budget resolution also required "savings" of $7.8 billion in defense spending.

The House Democrats used the budget process in 1983 to draft their own budget blueprint as an alternative to the Republican budget submitted by Reagan. The Democrats' budget added $33 billion in domestic spending to Reagan's proposal, requested $30 billion in new revenues, and "cut" Reagan's defense request by $16 billion.

The Republicans in the Senate and the Democrats in the House chose alternative strategies in using the budget process to further their programs. The Republican leadership used the budget process to give direction to Senate committees. The Democrats used the budget process as a means to unite the party behind a common program, with the House Budget Committee holding hearings with the entire Democratic caucus.

Ultimately, the result of these efforts on the part of party caucuses to control the product and actions of committees is that spending policy reflects the desires of the majority party in each chamber. Indeed, the single best predictor of changes in spending policy for almost the whole range of federal programs and agencies is party control of Congress and the White House (Kiewiet and McCubbins 1991, chap. 8). This analysis suggests that policy is influenced, to a far greater extent than commonly believed, by party politics.

3.3 The Partisan Roots of Deficits

Having rejected the two most common explanations of the runaway deficits of the 1980s, how can they otherwise be explained? To explain deficits, I first need to explain federal spending and revenue policies, and how they are affected by divided government.

With regard to federal spending decisions, it can be shown that these, at every stage of the spending process, reflect party politics.[17] Domestic agencies, for example, do better under Democratic administrations and Democratic Congresses than under Republicans. Defense and high-technology programs do better under Republican administrations and Republican Congresses than under Democrats.

When the president is a Republican and both houses of Congress are controlled by Democrats, spending on domestic and social programs is somewhat restrained, but is close to the levels that would have been adopted had the Democrats controlled the White House as well. In such instances, though the Republican presidents act as a restraint on domestic spending, the ability of Congress to package various spending items into an omnibus bill makes it difficult for even the most ardent Republicans to limit spending.

But, what happens when control of Congress is divided, when a Democratic majority controls the House and a Republican majority controls the Senate?[18] This has happened several times, mostly in the waning decades of the nineteenth century, though in this century it has occurred twice, once during the second half of Hoover's administration and most recently between 1981 and 1986.

The Constitution established a bilateral veto game between the two chambers, and each chamber holding a check on the actions of the other. The cooperation and coordination necessary to overcome these constitutional checks and balances is frequently inadequate. Budget deficits present members of Congress with a collective dilemma: everyone would be better off if deficits could be reduced, but, individually, members are not willing to reduce spending on their preferred programs or to raise taxes for their constituents. Party discipline is often required to solve such collective dilemmas. Neither congressional party is likely to go along with a solution to a problem such as the deficit for which the other party can claim credit, and each will use its institutional position to defeat the other party's attempts to solve the problem. What is implied by divided control, then, is that the cooperation to solve collective problems, like the deficit, will largely be nonexistent.

What then will be the equilibrium to this bilateral veto game? In an effort to model this game I make a simplifying assumption about the preferences of the members of each party. I assume that there are two types of programs: domestic programs favored by the Democrats and defense programs favored by the Republicans. The preferences of the two parties over budgetary allocations to these two goods is given in table 3.2. The Democrats, I assume, prefer most that spending on their programs be increased, while spending on the Republicans' programs be decreased (denoted D, r in the table). Democrats next most prefer that spending on all programs be increased (denoted D, R). Democrats are then assumed to prefer decreases in both their own programs and the Republicans' programs (denoted d, r) to a decrease in their programs with an increase in the Republicans' programs (d, R). I assume that Republican preferences are similar with respect to their own programs.

In bilateral veto games, the reversionary outcome (i.e., if no solution is adopted) determines what if any cooperative solution will be an equilibrium. The spending reversion point for most federal programs is zero. Congress must annually enact legislation appropriating money for most of these activities if they are to continue. Typically, however, Congress will pass a continuing resolution that pegs spending at some low baseline level (often at the

Table 3.2 **Party Ranking of Spending Allocations**

Democrats	Republicans
D, r	d, R
D, R	D, R
d, r	d, r
d, R	D, r

Note: D denotes increased spending on Democratic programs; R denotes increased spending on Republican programs; d denotes decreased spending on Democratic programs; and r denotes decreased spending on Republican programs.

spending rate for the previous fiscal year) if no appropriations bill is enacted. Continuing resolutions typically yield little or no growth in spending and may even entail a modest decrease (adjusting for inflation) in spending for the programs covered by the resolution. Thus, the reversion, if no spending policy is agreed to by the two parties, is to decrease appropriations for all programs (i.e., the outcome denoted d, r in the table is the reversion point).

The only alternative in the table, then, that is preferred by both parties to the reversionary outcome and thus will not be vetoed by one or the other party, is the outcome in which spending for the programs of both parties is allowed to increase (denoted D, R). Thus, under conditions of divided control, I expect overall spending to *increase.*

In 1983, for fiscal year 1984, for example, reconciliation legislation did not "cut" budget authority in any area. In 1985, for fiscal year 1986, reconciliation legislation passed by Congress and signed by the president, though requiring "cuts" in agriculture, defense, energy, Medicare, and 10 other programs, increased spending for the EPA's Superfund, income and social security programs, veterans' affairs, and three other programs. The following year, there again were no significant "cuts" in any area.

Throughout the decade, the Democrats in the House and the Republicans in the Senate forged a union that enacted policies *contrary* to the basic tenets of Reagan's budget policy. In his second term this "coalition" enacted increases in social and education programs and "cuts" in defense spending, despite Reagan's strenuous opposition.

I have already noted that spending increased during Reagan's two terms in office—nearly doubling in current-dollar terms during these eight years. The Democratic-Republican spending compromise can be seen in an examination of the budget. Though some areas of domestic spending were reduced, largely those that were under pressure in earlier decades, other areas increased tremendously. Defense spending also increased during Reagan's first term. As expected, this spending compromise was abrogated once the Democrats regained control of the Senate. With unified party control of Congress, the Democrats could undertake to cut back on those programs favored by the Republicans, namely defense.

With regard to federal revenues, the story is much simpler. The logic of the

revenue game is presented in figure 3.2. The figure presents the ideal points of congressional Democrats (denoted D in the figure), Southern Democrats (SD), and Republicans (R), in an abstract policy space whose dimensions are the incidence of the tax system (along the horizontal axis) and the tax rate (along the vertical axis). The incidence of the tax system can be thought of as identifying the individuals who will carry the tax burden (from richer to poorer); the tax rate merely runs from zero to 100 percent of income. I assume that the loss of welfare to each player as the policy moves away from that player's ideal point is proportional to the distance from the ideal point (that is, their indifference contours can be represented as circles). If this is the case, the triangle defined by the line segments connecting the three ideal points contains all the Pareto-optimal outcomes—that is, the policy choices that cannot be changed without making one of the three members worse off.

Before the victory by Reagan and the Senate Republicans in 1981, I assume tax policy was set by the Democrats and was at D, their ideal point. Had the Senate remained under Democratic control, or had the Democrats maintained a large enough majority in the House, no change in tax policy would have been expected, as the Democrats would have had the institutional means to

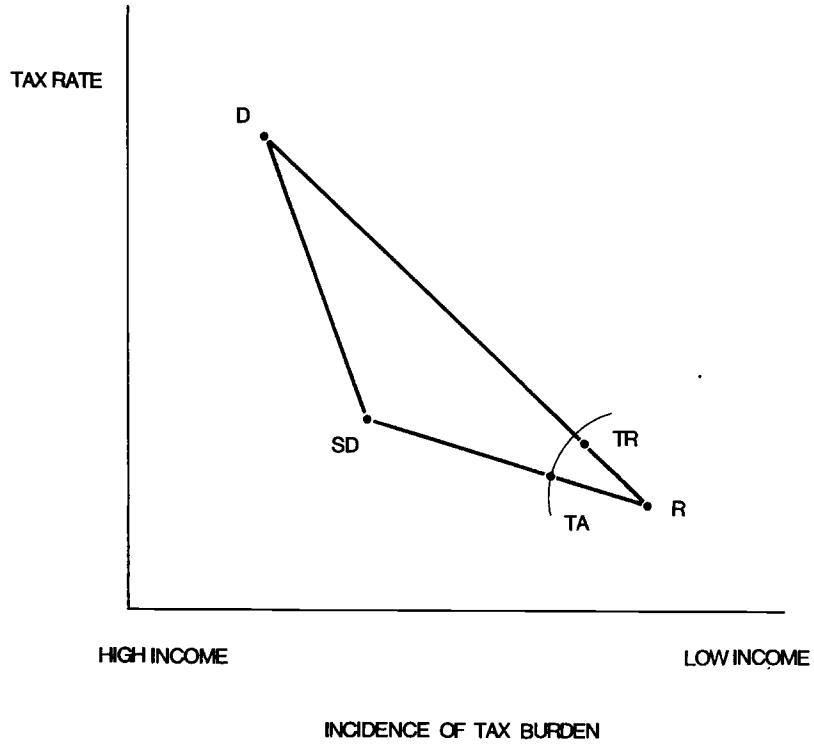

Fig. 3.2 Divided government and tax reform

veto any changes in the status quo (which was D). But, after the 1980 election, the Republicans were able to strike a deal to change the tax system with conservative, mostly Southern, Democrats in the House. The new tax policy was then chosen somewhere between SD and R in figure 3.2, at a point such as TA. This point was a new equilibrium: once Reagan proposed the tax cut, and the Senate Republicans endorsed it, the Democrats felt they could not oppose it. Once the tax reduction was enacted, however, tax increases could not be passed, even in the face of mounting budget deficits. Reagan promised to veto any tax increase, and with a large Republican minority in the House and Republican control of the Senate, such vetoes were certain to be sustained. The 1981 tax cut reduced current revenues for each succeeding year by over $100 billion.

It was not until the 99th Congress that a new deal, this time between the Democrats, who controlled the House, and the Republicans, who controlled the Senate and White House, could be struck. This new tax policy, denoted TR in the figure, is not much different than the previous tax policy, TA. The reforms of 1986, however, were preferred by both the Democrats and the Republicans to the 1981 tax policy. Tax policies that would raise revenue, as proposed by the Democrats, require that one or the other of the parties (presumably the Republicans) be made worse off. Since each party controls a veto in this game, by virtue of their holding one or the other branch of government, no increase in revenue was possible. Divided party control within a setting of a bilateral veto game as established by the Constitution, then, led to a form of stalemate in which the deficit problem was allowed to fester.

Spending continued to climb at the same constant rate throughout Reagan's administration. Revenues were climbing at almost exactly the same rate as expenditures prior to 1982, with a relatively small difference between the two trends. As a result of the 1981 tax cut, revenue declined for three years from 1982 to 1984. After 1984, revenues again paralleled expenditures, but with a dramatic increase in the deficit.

Taken together, the effect of divided government on revenue and spending decisions, and the effect of the tax cut of 1981, produced the runaway deficits of the 1980s. The pattern is not new, it has recurred throughout the twentieth century: since 1929, divided government has yielded sizable increases in the national debt. Indeed, the increase in the debt attributable to divided government exceeds the effects of national unemployment and inflation by an order of magnitude (these results are reported in the appendix below). If the Democrats continue to hold majorities in the House and Senate, and the Republicans continue to occupy the White House, then little progress will be made toward reducing the national debt.

3.4 Conclusion

Drawing from the literature on American national government, two explanations for the runaway deficits of the 1980s have received widespread com-

ment. The first is that the president did it—that Ronald Reagan, on his way to forging a revolution in American politics, put into place policies that pushed America over the deficit precipice. The second has its roots in Congress—that the Budget Act of 1974 led to the unraveling of fiscal restraints in Congress. Both of these explanations have, at their core, a perception that congressional parties are merely shells within which policy is bartered and to which no control over policy is granted. Congressional majorities, in these models, have abdicated their collective responsibilities over national policy on the one hand to the president and, on the other, to congressional committees and subcommittees.

The deficits of the 1980s are the consequence of a structural problem: divided government. Once the deficits of the 1980s were in full bloom, the check Ronald Reagan held over increases in revenue was sufficient to prevent Congress from enacting a tax increase. The compromise required to overcome the mutual checks held by the House Democrats and the Senate Republicans over each other's spending programs led to increased spending on nearly every function of government. Though spending has been held in check since the Democrats took control of both houses of Congress in 1986, especially spending for Republican programs such as defense, Republican threats to veto tax increases will keep budget deficits in the headlines for some time to come.

Appendix

The central thesis of my paper is that parties exert substantial control over the policy-making apparatus in Congress. It follows that divided government will lead to increased budget deficits. In this appendix, I examine the effects of party politics on the level of the deficit for the period from 1929 to 1988.

On Measuring Changes in Spending and Deficits

Before describing my test and results, however, it is important to discuss some measurement issues. The first has to do with choosing baselines in comparing fiscal policy from one year to the next. For example, is it possible to compare the defense budget in the 1950s to the defense budget in the 1980s? There are many pitfalls. Several data transformations are commonly used to facilitate this comparison. Budget figures are deflated to account for price increases; budgets are described as a percent of total spending or of GNP. Each transformation serves a purpose, and each introduces errors, distortions, and biases into the comparison. Using data transformation willy-nilly especially in making comparisons across many years, can introduce more confusion than clarity.

On a more abstract level, without explicating a specific theory of the demand for government goods and services, we can make use of the general

properties of demand functions as an approximation and apply the Slutsky equation. The Slutsky equation states that changes in the demand for a commodity can be decomposed into a substitution, or price, effect and an income effect. Thus, in modeling fiscal policy decisions, most analysts have included GNP as an explanatory variable (Kiewiet and McCubbins 1991; Barro 1979). Dividing your dependent variable—whether it be federal spending or deficit—by an independent variable is highly problematic. To avoid these problems, in the text I compare spending figures over time for federal programs in constant dollars.

The second measurement issue has to do with how to measure the deficit. It may seem odd that this is problematic. The deficit, it seems, should just be the difference between how much the government spends and how much it takes in. Something akin to this is the measure commonly reported by the government as the deficit.

But, this measure of the deficit minimizes the apparent size of the deficit. The current surplus in the Social Security trust fund is used to offset the deficit in spending on other items. This measure, however, ignores the obligations created by the Social Security system. The surplus in the Social Security trust fund is not treated as tax revenue for general obligations; the Social Security Administration purchases Treasury bonds with the surplus. These bonds must be repaid if the Social Security system is to remain solvent. Thus, while the deficit measure commonly used by the federal government treats Social Security contributions as general revenue, in actuality the surplus in contributions just adds to the debt, which in this case the government owes to the Social Security trust fund.

Another measure, which treats the bonds held by the Social Security trust fund—and other federal agencies—as debt instead of revenue, is to examine changes in the national debt from one year to the next. This measure captures all government borrowing from private and public sources and gives a measure of how far government expenditures exceed general revenue. I examine both measures here.

There are still yet more complications, however. Analysts, members of Congress, and the administration often seek to subtract various components of federal spending from deficit measures. These, of course, all have the characteristic that they make the deficit smaller. Indeed, as is true at many savings and loans, the book juggling often yields black ink instead of red.

As long as people are clear about what they are doing and why, book juggling is not necessarily a problem. Subtracting interest payments, or some fraction thereof, from the deficit might be the right measure to test some hypothesis in which you are unconcerned about wealth transfers between individuals in society. The hypotheses examined here are about policy decisions, made by political actors in the federal government. In choosing how to measure and report deficit figures in, for example, Gramm-Rudman-Hollings, interest payments were included. In fact no measure of spending is excluded from the deficit measures or measures of the debt in legislation.

On the Determinants of the Deficit

In the 1980s, the annual increments to the national debt (i.e., the budget deficit) became larger than the entire budget of just a few years earlier. To test my hypothesis that divided government leads to increased budgetary imbalances, I estimate a model of the choice of the deficit, derived from models of spending and revenue developed elsewhere (Kiewiet and McCubbins 1991; McCubbins 1990). The estimation involves income effects (modeled as GNP and unemployment) and substitution effects (various political variables, including dummy variables corresponding to periods of divided government, wars and inflation). The model is represented by the independent variables listed in table 3.A1.

The estimation in table 3.A1 was affected by a few econometric problems, the most serious of which was autocorrelation. In each case I included a set of lagged dependent and independent variables to correct for potential inefficiencies. Other details of the estimation can be found in McCubbins (1990).

In table 3.A1, I estimate a model of deficit determination using three different measures of the deficit. In column 1, I estimate the model using the common definition of the deficit that is reported each year by the federal government (measured in constant collars). This measure is simply the difference

Table 3.A1 On The Determination of the Federal Budget Deficit, 1929–88

	Dependent Variable		
Independent Variable	DEFICIT (1)	ΔDEBT (2)	DEBT/GNP (3)
Constant	28.69	−.06	.01
WWII	−84.39*	.45*	.29*
KOREA	−9.40*	.02	.03*
PRES DEM/CONGRESS REP	2.81	−.08*	.00
PRES REP/CONGRESS DEM	−2.68	.01	.01*
PRES REP/CONGRESS DIV	−26.99*	.09*	.04*
U	.50	.01*	.003*
I	.07	.00	.00
GNP	−.17*		
POSTWAR GNP	.12*		
ΔGNP		.29	
POSTWAR ΔGNP		.13	
DEFICIT_{t-1}	.09		
DEFICIT_{t-2}	−.09		
ΔDEBT_{t-1}		−.02	
DEBT/GNP_{t-1}			.92*
Observations	58	58	58
R^2	.89	.68	.98
Sum of Squared residuals	6,945	.22	.06

Note: For definition of variables, see appendix text. Values in table are estimated coefficients. The coefficient is significant with probability greater than or equal to .95.

each year between federal expenditures and federal revenue from all sources (including, e.g., Social Security). In column 2, I estimated the model using as a measure of the deficit the percentage change from one year to the next in the size of the (constant-dollar) federal debt. This measure has the advantage that it includes purchases of Treasury notes by Social Security (which in fact must be repaid by future taxes) as part of the debt, and, therefore, as part of the deficit. In column 3, at the request of the editors, I measure the deficit as the percent of GNP accounted for by the debt (both in current dollars). This latter measure, of course, necessitated the elimination of GNP as an independent variable.

The variables in table 3.A1 are defined as follows: DEFICIT is the constant-dollar federal budget deficit, calculated from the current-dollar figures reported in *Historical Statistics of the United States* (U.S. Department of Commerce, Census Bureau 1975) and summary tables in *The Budget of the United States Government* (U.S. Executive Office of the President, Office of Management and Budget, various years), and the Implicit Price Deflator for federal government purchases of goods and services as reported in *Survey of Current Business* (U.S. Department of Commerce, Bureau of Economic Analysis, various years); ΔDEBT is the percentage change in the (1972) constant-dollar federal debt,[19] using the Implicit Price Deflator for federal government purchases of goods and services to deflate the current debt figures, as reported in *Historical Statistics* (U.S. Department of Commerce, Census Bureau 1975), *Historical Tables, Budget of the United States Government* (U.S. Executive Office of the President, Office of Management and Budget, 1989) for fiscal 1990, and the *Economic Report of the President* (U.S. Council of Economic Advisers, 1989); DEBT/GNP is the ratio of current debt to current GNP for each year, drawn from *Historical Statistics, Historical Tables, Budget of the United States Government* for fiscal 1990, and the *Economic Report of the President;* WWII is a dummy variable that takes a value of one for the fiscal years of World War II, 1943–45, and zero otherwise; KOREA is a dummy variable that takes on a value of one for the fiscal years 1952 and 1953, and zero otherwise; PRES REP/CONGRESS DEM is a dummy variable that takes on a value of one when the presidency was held by a Republican, and the Congress was controlled by the Democrats (fiscal years 1956–61, 1970–77, and 1988), and zero otherwise; PRES DEM/CONGRESS REP is a dummy variable that takes on a value of one when the president is a Democrat and the Congress is controlled by the Republicans (1948–49), and zero otherwise; PRES REP/CONGRESS DIV is a dummy variable that takes on a value of one when the president is a Republican and control of the two houses of Congress is divided (fiscal years 1932–33 and 1982–87); *U* is the unemployment rate during the fiscal year, as reported by *Survey of Current Business; I* is the rate of inflation during the fiscal year, calculated as a change in the Consumer Price Index, as reported in *Historical Statistics* and *Survey of Current Business;* GNP is the (1972) constant-dollar GNP as reported by *Survey of Current Business;* POSTWAR GNP is a variable

that is equal to GNP for fiscal years after the end of World War II (1946–88), and is zero otherwise; ΔGNP is the percentage change in real GNP;[20] POST-WAR ΔGNP is a variable that equals ΔGNP for 1946–88, and is zero otherwise.

From previous research on spending decisions, I expected increasing unemployment to lead to increased spending. I therefore expect increases in the unemployment rate, all else constant, to lead to increased deficits, and thus, *U* to have a negative coefficient in column 1 (deficits are measure as negative numbers, surpluses as positive numbers) and positive coefficients in columns 2 and 3. I have no prediction about how changes in *I* will affect budget deficits. Wars increase defense and related spending and seem to have a mixed effect, but no net decrease, on domestic spending. I thus expect the wartime variables (WWII and KOREA), all else constant, to yield negative coefficients in column 1 and positive coefficients in columns 2 and 3.[21] If spending has increased faster than revenue as the economy has grown, then the coefficients for the two GNP measures will be negative in column 1 and positive in the other two columns. My model of party politics implies that deficits will not increase (Republican majorities might decrease spending and therewith the deficit) when both houses of Congress are controlled by the same party (the majority party in Congress will control the agenda over spending and taxes), even when the president is of a different party, all else constant. Thus, PRES DEM/CONGRESS REP and PRES REP/CONGRESS DEM should be nonnegative in column 1 and nonpositive in the remaining regressions. It is important to note, however, that divided control of Congress should yield higher deficits: that is, PRES REP/CONGRESS DIV should be negative in column 1 and positive in column 2 and 3.

The results here strongly support the hypothesis that divided control of Congress leads to increased deficits: in all three equations, the coefficient on divided control of Congress was significant and in the predicted direction. We have had two occurrences of divided congressional control in this century, once in the latter half of the Hoover administration and for the first six years of the Reagan administration. If we estimate two dummies, one for each occurrence, both yield significant coefficients in an auxiliary regression. Divided control of government, otherwise, when the effects of divided control of Congress and the tax act of 1981 are held constant, shows either no effect on deficits or confirms that Republican control of Congress produces decreased spending and therewith decreased deficits. The coefficients for unemployment and GNP had the predicted sign, but were not always significant. The war dummies always had the right sign, and the dummy for World War II was always significant.

Notes

1. The measure of the debt used in fig. 3.1 is the gross federal debt. This "is the broadest generally used measure of the Federal debt. It is composed primarily of the public debt (direct borrowing by the Treasury) but also includes agency debt (such as borrowing by the Tennessee Valley Authority or the Postal Service). About three-fourths of the gross debt is held by the public, and about one-fourth is held by Government accounts" (U.S. Department of Commerce, Census Bureau 1975, 1097). This is the measure of the debt most commonly applied by Congress, e.g., in defining debt ceilings. As the debt and deficit have become important political issues, many new and creative measures of each have been prescribed. I address some of the measurement issues involved in measuring the debt and the deficit in the appendix.

2. The 1921 act redelegated the responsibility to compile budget estimates to the president from the Treasury Department, Division of Book Keeping and Warrants. The act specified that the new budget conform to existing law on agency reporting, which included such minutiae as estimates from the Navy Department for printing and stationary; advertising; postage; fuel oil and candles for navy yards; funeral expenses, etc. (see Kiewiet and McCubbins 1989; see also U.S. Congress, House 1921).

3. Sundquist (1981, 12) describes the difference between delegation and abdication as merely semantic, saying that any delegation by Congress is abdication.

4. In granting authority to the president under the 1921 act, Congress required that the estimates submitted conform to existing law. The earlier legislation, e.g., required that estimates be made only for those items authorized by law and that large deviations in estimates from the previous year's appropriations must be explained in detail (for details on the requirements of the 1921 act, see U.S. Congress, House 1921).

5. Why members of Congress have delegated the authority to propose legislation to the president is explored in Kiewiet and McCubbins (1988). They argue that Congress will always delegate to someone the jobs of fact-finding and the drafting of legislation. The choice is between an executive agency or department, which will be heavily influenced by congressional committees or the president, who is independent of such "iron triangles." When the members want to establish a check on their own committees, they must secure information from sources independent of those committees. Only one official in the federal government satisfies the requirements—the president.

6. Continuing resolutions are joint resolutions that may provide temporary funding for affected agencies when Congress fails to complete action on one or more regular appropriations bills before the start of a fiscal year (see Oleszek 1989).

7. Reagan, in each of his budget requests, sought to terminate several dozen programs, ranging from the Jobs Corps, to Amtrak, to the Small Business Administration, to urban mass transit subsidies and rural water and waste disposal grants. Congress voted only to terminate the U.S. Travel and Tourism Agency and to sell Conrail. Indeed, of those programs the president tried to kill in, e.g., 1985, only half even had their budgets reduced.

8. Based on an analysis of a sample of 63 domestic programs. Elsewhere (McCubbins 1990, table A-2), I present results that compare the effects of all postwar presidents on budget requests. The regression reported there shows that Reagan, on average, all else constant, requested far deeper spending cuts than any postwar president. Further, Republicans requested greater cuts in spending, all else equal, than did Democrats, with the exception of Carter. See section 3.2.2 below.

9. Restraint in spending growth contrasts with the budget "cuts" most often referred to in Reagan's fiscal 1982 budget, which were changes in authorizations relative to policies set under Carter (see Muris 1989).

10. These expectations reflect projections of the success of a Republican president facing a Democratic majority in the House and a Republican majority in the Senate.

11. For some critical tests, see Kiewiet and McCubbins (1991) and Cox and McCubbins (1989).

12. The obverse, of course, is that the committee increased spending for over 19 percent of the budget items that came before it, and they granted an amount equal to the president's request in almost 10 percent of the cases. The proportion of times the committee recommended an increase for one of these items over the president's request ranged from zero percent in fiscal year 1947 to over 13 percent in fiscal years 1959–61, to a high of 51 percent in 1984.

13. This, of course, is implicitly Mayhew's (1974) model of agency estimates. If we are to believe that the committee is protecting members from themselves, the estimates the committee deals with must be a reflection of their own desires. If they were not, then the committee would be protecting members from the executive branch, not from themselves.

14. On the unrepresentativeness of many House committees see Cox and McCubbins (1991). On the representativeness of the House Appropriations Committee, see Kiewiet and McCubbins (1991).

15. "Cuts" referred to changes in authorization so that spending was less than it would have been under existing law. For example, "cuts" in Medicare were said to exceed $50 billion for the 1980s. Yet current dollar Medicare outlays actually grew from $32 billion to $94 billion between 1983 and 1988 (Muris 1989). Growth in real terms was only 45 percent.

16. Under this rule, adopted by the House in May 1982, seven budget alternatives were considered (and 68 perfecting amendments), with the House Budget Committee's recommendation being voted last. The rule requires that the last alternative to win a majority is the plan that prevails. This is just one example of the extraordinary rule changes used by the Democrats to control the budget process and the conservative Boll Weevil faction. In 1982 none of the alternatives won a majority. It was used again in 1983, when the Democratic House Budget Committee's plan prevailed.

17. See, generally, Kiewiet and McCubbins (1991). McCubbins (1990, tables A-2, A-3) also presents results that model partisan differences in presidential spending requests and congressional appropriations decisions.

18. Alesina and Tabellini (1989) and Roubini and Sachs (1989) discuss cross-nationally the impact of party policy and divided government on budget deficits.

19. I use an approximation for the percentage change that is calculated as $\Delta\text{DEBT} = \log(\text{DEBT}_t/\text{DEBT}_{t-1})$ where DEBT_t is the federal debt measured in constant dollars in year t. This transformation is referred to as a partial log.

20. I again use a partial log transformation.

21. A dummy variable for the Vietnam war was dropped from the specification, all tests showed that its effect was insignificant.

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Comment

Robert J. Barro

Over the last few years, many costs have been assigned to federal budget deficits. Until now, I have argued that these costs were small. I see now that

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there are also offsetting benefits; after all, if Reagan had not run his deficits I would not have experienced the joy of discussing this paper.

One thesis in McCubbins's paper is that Reagan's record in holding down federal expenditure was unimpressive in comparison with his presidential predecessors. The data presented to support this proposition are hard to understand because of the random switching between real and nominal magnitudes ("current-dollar spending nearly doubled from fiscal year 1981 to 1989") and the failure to make historical comparisons on a consistent basis. ("Constant-dollar spending grew at a faster rate during Reagan's administration [25 percent from 1981 to 1988] than during the Eisenhower [16 percent growth], Nixon [13 percent], Ford [three percent], and Carter [12 percent] administrations." Even after noticing that the figures represent accumulations over administrations of different length, I could not reproduce some of these figures.)

Table 3.C1 shows the annual average growth rates of real federal expenditures during the presidential administrations beginning with Eisenhower's.[1] I use calendar-year figures that correspond as closely as possible to the actual dates in office (e.g., 1961–63 for Kennedy and 1969–74 for Nixon). These numbers (col. 1 of the table) show that Reagan's growth rate, 3.1%, exceeded the growth rates for Eisenhower (1.0%) and Nixon (2.6%), but were below those of the other presidents, including Carter (3.5%) and Ford (4.9%).

The figures based on total federal spending are somewhat misleading because they credit Eisenhower and Nixon with the cutbacks in defense spending associated with the terminations of the wars in Korea and Vietnam, respectively. For nondefense expenditures (col. 2 of table 3.C1), Reagan's growth rate of 2.6% was below that of the others. The growth rate for Eisenhower and Nixon are now 5.8% and 6.7%, respectively, and the second-lowest growth rate is 3.7% for Carter. My inference from these figures is that a substantial slowing of the growth rate of real nondefense federal spending has occurred, although this slowing began during the Carter administration.

Two types of adjustment for inflation arise in analyses of budget deficits and public debt. The first is the division of nominal magnitudes by a price index or by nominal income or product. As mentioned before, this type of adjustment occurs only occasionally in McCubbins's paper. The second adjustment involves the inflation rate, rather than the price level, and concerns the distinction between nominal and real interest rates. The natural definition of the government's real budget deficit is the change over time in the government's net real obligations. If the government holds no assets and if its liabilities are all in the form of nominal bonds, then the real deficit equals the change in the real public debt:

1. Real federal spending is the ratio of nominal spending to the GNP deflator. The results are similar with the deflator for federal purchases. The federal purchases deflator is problematic, however, because it is based mainly on cost measures, especially wage rates. This deflator is also inappropriate for transfer payments.

Table 3.C1 Growth of Real Federal Spending during Presidential Administrations

President and Period in Office	Growth Rate of Real Federal Spending (1)	Growth Rate of Real, Nondefense Federal Spending (2)
Eisenhower, 1953–60	.010	.058
Kennedy, 1961–63	.053	.075
Johnson, 1964–68	.062	.067
Nixon, 1969–74	.026	.067
Ford, 1975–76	.049	.071
Carter, 1977–80	.035	.037
Reagan, 1981–88	.031	.026
Overall, 1953–88	.033	.053

Note: Real federal spending is the ratio of nominal spending (as defined in the national accounts) to the GNP deflator. The figures shown are average annual growth rates from the calendar year preceding each president's first term to his final year in office.

$$(1) \qquad d(B/P)/dt = (1/P) \cdot (dB/dt) - \pi \cdot (B/P),$$

where B is the nominal quantity of government bonds, P is the price level, and $\pi = (1/P)\,(dP/dt)$ is the inflation rate. The first term on the right side of equation (1) is the conventionally defined nominal deficit, dB/dt, divided by the price level. The second term, $\pi \cdot (B/P)$, is the adjustment of the deficit to account for the erosion of the real value of the nominal debt due to inflation. The real budget deficit can also be expressed as the difference between real spending and real revenue. The result corresponds to equation (1) if the term $\pi \cdot (B/P)$ is subtracted from the real value of the government's nominal interest payments, $R \cdot (B/P)$, where R is the nominal interest rate. That is, real interest payments are computed by using the real interest rate, $R - \pi$, rather than the nominal rate, R. From an ex ante standpoint, the adjustment involves the expected inflation rate, π^e, rather than the actual rate, π. That is, if π^e appears instead of π in equation (1), then the relation determines the change in the real debt that would occur in the absence of unanticipated inflation.

The adjustment of budget deficits for inflation is quantitatively important. For example, using numbers that correspond roughly to the present situation, if the expected inflation rate is 5% per year and the stock of debt is $2 trillion, then the adjustment, $\pi^e \cdot B$, reduces the deficit by $100 billion.

In the empirical work (table 3.A1), McCubbins uses the growth rate of the real public debt (his variable ΔDEBT) as one of the dependent variables. This concept corresponds to the real deficit as defined in equation (1) (except that he does not net out the portion of the debt held by government agencies and trust funds or the Federal Reserve). In another specification, he uses the conventional nominal budget deficit divided by a price index as a dependent vari-

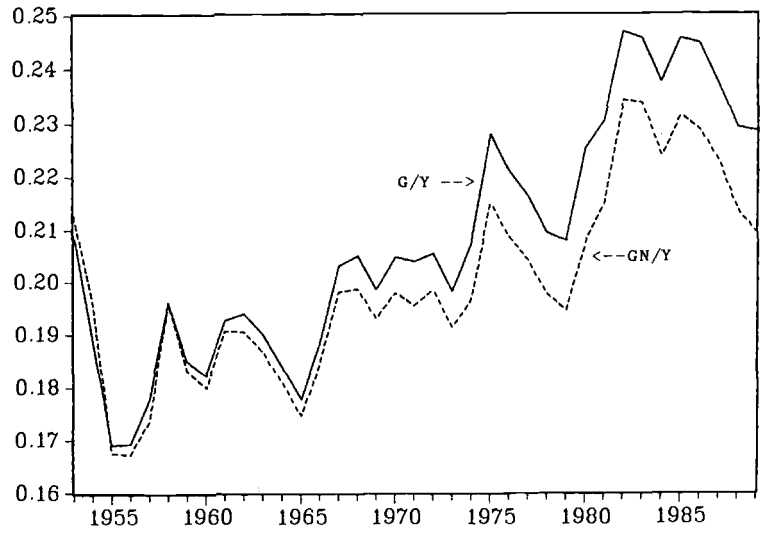

Fig. 3.C1 Federal spending as a ratio to GNP (GN: interest payments adjusted for expected inflation)

able (his variable DEFICIT). This measure does not adjust for inflation; in fact, McCubbins criticizes this type of adjustment. Apparently, he does not realize that his ΔDEBT variable makes the (reasonable) adjustment that he is criticizing.

Figures 3.C1–3.C8 provide measures of the history of U.S. government spending, revenue, budget deficit, and public debt. Figure 3.C1 plots the ratio of total federal spending, as customarily defined, to GNP. The dashed line in the figure shows the ratio when federal spending is revised downward to eliminate the portion of nominal interest payments that corresponds to expected inflation, $\pi^e \cdot (B/P)$. I use the Livingston survey of expected future values of the consumer price index (provided by the Federal Reserve Bank of Philadelphia) to compute π^e.

During the Reagan administration, the (adjusted) spending–GNP ratio rises from .208 in 1980 to .234 in 1982–83 and then falls to .213 in 1988. The increase in the ratio from 1980 to 1982–83 corresponds mainly to increases in defense spending (fig. 3.C2) and interest payments (fig. 3.C3), as well as to the decline in real GNP because of the 1982–83 recession. After 1983, defense spending and adjusted interest payments are roughly constant as ratios to GNP; therefore, the decline in the overall spending ratio involves cuts in other components of spending in relation to GNP. One thing to notice in figure 3.C2 is that the trough in the defense ratio occurs in 1978–79. The rise in the ratio starts with Carter, not Reagan.

Figure 3.C4 plots the ratio of federal revenue to GNP along with the ad-

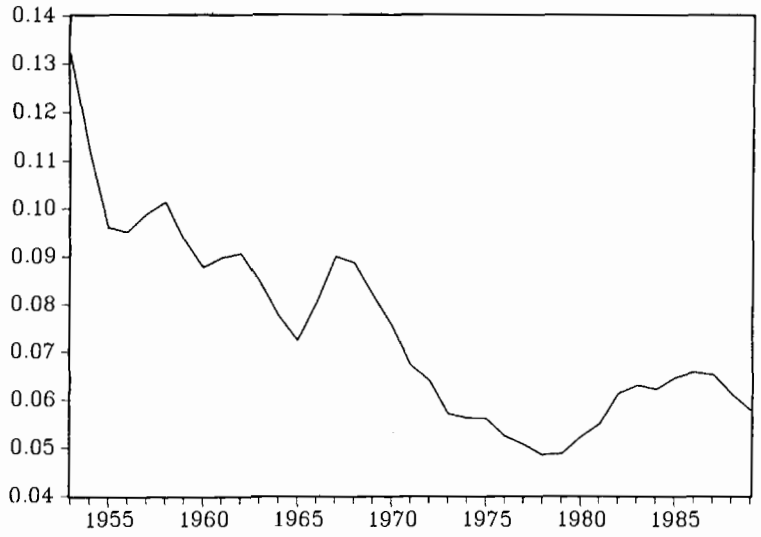

Fig. 3.C2 Defense spending as a ratio to GNP

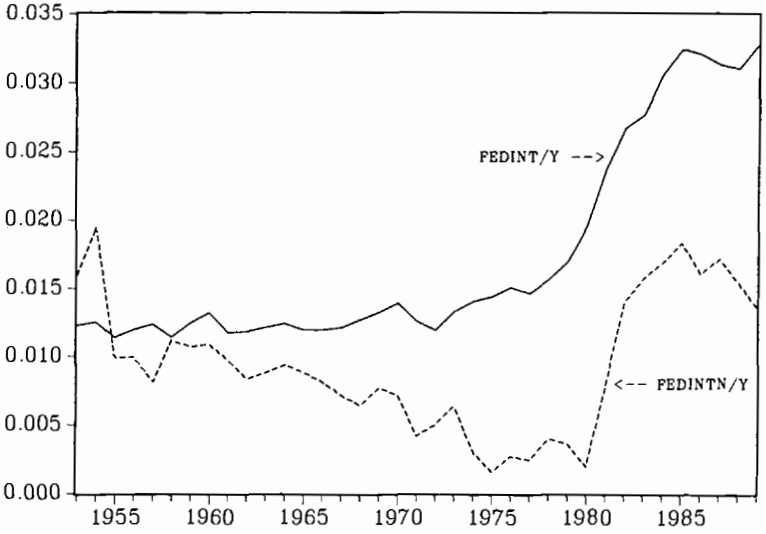

Fig. 3.C3 Federal net interest payments as a ratio to GNP (FEDINTN: adjusted for expected inflation)

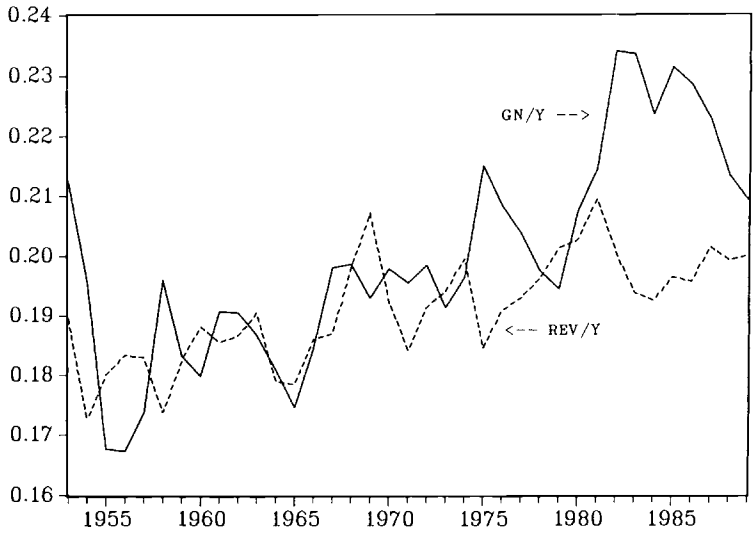

Fig. 3.C4 Federal spending and revenues as ratios to GNP

justed spending ratio. The gap between these two series equals the ratio of the budget deficit (adjusted for expected inflation) to GNP; this ratio is plotted as the dashed line in figure 3.C5. (The solid line shows the ratio for the conventional budget deficit.) The onset of a substantial deficit in 1982 corresponds to an increase in the spending ratio and a decrease in the revenue ratio. This behavior is customary during a recession; for example, figure 3.C4 and 3.C5 reveal similar patterns for 1958 and 1975. From the perspective of the long-term U.S. history, the data for 1982–83 accord with the usual relation between budget deficits and economic contraction.

Starting in 1984, the budget deficit gets out of line with the behavior of the economy. The spending ratio does not decline much until after 1986 and the revenue ratio rises slower than usual during an economic recovery (because of the Reagan tax cuts). The spending and revenue ratios do converge gradually over time, and the ratio of the adjusted deficit to GNP falls from a peak of 4.0% in 1983 to 1.4% in 1988 and 0.9% in 1989.

Figure 3.C6 shows the ratio of privately held U.S. public debt to GNP. (The debt figures are at the end of the calendar year since 1916 and at midyear before 1916.) This measure of the debt nets out the amounts held by federal agencies and trust funds and the Federal Reserve. Note that the debt ratio rose from 21.5% in 1979 to 38.6% in 1987. Then, with the cutback in the deficit-GNP ratio, the debt ratio fell to 38.0% in 1989. In particular, the reduced deficits meant that the debt-GNP ratio was no longer rising after 1987.

Figures 3.C7 and 3.C8 provide information for the total government sector. The overall story is similar to that for the federal government. Because of the

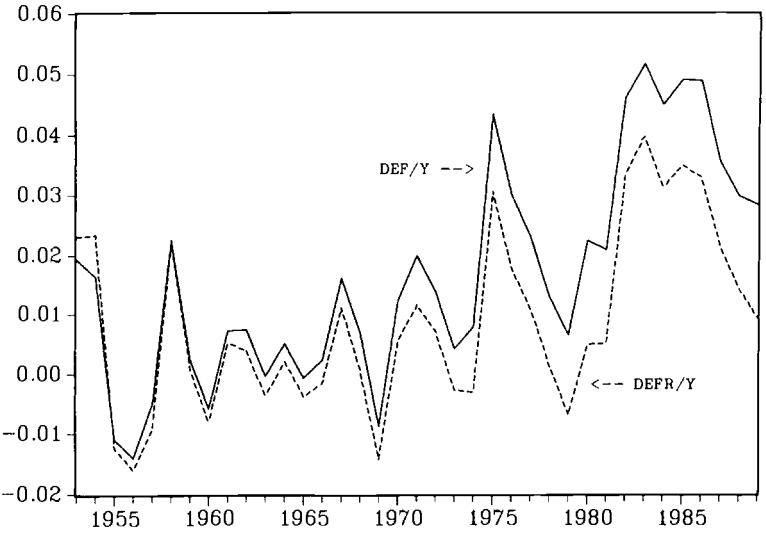

Fig. 3.C5 Federal budget deficit as a ratio to GNP (DEFR: adjusted for expected inflation)

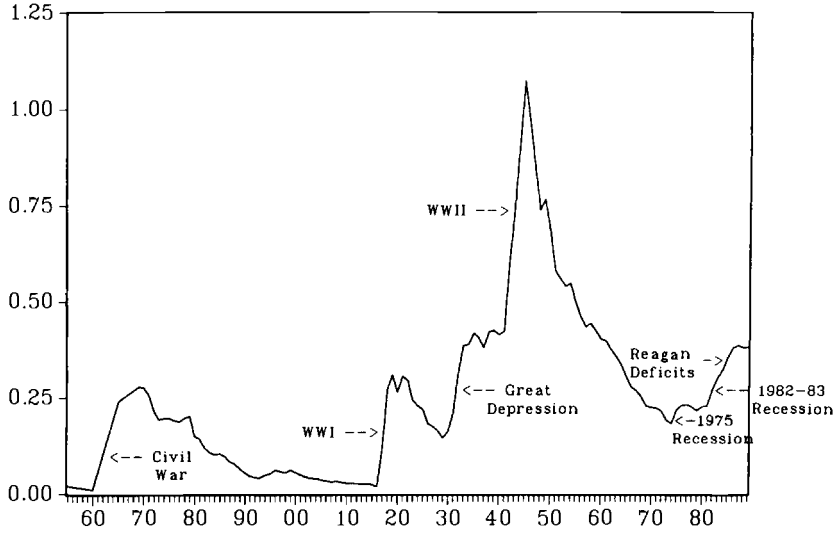

Fig. 3.C6 Ratio of privately-held public debt to GNP, 1855–1989

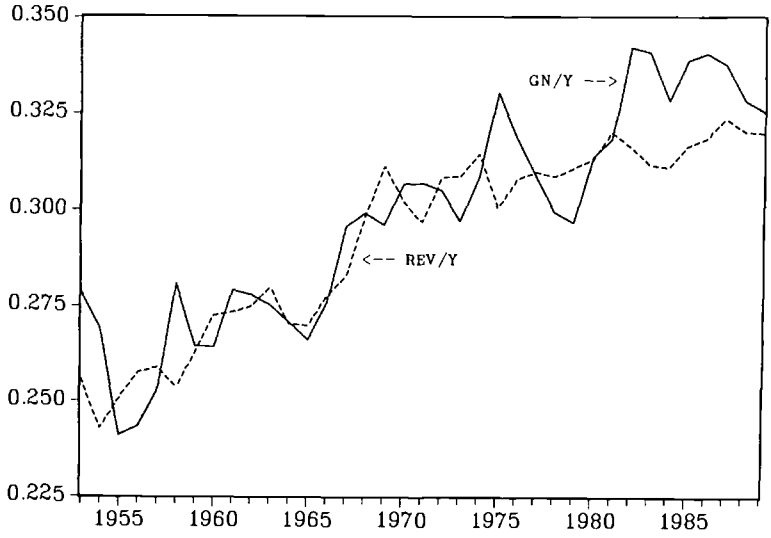

Fig. 3.C7 Total government spending and revenues as ratios to GNP

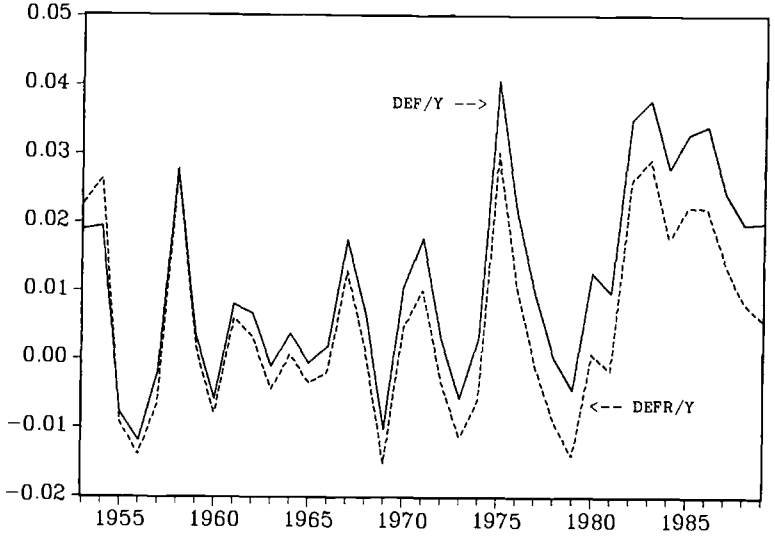

Fig. 3.C8 Total government budget deficit as a ratio to GNP (DEFR: adjusted for expected inflation)

state and local surplus, however, the ratio of the adjusted budget deficit to GNP for total government peaks at only 2.9% in 1983 and then declines to 0.6% in 1989.

McCubbins sketches a game-theoretic political model of government spending. Republicans like high defense spending and low nondefense spending, whereas Democrats have the opposite preferences. (I do not see how this fits with Carter's initiation of the defense buildup or with the Democrats being in power when the United States entered the Vietnam War, the Korean War, World War II, and World War I.) McCubbins also assumes that both political parties prefer high levels of each category of spending to low levels of each. Therefore, in a situation of divided political power, the equilibrium entails high levels of both types of spending.

One point about the model is that any desired result can be obtained by making the appropriate assumptions about preferences. For example, it would be easy to generate the conclusion that divided government leads to a low level of government spending, rather than a high level. This observation is important because the theoretical "predictions" are tailored (as discussed below) to fit a single episode, the Reagan budget deficits. A second point is that the theory pertains to the size of government, not to budget deficits, per se.

To generate a theory of budget deficits, McCubbins sketches an analogous game-theoretic model of tax revenues. I could not find an intertemporal budget constraint in this analysis; that is, preferences about expenditures seem to be independent of those for taxes, and preferences for taxes seem to be independent of those for expenditures. If politicians perceive no intertemporal budget constraint, then tax revenues would presumably be set to zero. If they take account of the (eventual) link between spending and taxes, then preferences about expenditures cannot be separated from those about taxes. One could introduce a political game that concerns the composition of taxation in terms of degree of graduation, direct versus indirect taxes, and so on. But that analysis need not interact very much with the determination of total tax revenues, which is the aggregate that matters for the budget deficit. The analysis could also consider conflicts between older and younger generations, which might matter for budget deficits (and Social Security). Interesting political models of this type include Cukierman and Meltzer (1989) and Tabellini and Alesina (1990). As it stands, however, the McCubbins paper does not consider intergenerational conflicts or other forces that could provide a theory of budget deficits.

In the empirical analysis, McCubbins includes some variables—wartime, business-cycle measures, and inflation—that do not appear in his political analysis but that enter naturally into a familiar theory of budget deficits that relies on optimal public finance. This approach determines the timing of taxes, given the size and time pattern of public expenditures and the composition of taxes by type. (These variables could be determined from a model that includes political interactions.) Optimal fiscal policy features tax smooth-

ing (Pigou 1928, chap. 6; Barro 1979, 1986). This smoothing implies that temporary government expenditures, as in wartime, are financed primarily by debt issue to avoid temporarily large increases in tax rates. Similarly, shortfalls in income during recessions call for debt finance; otherwise, tax rates would be temporarily high during economic contractions. The model implies also that an increase in the expected-inflation portion of the government's nominal interest payments, $\pi^e \cdot B$, raises nominal debt issue, dB/dt, one to one. Equivalently, the conventional deficit can be adjusted for expected inflation as described before.

I showed (Barro 1986) that the tax-smoothing model provides a good explanation for the determination of U.S. budget deficits from 1916 to 1983. Three variables—temporary federal spending associated especially with wars, temporary movements of income and hence tax receipts due to business fluctuations, and the expected inflation term, $\pi^e \cdot B$—account for the main variations in the federal deficit. The model also explains the bulk of U.K. budget deficits from 1706 to 1918 (Barro 1987). In this case, the major influence is temporary government spending during wars.

In terms of the Reagan administration, the tax-smoothing model fits the observed behavior of federal budget deficits through 1983. That is, the recession for 1982–83 is large enough to explain the deficits, which were about 5% of GNP (or 4% of GNP after the adjustment of interest payments for the effect of expected inflation). The deficits recorded from 1984 onward are, however, significant outliers. In particular, the variables used in the 1916–83 relations and the coefficients estimated from this relation lead to a significant underprediction of the budget deficits for 1984–88. The residual from these forecasts peak at about 2.5% of GNP in 1986, but falls to about 1.5% of GNP in 1988 (and about 1% of GNP in 1989). Given these substantial errors that persist over several years, it is reasonable to think about additional factors as determinants of budget deficits. It is, however, not very promising to advance political arguments that would have been operating throughout the 1916–83 period but were unnecessary to explain the behavior of deficits over those years.

Although McCubbins's empirical work on budget deficits from 1929 to 1988 (table 3.A1) includes variables that arise in the tax-smoothing model, his specification does not accord with that model. In the theory, temporary government spending, as in wartime, has roughly a one-to-one effect on the deficit. McCubbins enters dummy variables for World War II and the Korean War, but does not attempt to measure the size of temporary federal spending either during these wars or at other times.

In the tax-smoothing theory (and in standard computations of a full-employment budget deficit), the effect of recession involves the shortfall of tax receipts associated with the shortfall of income. McCubbins includes the unemployment rate and the level of real GNP in a linear form. The unemployment rate and the growth rate of real GNP provide information about the percentage shortfall in real GNP, but the effect on tax receipts involves an inter-

action with the share of tax receipts in GNP. For example, an unemployment rate of 25% in 1991 would lead to a much larger deficit as a fraction of GNP than it did in 1933 when the share of government in GNP was much smaller. By forcing a linear form over a sample (1929–88) in which the share of government changed greatly, McCubbins fails to account satisfactorily for the cyclical behavior of the budget deficit.

McCubbins also does not measure properly the effects of inflation, although this problem would be minor in the equation that uses the growth rate of the real debt (ΔDEBT). This specification, however, does not adjust the gross public debt for the amounts held by federal agencies and trust funds or the Federal Reserve. Thus, the measured deficit would rise, for example, if the government cut income taxes and raised Social Security taxes by an equal amount (so that the Social Security trust fund absorbed more of the Treasury's debt). Since the Social Security tax is a form of federal tax and Social Security benefits are a form of federal expenditures, it is natural to consolidate Social Security with the rest of the government in computations of total federal revenue, spending, budget deficit, and public debt.

Recently—that is, since Social Security began to run a substantial surplus—some people have argued that the federal deficit should be calculated independently of Social Security. One reason to think separately about Social Security is that, because of demographic trends, the ratio of benefits to GNP is projected to grow over time. If other components of federal spending are expected to maintain a constant ratio to GNP, then the tax-smoothing model prescribes a current budget surplus. That is, current tax rates are set to match the higher anticipated ratio of overall federal spending (including Social Security benefits) to GNP. Of course, this projection for Social Security may be wrong. Future spending depends on changes in benefit formulas, immigration may upset the demographic forecasts, and so on.

The general point, which is not special to Social Security, is that prospects for future government spending influence today's optimal fiscal policy. If the ratio to GNP of some component of spending, such as defense, is projected to rise or fall over time, and if the rest of spending is expected to stay constant in relation to GNP, then tax-smoothing calls, respectively, for a current budget surplus or deficit. For example, if we (or, more pertinently, Ronald Reagan) believed in the mid-1980s that future changes in Eastern Europe would generate a peace dividend, then the appropriate response would have been to run a budget deficit.[2] This mechanism is one way to reconcile the "excessive" budget deficits of 1984–88 with the tax-smoothing model. If Reagan thought that the ratios of federal spending to GNP in the mid 1980s were about two percentage points higher than "normal," then the deficits were not excessive.

2. I abstract here from possible adverse effects from the Persian Gulf War. This event was unanticipated at the time of this conference. I assume, perhaps unreasonably, that Reagan also did not anticipate this war in the mid-1980s.

McCubbins argues that his political theory is strongly supported by the significantly positive effect on deficits of his variable, PRES REP/CONGRESS DIV (his table 3.A1). This variable is, in fact, a dummy for the fiscal years 1932–33 and 1982–87. In 1932–33, which is the trough of the Great Depression, budget deficits were large (4% of GNP in 1932 and 6% in 1933). A proper treatment of cyclical variables explains these deficits without any reliance on political variables (Barro 1986, table 10.4). As mentioned before, the appropriate cyclical variables also fit the budget deficits for 1982–83. Since McCubbins does not account adequately for cyclical factors, his estimation gives too much credit to the dummy variable that takes on the value "1" in 1932–33 and 1982–83.

The rest of the period covered by the dummy variable is 1984–87; as already mentioned, the Reagan budget deficits in this period are larger than the historical relation would predict (unless one adjusts the measure of temporary federal spending as discussed before for the projected peace dividend). In any event, the high budget deficits for 1984–87 add to the explanatory power of the dummy variable. But there is no trick to explaining the Reagan deficits by invoking a dummy variable for the relevant period. In fact, after the event, there are many variables that one could select that happen to be unusually high in 1984–87. (Unfortunately, the anticipated peace dividend falls into this category; therefore, I am reluctant to stress this argument.) The serious challenge is to find a force that accords with a complete theory and that also can be checked out by more than a single episode. Perhaps after McCubbins completes his political theory he will apply it to the experiences of many countries.

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