

Statement of
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before the
Subcommittee on Defense
Committee on Appropriations
United States Senate

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NOTICE

This statement is not available for public release until it is delivered at 10:00 a.m. (EDT), Thursday, August 7, 1986.

Mr. Chairman and Members of the Subcommittee, I am pleased to have this opportunity to discuss Department of Defense expenditure rates. My statement this morning will cover three topics-- a review of our past and current estimates for defense outlays in 1987, a discussion of outlays to date, and a discussion of the practicality of "managing" outlays so that they hit a given target.

REVIEW OF 1987 OUTLAY ESTIMATES

Last February, for function 050 (that is, national defense) the Administration requested budget authority of \$320 billion for fiscal year 1987 and estimated that this amount would result in outlays of \$282 billion. In contrast, the Congressional Budget Office (CBO) estimated that appropriations of this magnitude would result in outlays of \$297 billion, or \$14.5 billion higher than the amount estimated by the Administration. Our estimating differences with the Administration were concentrated in three appropriation categories: operation and maintenance (O&M); procurement; and research, development, test, and evaluation (RDT&E). Incidentally, CBO and the Administration have never had an estimating difference of that magnitude before.

The estimating difference occurred because CBO and the Administration had different assumptions about the relevance of historical spending patterns. CBO assumed that history would continue to be a reliable guide for predicting future outlays. The Administration assumed that history would not be a reliable guide because of management initiatives and other factors that would tend to reduce outlays. In fact, as we showed in our Analysis of the President's Budgetary Proposals, published last February, we had little disagreement with the Administration as to what the historical rates were--only if they were still relevant.

In the Office of Management and Budget mid-session review of the 1987 budget, which was released yesterday, the Administration has reduced its 1987 appropriation request for national defense programs to \$299 billion. Total estimated outlays remain at \$282 billion, which implies an upward adjustment of at least \$9 billion in the Administration's outlay estimates for 1987. Based on the distribution of budget authority by appropriation account, CBO estimates that the \$299 billion in new budget authority would produce total outlays of about \$289 billion, or \$6.7 billion more than estimated by the Administration. Table 1 summarizes the estimating differences in February and August; it shows that the main areas of disagreement continue to be O&M, procurement, and RDT&E.

OUTLAYS TO DATE FOR 1986

Outlays for the first nine months of 1986 are 9.5 percent greater than a year ago. If that rate of growth continues for the rest of the year, outlays will total about \$277 billion compared with our February estimate of \$270 billion and the Administration's \$266 billion. Table 2 shows that most of the unexpected growth is occurring in O&M, RDT&E, and the revolving funds.

TABLE 1: COMPARISON OF DEFENSE OUTLAY ESTIMATES
FOR FISCAL YEAR 1987 (In billions of dollars)

Category	Outlays Based on Budget Authority of \$320 Billion (as of February 1986)			Outlays Based on Budget Authority of \$299 Billion (as of August 1986)		
	CBO	Admin.	Diff.	CBO	Admin.	Diff.
Military Personnel	73.4	73.6	-0.2	72.9	73.1	-0.2
O&M	81.6	80.9	0.7	76.7	75.1	1.6
Procurement	86.3	76.7	9.6	85.1	81.7	3.4
RDT&E	35.7	31.6	4.1	35.4	33.0	2.4
Military Construction	5.2	4.6	0.6	5.1	5.0	0.1
Family Housing	3.0	2.5	0.5	3.0	2.7	0.2
Revolving Funds	1.2	1.8	-0.6	1.0	1.6	-0.7
Other:DoD	2.3	2.6	-0.3	2.1	2.1	0.0
Subtotal:DoD	288.7	274.3	14.5	281.1	274.4	6.7
DOE	7.7	7.7	---	7.4	7.5	-0.1
Other Defense	0.3	0.3	---	0.3	0.3	0.0
Total:050	296.7	282.2	14.5	288.8	282.2	6.7

SOURCES: Congressional Budget Office and Office of Management and Budget.

With such a high rate of growth this late in the year, we raised our 1986 estimate by \$3.8 billion to \$273.3 billion. We expect the momentum of

TABLE 2: COMPARISON OF DEFENSE OUTLAY PROJECTIONS FOR FISCAL YEAR 1986 (In billions of dollars)

Category	Feb. 1986 Estimates			Aug. 1986 Estimates			Actual Growth thru June (Percent)	Extrapolation
	CBO	OMB	Diff.	CBO	OMB	Diff.		
Military Personnel	71.7	71.4	0.3	71.2	71.4	-0.3	6.8	72.5
O&M	74.1	74.1	*	76.5	74.1	2.4	5.3	76.2
Procurement	78.1	75.7	2.4	77.7	79.1	-1.4	11.4	78.4
RDT&E	30.3	28.7	1.6	31.8	30.0	1.8	18.6	32.2
Military Construction	5.0	4.5	0.5	5.0	4.8	0.3	17.3	5.0
Family Housing	2.6	2.4	0.2	2.6	2.6	0.1	9.6	2.9
Revolving Funds and Other-DoD	0.3	1.6	-1.4	0.7	1.4	-0.7	54.7	1.2
Subtotal	262.1	258.4	3.6	265.5	263.5	2.1	9.7	269.1 ^{a/}
DOE & Other	7.5	7.5	*	7.8	7.9	-0.2	6.2	7.6
Total 050	269.5	265.8	3.7	273.3	271.4	1.9	9.5	276.7

SOURCES: Congressional Budget Office and Office of Management and Budget.

- a. This amount is not the sum of the preceding categories; rather, it is an extrapolation of aggregate growth based on a 9.7 percent aggregate growth rate over total 1985 outlays of \$245.3 billion. The sum of the extrapolations of the first seven categories is \$268.4 billion.

this spending surge to carry into 1987, and we raised our estimate for that year by \$1.5 billion. Some data suggest that we should have raised our estimates more, but actual outlays also could be lower. Outlay estimating is an imprecise process that uses both historical data and analytic judgements. CBO's estimating goal is to find the number with equal probability of being too high as too low. The range of estimating error is likely to be around 1 percent to 2 percent--that is, around \$3 billion to \$5 billion.

THE DIFFICULTIES IN MANAGING OUTLAYS

Occasionally, there is a suggestion that the government in general and the Defense Department, in particular, should manage its program so that outlays hit some specific target. In February, the Administration argued that it could manage its outlays to achieve its defense outlay estimates through various policy changes and other measures. CBO believed that these factors could affect outlays by only a small amount, if at all. What impact they might have should be temporary and would not affect outlays beyond a few months. We discussed this at some length in our analysis of the President's budget for 1987.^{1/}

1. See Congressional Budget Office, An Analysis of the President's Budgetary Proposals for Fiscal Year 1987 (February 1986), Chapter III.

We believe that managing outlays would be difficult because of the decentralized nature of the defense finance and accounting system. Managing outlays would require fundamental changes in the way thousands of programs are pursued and in the business practices of equally numerous finance officers. To make a reasonable attempt to meet an exact outlay target would require an intricate set of controls that would take a long time to develop. Certainly, one should not expect such a system to yield much more than marginal savings during 1987.

Even over the long term, a number of considerations would affect the desirability or practicality of moving toward outlay management. One such difficulty stems from the fact that about a third of all defense outlays result from prior-year appropriations and contract commitments. Controlling these outlays would be difficult because, as contractors make deliveries, they expect to be paid. In those instances where delays are legally possible, they may induce contractors to raise future contract bids, thereby raising the cost of procurement.

One way to manage outlays, however, is to slow obligations. Yet, this avenue has certain problems that stem from conflicting objectives of

keeping outlays down and, at the same time, using appropriations to serve their purpose of improving national defense. Further, the ability to slow obligations is constrained by time limits on the availability of funding. After these limits are reached, unobligated funds lapse or are no longer available. To the extent that obligations were slowed, inefficiencies and cost growth might result, making the slowdown undesirable even if it were possible. Obviously, these problems would be less severe the smaller the attempted reduction in outlays.

A recent study by the RAND Corporation for the Air Force made many of these same points and others.^{2/} The study concluded that moving toward outlay controls would require immediate attention to:

1. Bringing outlay planning into the defense planning, programming, and budgeting system so that plans reflect long-term outlay concerns (to include better forecasting and tracking of outlays);
2. Identifying within the year adjustment measures and their effects so that fine tuning of outlays could be based on priorities; and

2. Massey, H.G. et al, Air Force Outlay Control: Management Implications and Options, (Santa Monica, California: RAND Corporation, 1985).

3. Establishing a central authority for implementing adjustment measures within the year.

Perhaps the most important observation of the RAND study was that:

"Financial management under outlay budgeting appears to require greater budgetary discretion for the Executive branch than is likely to be acceptable to the Congress."

In particular, the study found that authority and flexibility were critical to effective outlay control and that to provide them would require giving the Executive branch greater reprogramming and impoundment authority as well as reducing full funding of procurement.

CONCLUSION

In conclusion, Mr. Chairman, while outlay estimating is difficult and inexact, CBO estimates are holding up very well. We have had to make only small adjustments to our estimates as outlays for 1986 have come in very strongly.