

What does it mean for a government program to be off-budget?

Off-Budget versus On-Budget Accounting

The budget brings together the spending and receipts of virtually all federal activities, from paying doctors who treat Medicare patients to financing the Environmental Protection Agency to collecting income taxes to selling oil leases on federal land. In two cases, however, Congress has separated programs from the rest of the budget. The Postal Service Fund and the disability and retirement trust funds in Social Security are formally designated “off-budget,” even though their spending and revenues are included in the unified budget.

Lawmakers created this special accounting to try to wall off these programs. For the postal service, the intent was to free the agency to pursue more efficient practices than the conventional budget process allows. But that has not helped the postal service avoid financial difficulties.

With Social Security, the intent was to protect any surpluses from being diverted into other programs. The two Social Security trust funds have accumulated large surpluses since 1983. Those will eventually be drawn down to pay benefits. Advocates therefore argued that those surpluses should be separated from budgeting for the rest of government. Congress hoped that this separation would induce greater fiscal discipline in the rest of the government.

RESULTS

This accounting has had mixed results. Congressional budget rules prevent spending reductions or revenue increases in Social Security from being explicitly used to pay for spending increases or tax cuts elsewhere. In that sense, off-budget accounting has protected the program. But high-level budget discussions focus on the unified budget deficit and thus ignore the off-budget versus on-budget distinction. As a result, Social Security surpluses have effectively helped finance deficits elsewhere in the government. Just how much is unclear, but in the almost three decades that Social Security has been off-budget, the rest of government has run a surplus in only two years (1999 and 2000).

In any case, these arguments have less relevance today. Annual Social Security expenditures have exceeded noninterest income since 2010. The combined trust funds still run surpluses through 2019 because of interest payments from the Treasury, but these payments are simply transfers from one government office to another and therefore do not affect the unified deficit. Trust fund balances may begin to decline in 2020.

The Federal Reserve System

The Federal Reserve System (the Fed) is part of the federal government but is explicitly excluded from the budget to shield monetary policymakers from political pressure. Other developed nations do the same. The Fed thus sets its own spending and finances itself from earnings on lending to banks and its financial assets. The Fed remits its profits to the Treasury each year, which the budget records as receipts, but the agency otherwise operates outside the budget.

OTHER ACTIVITIES OUTSIDE THE BUDGET

Some federal activities are outside the budget because the government plays a limited role in what is otherwise a private activity. The government manages various funds whose assets belong to Indian tribes, federal employees, copyright holders, and other private individuals. Spending from and receipts to those funds are generally not included in the budget.

Government-sponsored enterprises, such as the Federal Home Loan Banks, also fall outside the budget because they are privately owned and their debt does not bear the full faith and credit of the US government. However, most observers assume their close ties to the government would lead to a bailout if they got into financial trouble.

That assumption proved accurate for Fannie Mae and Freddie Mac, the giant mortgage finance enterprises. During the 2008 financial crisis, they received substantial financial assistance and were put into federal conservatorship. This has led to a dispute regarding their status. The Office of Management and Budget believes Fannie Mae and Freddie Mac are still sufficiently private to fall outside the budget. The Congressional Budget Office believes federal control is now so strong that the two entities are effectively federal agencies and their spending and receipts should be in the budget.

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