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1976 Budget
Session With The
President

12/6/74

1976 Budget
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President
12/6/74



THE WHITE HOUSE

WASHINGTON

December 5, 1974

MEETING WITH ROY L. ASH
Friday, December 6, 1974
2:00 p.m. (60 minutes)
Oval Office

From: Roy L. Ash



I. PURPOSE

To make final FY 76 budget decisions for the Departments of Commerce and Treasury, for the Small Business Administration, and for several smaller agencies.

II. BACKGROUND, PARTICIPANTS AND PRESS PLAN

- A. Background: The FY 76 budget submissions of the Departments of Commerce and Treasury, the SBA and several smaller agencies have been reviewed by OMB and members of the White House staff. The results of these reviews have been discussed with the affected departments and agencies. This meeting will focus on the issues raised during the budget review process that require Presidential consideration and determinations.
- B. Participants: Roy L. Ash, Paul O'Neill, Wally Scott, and Dale McOmber
- C. Press Plan: David Kennerly photo

III. TALKING POINTS

- A. Wally Scott, will you describe the first issue we shall be considering for the Department of Commerce?
- B. Wally Scott, would you begin our discussion of the issues raised in the FY 76 budget for the Small Business Administration?
- C. Wally Scott, what is the first issue we should discuss for the Treasury Department?

D. Wally Scott, would you describe the issues raised by the budgets of the smaller agencies for us?



Commerce

THE WHITE HOUSE

WASHINGTON



MEMORANDUM FOR: THE PRESIDENT

FROM: Roy L. Ash

SUBJECT: 1976 Budget decisions: Department of Commerce

The agency request and my recommendations with respect to 1976 budget amounts for the Department of Commerce are presented in the tabulation attached (Tab A). A summary of the principal budget decisions reflected in my recommendation is provided as background information (Tab B).

Three key issues have been identified for your consideration (detail at Tab C).

I. Ship construction program.

Commerce proposes to continue to encourage expansion of U.S. ship construction activities through a subsidy program of \$286 million in 1975 and \$285 million in 1976.

OMB proposes to restrain this subsidy program by holding it to \$256 million in 1975 and \$198 million in 1976. This will help reduce Commerce competition with Navy for scarce shipbuilding resources, and reduce inflationary pressures in the industry.

Decision: Approve agency recommendation _____
Approve OMB recommendation _____
See me _____

II. Export promotion services.

A. Full cost recovery fees.

OMB recommends that no funds be appropriated for subsidizing Commerce services to experienced exporters. These firms recognize the benefits of exporting, and should pay the full cost of Commerce services if those services are considered useful by the exporters.

Commerce believes that it should continue to subsidize its services for all exporters, in order to promote more U.S. exports.

Decision: Approve agency recommendation _____
 Approve OMB recommendation _____
 See me _____

B. Trade centers in developed markets.

Commerce proposes to continue funding for seven trade centers in the developed export markets of Europe, Japan and Australia, because it believes the centers are useful means of promoting exports, and closing them may have an adverse impact on the international trade environment.

OMB recommends closing these seven centers because they are not needed to promote exports to these well developed markets and they are more costly than alternative export promotion mechanisms.

Decision: Approve agency recommendation _____
 Approve OMB recommendation _____
 See me _____

III. Tourism program.

Commerce proposes that legislation be requested to extend the authorization for the U.S. Travel Service program indefinitely, to promote foreign travel to the U.S.

OMB recommends that the program be continued only through the end of calendar year 1976 (until the end of the Bicentennial year). We recommend that the program be terminated after the Bicentennial because it is not needed to meet any U.S. economic or foreign relations objectives.

Decision: Approve agency recommendation _____
 Approve OMB recommendation _____
 See me _____

Attachments



THE WHITE HOUSE

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 See me _____

Attachments

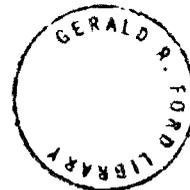


Department of Commerce

1976 Budget

Summary Data

	(\$ in Millions)		Employment	
	<u>Budget Authority</u>	<u>Outlays</u>	<u>Full-time Permanent</u>	<u>Total</u>
1974 actual	1,513	1,455	28,592	35,182
1975 January budget	1,727	1,712	29,138	35,698
enacted	1,647	1,664	xxx	xxx
outlay reduction	-6	-25	xxx	xxx
supplemental recommended	+6	0	xxx	xxx
OMB recommendation	1,647	1,639	28,645	36,073
1976 planning ceiling	1,665	1,780	xxx	xxx
agency recommendation	1,766	1,739	28,840	35,743
OMB recommendation	1,671	1,718	28,612	35,515
Transition period				
agency recommendation	462	440	28,840	35,743
OMB recommendation	435	430	28,612	35,515
1977 OMB estimate	1,766	1,860	28,495	35,382



Tab B

1976 Budget

Department of Commerce

Background Information

The OMB recommendations for Commerce provide a \$24 million increase in budget authority. With unused funds which will be available from 1975, this will provide \$1,761 million in total funds available in 1976, an increase of \$105 million from 1975. Commerce initially requested an increase of \$235 million. The estimate of outlays for 1976 is \$1,718 million, an increase of \$79 million from 1975, and \$47 million less than initially requested by Commerce.

We estimate that continuation of these program recommendations into 1977 will result in 1977 outlays of \$1,860 million, compared to the Commerce estimate of \$2,030 million for its initial request.

OMB and Commerce have now reached agreement on budget and program recommendations for about 85% of the recommended budget. The major program areas where we have reached agreement are as follows:

1. National Oceanic and Atmospheric Administration. The agency requested an increase of \$83 million. We have agreed on a total program level of \$514 million, an increase of \$57 million. Emphasis will be given to improving the productivity of the weather services, and to preparing for increased exploitation of ocean living and mineral resources. Increases are provided to help States plan for accelerated oil and gas exploitation on the continental shelf. The Department agreed that it should not undertake programs to try to "revitalize" the U.S. fishing industry through subsidies or protection from competition.
2. Economic Adjustment Assistance. \$356 million is included for assisting communities or regions to adjust to serious, structural economic problems. This is an increase of \$42 million from 1975, and \$23 million less than requested. The increase includes funds for assisting communities impacted by imports, Defense base closings, and natural disasters, as well as for those depressed rural and urban areas which are suffering from long-term economic declines. These programs are being restructured to increase the decision making role of States and local governments. No funding is included to help respond to temporary unemployment problems; these programs are not effective means of creating quick, short-term employment.
3. Science and Technology. \$156 million is included for the programs of the National Bureau of Standards, the Patent Office and the new Fire Administration. This is an increase of \$14 million over 1975, but is \$8 million less than initially requested by Commerce. This will permit continuation of efforts to improve productivity through technology, acceleration of patent approvals, and initiation of the new program to improve fire prevention capabilities of States and communities.

4. Social and Economic Statistics. The recommended budget includes \$80 million for data collection and analysis by the Bureau of Census and the Bureau of Economic Analysis. The increase of \$11 million over 1975 is primarily to improve the quality and timeliness of data gathered on economic conditions, and to begin work on the periodic censuses of Economics, Agriculture, Governments and the 1980 Decennial Census.
5. Ship Operating Subsidies. The recommendation includes \$287 million in outlays for subsidies for operation of U.S. ships in international trade. The subsidy represents the higher costs of U.S. ship operations compared to foreign competitors. The 1976 expenditures are \$44 million higher than 1975, and result entirely from past contractual commitments to ship operators.

The areas of disagreement with the Department are discussed under Tab C.



Tab C

Issue Paper
Department of Commerce/MARAD
1976 Budget
Issue #1: Ship Construction Program



Statement of Issue

What actions can the Federal Government take in the short term to reduce the inflationary demand on the U.S. ship construction industry and reduce the potential for competition between Navy and MARAD for scarce yard resources?

Background

In developing the President's Budget last year it was decided that the MARAD program should not be focused on attaining certain arbitrary trade penetration goals through subsidizing the construction and operation of ships. Its focus should rather be on improving the international competitive position of the shipping industries, consistent with defined national security requirements for the industries, in order to minimize the continuing need for Federal support.

In response to OMB guidance, MARAD conducted a review of national security requirements for the program, which concluded that the current construction differential subsidy (CDS) program level does not need to be maintained to provide for national security needs, and that any available CDS funding could be focused on improving the international competitive position of the industry rather than used to build certain ships or support certain yards for national security purposes.

During this past year the shipbuilding industry has been affected by several developments. First, yards are now approaching their actual capacity to produce ships. Second, labor and material shortages are developing, and ship prices are projected to increase as much as 40% during the next year. Third, there is concern that MARAD is now competing with the Navy for scarce shipbuilding resources; the Navy has recently advocated the initiation of ship construction in Navy-owned yards, because of the lack of interest in their contracts by private yards.

Alternatives

- #1. Continue the Commerce approach of funding a variety of ship types in a number of yards to encourage the continued expansion of the ship construction industry. (Agency request)
- #2. Reduce MARAD ship construction funding to stabilize demand on shipyards at about the current level. (OMB recommendation)

Analysis

Program Level/Outlays (\$ Millions)	1974		1975		1976		July 1-Sept. 30, 1976		1977	
	PL	O	PL	O	PL	O	PL	O	PL	O
Construction Subsidy Funding:										
Agency request	293	200	286	256	285	313	76	83	378	340
OMB recommendation	293	200	256	256	198	303	50	77	170	299

The Department of Commerce recommends the continuation of the current approach to the subsidy program, which would result in continued rising employment in the ship construction industry. Employment on new ship construction in U.S. shipyards has grown from 44,000 in 1970 to 66,000 today. Commerce projections indicate that employment would rise to 78,000 by 1978 if the MARAD programs continue as requested.

OMB recommends reducing CDS funding by \$30 million in 1975, by \$87 million in 1976 (to \$198M rather than \$285M) and to \$170M in 1977. This should have the following desirable impacts:

- It would reduce competition with Navy for scarce shipbuilding resources; and
- The reduction would help reduce the inflationary pressure on ship prices, and help assure that additional shipyard capacity which might require continued Federal support, would not be created.

This reduced funding level will still result in an increase in the size of the U.S. flag fleet engaged in international trade.

The recommended funding level will not create serious shipyard employment reductions. There may be some reductions in a few yards if those yards fail to obtain Navy work. Because of the long lag time between MARAD funding and the start of ship construction, any changes in shipyard employment would not occur until late 1976.

Agency Request: Commerce continues to push for an expanded ship construction program, while spreading funding among the yards to meet political demands and to maintain or expand employment in the ship construction industry. Commerce argues that a reduction in the program would be perceived by the industry and the unions as a withdrawal of Administration support for efforts to "revitalize" the U.S. maritime industries.

OMB Recommendation. Reducing 1975-76 funding would help reduce inflationary pressures on the industry, and would reduce the potential for competition between MARAD and Navy.



Issue Paper
Department of Commerce
1976 Budget
Issue #2: Export Promotion Services

Statement of Issue

This paper covers two separate but related issues regarding Commerce's export promotion programs.

Background

The Department of Commerce provides marketing assistance and information to assist U.S. firms to export. Nominal fees are charged which recover approximately 7% of total program cost. In developing the 1975 President's Budget, it was decided that subsidized services to established exporters should be eliminated by the end of 1975, primarily because established exporters are familiar with the risks and complexities of marketing overseas. Established exporters could continue to use the Commerce services if they were willing to pay a full cost recovery fee.

Over the past year OMB has chaired an interagency review of export promotion programs, the findings of which support last year's budget decision to end subsidies to established exporters. This interagency study concluded that continuation of subsidies to established exporters promotes behavior that is uneconomic from the national viewpoint. It encourages exporters to continue to export where the cost of that activity (including the cost of the subsidy) is unprofitable.

As part of its export promotion services, Commerce maintains 14 trade center facilities around the world which are used to display U.S. products. Based on the interagency study of export promotion programs, continuation of these trade centers in the developed markets of Western Europe, Japan and Australia does not appear to be necessary or cost effective.

Issue A:

Should experienced exporters using Commerce export services be charged the full cost for the services?

Alternatives

- #1. Continue to provide subsidized export promotion services to established exporters. (Agency request)
- #2. Eliminate from the budget the funds for subsidized services for established exporters. (OMB recommendation)

Analysis of Alternatives

	<u>1974</u>	<u>1975</u>	<u>1976</u>	<u>July 1-Sept. 30, 1976</u>	<u>1977</u>
<u>Budget Authority/Outlays</u> <u>(\$ in Millions)</u>					
Agency request	22	21	20	5	20
OMB recommendation	22	21	14	4	14

Agency request: Commerce recommends continuation of subsidized services in order to "provide a leadership role in trade promotion".

Commerce believes that established exporters will not use its services at full cost recovery fees, and that the government should continue to subsidize all exporters to help solve U.S. balance of trade problems.

OMB recommendation: OMB recommends alternative #2. There is no good economic basis for taxpayer subsidy of these experienced exporters. Established exporters are familiar with the risks and complexities of marketing overseas, and can continue profitable activities without Federally-subsidized services.

The continuation of the subsidized services is not essential to solving balance of trade problems. The experienced exporters will continue to export when it is profitable for them, without the Commerce services or with full cost fees for the services.

Full cost fees will result in putting the services to a market test and should result in established exporters choosing the most cost-effective marketing alternatives. Also, full cost recovery fees would create an incentive for Commerce to reduce the cost of its services and generally increase the efficiency of its operations. The Department has provided no basis for reversing last year's decision on this issue.

Issue B:

Should Commerce continue to maintain trade center facilities in developed foreign markets?

Alternatives

- #1. Continue to maintain trade centers in both developed and emergent markets. (Agency request)
- #2. Discontinue trade centers in developed markets. (OMB recommendation)

Agency request: Commerce believes that the developed market trade centers are effective in expanding U.S. exports. It also is concerned that closing these



facilities would be detrimental to the U.S. negotiating posture in the upcoming GATT trade negotiations by sending "an inappropriate signal to our major trading competitors of a decline in U.S. interest in expanding trade."

OMB recommendation: OMB recommends closing the trade centers in the United Kingdom, Germany, Italy, France, Sweden, Japan and Australia. This will save \$4.5 million and 50 people required for these facilities. We recommend that Commerce be permitted to use \$2.4 million of these savings for more cost effective trade promotion activities for inexperienced exporters.

Analysis of the Commerce programs shows that other programs are more cost effective than the trade center program in stimulating exports. The trade center and the trade fair programs, for example, are almost identical in their methods of operations and objectives. The major difference is that trade fairs have a broader product theme, attract more visitors, and are not held at U.S. facilities. Based on 1972 actual data, trade fairs are more efficient than trade centers; a dollar of Federal expenditure resulted in \$45 of export sales under the trade fair program, compared with \$32 of sales per dollar spent for the trade centers.

In addition to Commerce programs, there are numerous well-developed alternatives in developed markets which could be used instead of a Federal trade center to bring buyer and seller together. These include industry associations and other privately arranged exhibitions, mailings, agents, distributors and the general services of export management associations.

Closing the trade centers in developed markets can certainly be explained so as not to give the impression of decreasing U.S. interest in international trade. It is, rather, an effort to improve the effectiveness of total resources available for stimulating trade.

U.S. ambassadors in the affected countries may resist closing the seven centers largely because of fears that the host country will interpret the action as a "diplomatic signal" of decreasing importance placed on their country by the U.S. Since this proposal does not single out any one country, but would apply equally to all developed markets, the "perceived downgrading" should not be a problem.

Issue Paper
 Department of Commerce
 1976 Budget
 Issue #3: Tourism Programs

Statement of Issue

Should the tourism promotion programs be terminated after calendar year 1976 (i.e., after the Bicentennial year)?

Background

The United States Travel Service (USTS) was established in 1961 with the principal objective of encouraging foreigners to visit the United States in order to help solve balance of payments problems. USTS maintains offices in six foreign countries (Canada, Mexico, the United Kingdom, France, West Germany and Japan) and, through advertising and direct promotional events with foreign travel agents, attempts to encourage foreigners to travel to the United States.

USTS estimates that approximately 14 million foreign travelers visited the United States in 1973 and that approximately 385,000 foreign visitors will come to the United States in 1976 as a result of its programs, providing a \$200 million contribution to the U.S. balance of payments. Based on these figures and the agency's 1976 request of \$12 million, each foreign visitor spends approximately \$500, and USTS spends about \$30 per visitor.

USTS has stated that beginning in 1975 it will emphasize the Bicentennial throughout all its programs. USTS is doing this indirectly and as an added theme to its existing promotional events. There is, therefore, no specific or identifiable amount in the USTS budget which is targeted on the Bicentennial.

Alternatives

- #1. Continue tourism promotion programs in 1976 and request a long-term extension of the current authorizing legislation. (Agency request)
- #2. Continue tourism promotion programs through calendar year 1976 and oppose an extension of the authorizing legislation beyond calendar year 1976. (OMB recommendation)

Analysis of Alternatives

<u>Budget Authority/Outlays</u> <u>(\$ Millions)</u>	<u>1974</u>		<u>1975</u>		<u>1976</u>		<u>July 1-Sept.</u> <u>30, 1976</u>		<u>1977</u>	
	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>
Agency request	11	11	11	11	12	12	4	4	12	12
OMB recommendation	11	11	11	11	12	12	5	3	0	2



The agency request would permit the indefinite continuation of the USTS programs. The Department contends that the program is necessary to encourage international travel to improve relations among countries, and to increase foreign exchange earnings.

The OMB recommendation would continue the program in fiscal year 1976, and provides \$5 million for the transition period to continue the program through the end of calendar year 1976. The program would be terminated at the end of the Bicentennial year (end of calendar year 1976).

Strong interest already exists among foreigners in traveling to the United States, and numerous organizations other than USTS continue to promote the United States as a desirable travel destination. The major obstacle to travel to the United States is its high costs, and USTS programs have no significant impact on this factor.

The program is not essential to improve relations among nations. The program is limited to only six countries which already have extensive tourism travel and generally good relations with the United States. The U.S. Information Agency has the primary responsibility for improving foreign understanding of the United States. It has a budget of over \$200 million, and programs in over 100 countries, for this purpose.

The USTS contribution to the U.S. balance of payments (accepting the USTS estimate of \$200 million) is insignificant when compared to total U.S. exports of goods and services, which were \$71.3 billion in 1973. This program is not an essential means of maintaining an equilibrium in the balance of payments. Flexible exchange rates are the primary means of maintaining an equilibrium.

Agency Request: The agency proposes indefinite continuation of the Travel Service activities.

OMB Recommendation. OMB recommends termination of the program at the end of calendar year 1976. USTS programs are unnecessary to meet U.S. balance of payments objectives, and by the end of calendar year 1976 the USTS program will have completed all promotional work related to the Bicentennial.



SBA

THE WHITE HOUSE

WASHINGTON



MEMORANDUM FOR: THE PRESIDENT

FROM: Roy L. Ash

SUBJECT: 1976 Budget decisions: Small Business Administration

The agency request and my recommendations with respect to the 1976 budget amounts for the Small Business Administration are presented in the tabulation attached (Tab A). A summary of the principal budget decisions reflected in my recommendation is provided as background (Tab B).

The following key issue has been identified for your consideration (detail at Tab C).

Full cost recovery interest rates on loans.

OMB recommends that legislation be requested to require full cost recovery interest rates on SBA direct loans, except on loans for the socially or economically disadvantaged (primarily minorities). This would prevent unwarranted demands for low interest funds, and end taxpayer subsidy for the loan recipients.

SBA opposes full cost recovery interest rates because it believes loan recipients should receive the additional assistance provided by the interest subsidy.

Decision: Approve agency recommendation _____
Approve OMB recommendation _____
See me _____

Attachments

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See me _____

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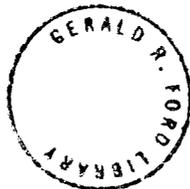


Small Business Administration

1976 Budget

Summary Data

	(\$ in Millions)		Employment	
	<u>Budget Authority</u>	<u>Outlays</u>	<u>Full-time Permanent</u>	<u>Total</u>
1974 actual	249	753	3,957	4,640
1975 January budget	448	471	4,321	4,413
enacted	443	470	xxx	xxx
outlay reduction	0	-22	xxx	xxx
supplemental recommended	0	0	xxx	xxx
OMB recommendation	443	398	4,196	4,494
1976 planning ceiling	435	335	xxx	xxx
agency recommendation	288	339	4,171	4,457
OMB recommendation	288	339	4,171	4,457
Transition Period				
agency recommendation	89	41	4,171	4,457
OMB recommendation	89	41	4,171	4,457
1977 OMB estimate	400	482	4,171	4,457



Tab B

1976 Budget

Small Business Administration

Background Information

FY 1976 is expected to be a year of transition for SBA, as it completely reevaluates its basic goals and objectives and redirects its programs to more effectively achieve the redefined objectives.

OMB has discussed with SBA our concerns about its lack of effective efforts to assist established small businesses. The bulk of SBA resources have been going to a very small proportion of all small firms (less than one-third of 1%) and many of these are marginal firms which are likely to have little economic impact. SBA agrees that there is a need to reevaluate its programs, and we have agreed to undertake a thorough study, to be completed by next September.

Loan Guarantees

Pending the outcome of that study, the agency will not undertake any major expansion of its principal loan guarantee program, which will be limited to \$1.2 billion in 1976, a slight increase over 1975, but a decrease from the 1974 level of \$1.8 billion. Upon completion of the study, the program may be expanded, terminated or redirected.

Direct Loans For Firms In Temporary Difficulty

Because of the severe problems facing many small businesses in the current economic situation, SBA will be giving top priority in 1976 to assisting established firms in temporary difficulty. The principal assistance will be long term direct loans which generally are not available from private institutions. The recommended budget amounts include \$200 million for these direct loans, which is double the 1975 level. OMB recommends that this \$200 million be made contingent upon a legislative change to provide for full cost recovery interest rates on these loans. (See Tab C)

Minority Business Development

The recommended budget will permit \$125 million for direct loans, management assistance and procurement assistance, and approximately \$195 million in guaranteed loans, for minority-owned businesses. This is approximately the same level of funding as in 1975. These programs are the subject of an on-going OMB, SBA and Commerce study, which is to be completed by next April. It is expected that the study will result in recommendations for major program changes, including some organizational restructuring. It is recommended that the funding be held at the 1975 level pending decisions resulting from that study.

Issue Paper
Small Business Administration
1976 Budget
Issue: Full Cost Recovery Interest Rates



Statement of Issue

Should interest charges on SBA direct loans be set at a level to recover full costs, including estimated average default losses?

Background

Current statutory authority for SBA loan programs places ceilings on the interest rates that SBA can charge on its direct loans to small firms. The rates vary by program, but they generally cannot be higher than the Treasury average cost of money (about 6.5% now).

The allowable interest rates do not recover the losses resulting from defaults on the loans, or the costs of administering the program. Recovery of these additional costs would increase interest rates by about 3% to 4% on programs which are effectively administered; this assumes that loans will be made only to established, competitive firms which are in temporary difficulty.

The current low SBA interest rates are very attractive to potential borrowers, and they result in demand for the SBA direct loans even when reasonable financing is available from private institutions. The low interest rates also result in a taxpayer subsidy to the individual borrower.

Alternatives

1. Continue to charge the low interest rates. (Agency request)
2. Request a legislative change to require full cost recovery interest rates. (OMB recommendation)

Analysis of Alternatives

Alternative #1. SBA objects to the full-cost recovery requirement. SBA disagrees with placing the burden of losses on the recipient of the loan. It believes this would place too high a burden on the people who are to be helped by these programs. SBA instead proposes that the interest rate be Government cost of money (currently 6.5%) plus 1% for recovery of administrative costs. The agency believes the full-cost recovery requirement would result in interest charges of at least 10.5% and perhaps more.

Alternative #2. OMB believes that subsidized interest rates are unnecessary and inappropriate for SBA loans, except those for the socially and economically disadvantaged. The small businesses which will be receiving SBA's direct loans will be established, competitive small businesses which are in temporary financial

difficulty due to adverse cyclical economic conditions, material shortages, etc. These firms are primarily in need of long-term loans (5, 10 or even 20 years) which they cannot obtain in the private sector. The long-term loans will help them spread the cost of adjusting to the temporary economic problem.

These firms are not in need of interest subsidies. They can afford the interest costs if they can obtain a long term on the loan.

The Federal Government is providing an important service for these firms by making available long-term loans. There is no economic or social reason why the taxpayers should subsidize these firms through low interest rates.

Agency request: SBA opposes requesting legislation to obtain full cost recovery.

OMB recommendation: The OMB proposes that the \$200 million planned for 1976, for direct loans for competitive firms in temporary difficulty, be requested from Congress only upon enactment of legislation to permit full cost recovery interest rates on the loans.

Tab C

Treasury

THE WHITE HOUSE

WASHINGTON

MEMORANDUM FOR: THE PRESIDENT

FROM:

Roy L. Ash

SUBJECT:

1976 Budget decisions: Department of the Treasury

The agency request and my recommendations with respect to 1976 budget amounts for the Department of the Treasury are presented in the tabulation attached (Tab A). A summary of the principal budget decisions reflected in my recommendation is provided as background information (Tab B).

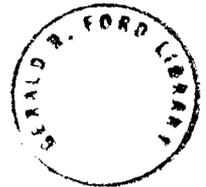
Seven key issues have been identified for your consideration (detail at Tab C).

I. IRS Tax Audit

Treasury proposes strengthening tax compliance by raising the level of audit coverage to 2.6 per cent of tax returns filed, thereby generating additional revenues and contributing to a balanced budget.

OMB recommends maintaining the 1975 level of 2.5 per cent audit coverage which will increase the absolute number of tax audits. Tax compliance will be encouraged by program increases in areas other than audit.

Decision: Approve agency recommendation _____
Approve OMB recommendation _____
See me _____



II. IRS Information Returns Processing (document matching)

Treasury proposes annually transcribing, correcting, and matching one-fourth of all information documents and tax returns.

OMB recommends initiating a selective program of document matching to stimulate voluntary taxpayer compliance by concentrating on documents with the highest potential yield or greatest likelihood of reporting inaccuracy.

Decision: Approve agency recommendation _____
 Approve OMB recommendation _____
 See me _____

III. IRS Data Processing

Treasury proposes adding 950 man-years in 1976, representing a 3 per cent growth in personnel, to process an estimated increase of 2 per cent in the number of tax returns filed.

OMB recommends maintaining the 1975 level of manpower, thereby relying on increased productivity aided by additional automatic data processing equipment to process the larger number of returns.

Decision: Approve agency recommendation _____
 Approve OMB recommendation _____
 See me _____

IV. IRS Administration of Pension Reform

Treasury proposes a supplemental appropriation of \$10.0 million in 1975. For 1976 they request a further increase of \$14.1 million. This would provide funds to handle increased responsibilities under the new Employee Retirement Security Act of 1974.

OMB recommends \$6.6 million of the \$10.0 million 1975 request and a further increase of \$4.1 million for the program in 1976. It defers additional increases in 1976 pending receipt of actual workload data. This is the same approach being recommended in the Labor Department request for this program.

Decision: Approve agency recommendation _____
 Approve OMB recommendation _____
 See me _____



V. IRS Tax Fraud Investigation

Treasury proposes adding 8 man-years in 1976 to handle increased case complexity, as part of an overall effort to demonstrate to taxpayers that those who do not meet their tax obligations are identified and prosecuted.

OMB recommends investigating the same number of criminal cases which IRS projects for 1975 and 1976, using an investigation-to-man-year standard similar to the ratio achieved in 1973 and 1974 and budgeted for in 1975, thereby reducing the 1976 budget 329 positions below the 1975 level.

Decision: Approve agency recommendation _____
 Approve OMB recommendation _____
 See me _____

VI. Taxpayer Service

Treasury proposes adding 63 positions on top of the base of 3,956 man-years provided in the OMB alternative (which reflects an increase of 878 man-years over the 1975 base) to conduct a special assistance program for the elderly and inner city taxpayers.

OMB recommends accomplishing the special emphasis program by redeploying some of the 3,956 man-years already provided in the 1976 budget for taxpayer service.

Decision: Approve agency recommendation _____
 Approve OMB recommendation _____
 See me _____

VII. U. S. Customs Service

Treasury proposes to add 311 man-years and \$19 million in 1976 to handle additional imports and people entering the United States and to expand enforcement programs to uncover duty fraud and interdict narcotics and other contraband.

OMB recommends handling the additional imports and people through a 2.5% increase in productivity, thereby reducing 323 positions below the 1975 level.

Decision: Approve agency recommendation _____
 Approve OMB recommendation _____
 See me _____



Attachments

DEPARTMENT OF THE TREASURY

1976 Budget

Summary Data

	(In millions)		<u>Employment, end-of-period</u>	
	<u>Budget authority</u>	<u>Outlays</u>	<u>Full-time Permanent</u>	<u>Total</u>
1974 actual	36,019	35,888	104,391	113,892
1975 January budget	37,688	37,633	111,431	119,250
enacted	37,683	37,637	xxx	xxx
supplementals recommended for operating accounts	26	24	xxx	xxx
outlay reduction	-24	-24	-80	-80
OMB recommendation	40,094*	40,061*	108,976	116,795
1976 planning ceiling	39,294*	39,259*	xxx	xxx
agency request (revised)	40,793*	40,680*	123,221	135,227
OMB recommendation	40,507*	40,391*	111,623	121,123
agency recommendation	40,593*	40,481*	118,522	128,722
Transition period				
agency request (revised)	10,443*	10,423*	123,221	135,227
OMB recommendation	10,365*	10,344*	111,623	121,123
agency recommendation	10,387*	10,365*	118,522	128,722
1977 OMB estimate	41,881*	41,894*	113,855	123,545

*Requests and recommendations do not include estimates of the net cost of the October 1974 pay increase:
1975: BA, \$54 M; Outlays, \$50 M. 1976: BA, \$93 M; Outlays, \$93 M.



1976 Budget

Distribution of Budget Authority#

	1974	1975		1976		July 1 -		1977	
	Actual	Jan. budget	Agency recom.	OMB recom.	Agency recom.	OMB recom.	Sept. 30, 1976 Agency recom.	OMB recom.	OMB est.
A. Open-ended programs and fixed costs (relatively uncontrollable under present law)									
1. Interest on the Public Debt	29,319	30,500	33,000	33,000	33,200	33,200	8,500	8,500	34,400
2. General Revenue Sharing	6,055	6,205	6,205	6,205	6,355	6,355	1,664	1,664	6,520*
3. Miscellaneous Permanent and Trust Funds	557	612	814	814	837	837	177	177	822
4. Offsetting receipts	-1,838	-1,930	-2,208	-2,208	-2,286	-2,286	-586	-586	-2,344
Total, open-ended and fixed costs	(34,093)	(35,387)	(37,811)	(37,811)	(38,106)	(38,106)	(9,755)	(9,755)	(39,398)
B. Discretionary programs (relatively controllable)									
1. Office of the Secretary	20	25	26	26	27	27	7	7	29
2. Office of Revenue Sharing	--	--	2	2	3	3	1	1	3
3. Federal Law Enforcement Training Center	2	22	22	22	17	17	1	1	8
4. Government Financial Operations	97	103	122	122	121	121	30	29	126
5. Alcohol, Tobacco and Firearms	81	94	92	92	97	97	26	26	106
6. U. S. Customs Service	241	286	282	282	301	285	76	73	300
7. Bureau of the Mint	25	45	34	34	80	80	10	10	51
8. Bureau of the Public Debt	81	88	96	96	97	97	27	27	102
9. Interest Revenue Service	1,309	1,558	1,530	1,526	1,651	1,581	426	408	1,661
10. U. S. Secret Service	70	80	81	81	93	93	28	28	97
Total, discretionary programs..	(1,926)	(2,301)	(2,287)	(2,283)	(2,487)	(2,401)	(632)	(610)	(2,483)
Total, Budget Authority	36,019	37,688	40,098	40,094	40,593	40,507	10,387	10,365)	41,881

*Assumes enactment of legislation to continue General Revenue Sharing

#Requests and recommendations do not include estimates of the net cost of the October 1974 pay increase: 1975, \$54 M; 1976, \$93 M.

1976 Budget

Department of the Treasury

Background Information

Treasury requests \$40.8 billion in new budget authority for 1976. Of this amount, \$38.1 billion is requested for uncontrollable accounts such as Interest on the Public Debt, Payments from the General Revenue Sharing Trust Fund, and other permanent accounts. The remaining \$2.7 billion is requested for discretionary operating programs, which fund the Department's major activities.

The OMB recommendation provides \$40.5 billion, which grants the Department's full request for uncontrollable programs but reduces the initial request for operating programs by \$217 million. OMB and Treasury have subsequently come into agreement on most 1976 budget recommendations, and the areas of dispute have been reduced to \$86 million. Items still in dispute, which are confined to the Internal Revenue Service and the Customs Service, are discussed in detail at Tab C.

The reductions in the Treasury request recommended by OMB in Treasury's operating programs stem largely from two major concerns:

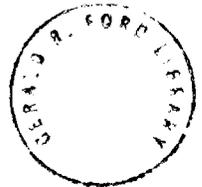
- very large staff expansion beyond the requirements of reasonable workload increases (a requested 13 percent staffing increase over 1975); and,
- failure by the Department to reflect increased productivity in some of its major programs.



The requested 13 percent increase in staff comes on top of substantial increases provided to the Department over the past few years. In both 1974 and 1975 employment increased by 4 percent over the previous year. These increases were well in excess of population growth (a basic ingredient in several Treasury programs) or workload.

The major staff expansion proposed by the Department comes in the Internal Revenue Service and the Customs Service, which historically have accounted for approximately 80 percent of the total Treasury work force. Over the years, the Department has been accustomed to requesting and receiving sizeable increases for these bureaus because, as revenue producers, they have been considered essentially costless. Treasury has maintained and continues to maintain that rapidly increasing staff in its tax collections and compliance forcing programs are necessary to avoid revenue losses. In several of these programs, staffing increases have exceeded actual workload requirements, resulting in static or declining employee productivity.

In light of the Administration's policy of maximum budget restraint in 1976, OMB has subjected the Treasury budget request to a more critical review than in recent years. While OMB agrees with Treasury on the need to maintain and improve the integrity and capability of the tax collection and enforcement system, we have attempted to more accurately relate staffing and budget needs to projected workload requirements and to assume productivity increases where appropriate. Although the OMB recommendation proposes significant reductions from Treasury's initial budget request for operating programs, it does provide \$118 million and 2,647 additional staff (2.4 percent increase) over 1975 to cope with workload increases and priority program improvements. Given the sizeable work force already in place, we believe this recommendation is adequate to successfully accomplish the 1976 program proposed by the Department and to continue progress toward the overall goal of the tax system: maximum voluntary compliance.



Issue Paper
 Department of the Treasury
 1976 Budget
 Issue #1: IRS Tax Audit

Statement of Issue

What proportion of tax returns should IRS audit in 1976?

Background

Reliance on a voluntary system of tax payments requires a level of audit activity which raises the threat that the validity of returns filed will be checked. Overall audit coverage steadily declined from 5.8 percent in 1963 to a low of 1.9 percent in 1971 and 1972, and then began rising from 2.0 percent in 1973 to 2.4 in 1974 and a projected 2.5 in 1975. There is no evidence to support the thesis that voluntary compliance changed significantly as the audit level fluctuated. In fact, voluntary compliance was estimated to be only 93.0 percent during the peak audit year of 1963, as compared to 92.6 percent when audit coverage was only 3.2 percent in 1969. It is projected by IRS to be 94.6 percent in 1976 with audits of 2.6 percent of returns.

Audit of certain income classes expected to generate the greatest potential yield far exceeds the level of overall coverage. For example, during the past four years audit of businesses with over \$30,000 in adjusted gross income has fluctuated from 8.8 to 13.0 percent, the rate projected for 1975. IRS plans comprehensive rates of audit coverage in 1975 for estate returns (24.2 percent), individuals with over \$50,000 adjusted gross income (15 percent), corporate returns (9.5 percent), and reported gifts (4.8 percent).

IRS estimates that the total amount of individual income tax owed to the Federal Government in 1976 will be \$157 billion. \$148.6 billion of this amount will be paid voluntarily, representing a compliance rate of 94.6 percent. Another \$1.3 billion will be collected as a result of audit examinations conducted by personnel requested in the FY 1976 budget. The remaining \$7 billion constitutes the projected tax gap between the estimated individual income tax owed and that actually received.

Alternatives

- #1. Raise the level of audit coverage to 2.6 percent in 1976. (Agency request)
- #2. Continue the 2.5 percent audit coverage budgeted for 1975. (OMB recommendation)

Analysis

Budget Authority/Outlays (\$ Millions)	1974		1975		1976		July 1- Sept 30, 1976		1977	
	BA	O	BA	O	BA	O	BA	O	BA	O
Agency request	497	482	595	595	635	623	159	156	656	656
OMB recommendation	497	482	595	595	620	610	155	152	640	660

IRS is requesting \$15.0 million and 946 man-years in additional resources to raise the audit level in 1976 to 2.6 percent of tax filings. Treasury supports its case for additional audit resources with the claim that the investment of an additional dollar in audit returns an average of six dollars in net direct tax revenues. However, IRS does not value the importance of this program to be great enough to warrant shifting resources from other IRS activities in order to maximize revenues. An OMB review of this estimate in 1972 concluded that a ratio closer to 2.5:1 more accurately represented the relationship of yield to cost, when taking into account IRS overhead and increased costs to the private sector required by tax audits. There are no data available to measure the effect of additional audit on potential noncompliers.

Arguments over the exact revenue producing ability of tax audits may be strictly academic and subject to an indeterminate margin of error. The real objective of this program is to encourage voluntary compliance, which accounts for over 99 percent of individual income taxes paid. Tax returns are selected for audit either because of characteristics which indicate underpayment of taxes or as part of a strategy to review a minimum number of returns in every income category in order to demonstrate the breadth of IRS audit coverage. The mix of audits expected to generate the greatest yield and audits intended to encourage voluntary compliance is decided by the Commissioner of IRS. There is some suspicion that any suggested reduction in the recommended level of audit coverage is priced from the revenue-producing cases to present the worst-possible direct revenue loss expected from such a decision. It is also difficult to accept the IRS contention that a relatively insignificant fluctuation in audit coverage, for example between 2.6 and 2.5 percent, actually causes individual taxpayers to cheat on their taxes or can really be measured.

Agency Request: Raise the level of audit coverage to 2.6 percent, thereby generating additional revenues which contribute to a balanced Federal budget.

OMB Recommendation: Maintain the 1975 level of audit coverage (2.5 percent) which should continue to assure a satisfactory level of voluntary compliance.

Issue Paper
 Department of the Treasury
 1976 Budget

Issue #2: IRS Information Returns Processing (document matching)

Statement of Issue

To what extent should IRS match information documents in 1976?

Background

In 1976 IRS expects to receive 400 million information documents related to individual income taxes--employer statements of wages earned, reports of interest and dividend payments, and declarations of profits distributed by partnerships. While taxpayers may have initially surmised that these data have been used to verify income reported by filers, the large quantity of information documents prevented IRS from actually doing so in most cases. IRS believes that many taxpayers are aware of this and are thereby encouraged not to report all sources of taxable income.

The 1975 budget provides 1,700 man-years to conduct a limited program to match information documents submitted on machine-readable tape, follow up on the non-filers identified by this tape match over the preceding two tax years, and correct missing or inaccurate spouse social security numbers on 8 million tax returns in preparation for more extensive document matching. All of these resources may be applied to whatever document matching program is approved for IRS in 1976. Of the 2.5 million discrepancies uncovered by the cursory 1975 match, IRS followed up on 250,000 cases in collections and audit. A large number of questions about unreported or under-reported income were therefore unanswered.

Alternatives

- #1. In addition to the 1,700 man-years included in the 1975 budget, provide 1,430 additional man-years in 1976 to conduct an expanded program to correct taxpayer identification numbers and match the information documents and tax returns of one-fourth of the filers, conducting related audit and collection activities in 1977. (Agency request)
- #2. Utilize the 1,700 man-years provided in the 1975 budget to initiate a selective program (covering 5 percent of the returns) of matching documents with high potential yield in 1976, and to expand audit and collection follow-up on discrepancies and non-filers identified. (OMB recommendation)

Analysis

<u>Budget Authority/Outlays</u> <u>(\$ Millions)</u>	<u>1974</u>		<u>1975</u>		<u>1976</u>		<u>July 1 -</u> <u>Sept 30,</u> <u>1976</u>		<u>1977</u>	
	<u>BA</u>	<u>0</u>	<u>BA</u>	<u>0</u>	<u>BA</u>	<u>0</u>	<u>BA</u>	<u>0</u>	<u>BA</u>	<u>0</u>
Agency request	2	2	24	24	43	42	11	11	51	51
OMB recommendation	2	2	24	24	25	25	6	6	26	26

It is important to agree on the objective of document matching and the most cost-effective way of achieving it before launching a massive program of random transcribing and matching millions of documents. As in the audit program, the IRS objective here is to encourage voluntary compliance, in this instance to cause taxpayers to accurately report all taxable income on their filings. Moving in this direction need not require a blanket match of every taxpayer or even every fourth taxpayer, as IRS proposes, but rather can selectively identify potential violators and use these matches as an example to encourage compliance from the general public (again similar to the approach used in tax audit).

The agency request proposes matching tax returns with 100 million information documents related to one-fourth of the population, selected by surname. Matches would be made of 60 million paper documents and 40 million machine-readable documents. The 60 million paper documents would have to be sorted, batched, edited, transcribed, corrected, and entered into the ADP system. Substantial personnel are requested in the collection activity to follow up on unresolved cases where no taxpayer identification number is shown on information documents. Some attention would be given to addressing discrepancies between reported income and income reflected on information documents, but investigation into underreported cases and non-filers would not begin until 1977.

In contrast to the agency request which would compare 100 million documents (25 percent of the total), the OMB recommendation would match 20 million high-potential documents (constituting 5 percent of the total), chosen according to predetermined criteria to maximize potential yield. The candidates for selection would be taken from 172 million documents (43 percent of total documents filed), consisting of the 160 million tape documents and 12 million paper documents entered into the ADP system in an initial step to begin some degree of paper sorting and matching in 1976. Only those documents selected would be corrected to enter valid taxpayer identification numbers. The OMB recommendation also includes resources for expanding and improving use of machine-readable tape input. It provides collection and audit personnel to follow up on a large proportion of cases developed by matching documents, whereas the agency request would use a larger number of collection personnel primarily to correct missing or inaccurate taxpayer identification numbers.

Agency Request: Begin annually transcribing and matching one-fourth of all information and tax returns.

OMB Recommendation: Initiate a selective program of document matching to stimulate voluntary taxpayer compliance, while concentrating on documents with the greatest yield potential, similar to the approach used in tax audit.

Issue Paper
 Department of the Treasury
 1976 Budget
 Issue #3: IRS Data Processing

Statement of Issue

What consideration should be given to productivity in budgeting for data processing in IRS?

Background

The data processing operations activity is responsible for receiving and processing tax returns, issuing refunds and notices, and accounting for revenues. In 1974 this program processed 121.6 million Federal tax returns. IRS estimates it will receive 124.0 million returns in 1975 and 126.5 million returns in 1976.

Alternatives

- #1. Add 950 man-years (\$11.3 million) to handle the increased workload projected for 1976. (Agency request)
- #2. Maintain the same work force provided in 1975 and expect the larger number of returns to be processed through increased productivity. (OMB recommendation)

Analysis

Budget Authority/Outlays (\$ Millions)	1974		1975		1976		July 1 - Sept 30, 1976		1977	
	BA	O	BA	O	BA	O	BA	O	BA	O
Agency request	316	306	370	370	386	379	97	95	398	398
OMB recommendation	316	306	370	370	375	368	94	92	375	375



IRS supports its case for additional staff by citing the growth in returns volume and complexity. Timely processing of returns is said to be important in maintaining public confidence in the efficiency of the tax system.

OMB acknowledges the desirability of prompt returns processing and has provided for procurement of additional automatic data processing equipment in 1976 to facilitate this activity. The OMB alternative allows for purchase of 191 new entry terminals, additional capacity for central processing units, and \$400,000 in miscellaneous auxiliary and accessory equipment. In addition to the workload savings generated by these additions, it is anticipated that the three new service centers opened by IRS in 1975 will operate more efficiently in 1976.

Data processing operations are particularly well-suited to productivity increases because of their industrial nature. The OMB alternative assumes a 2 percent productivity factor, a realistic goal which returns to the output-per-man-year level achieved in 1974. New ADP equipment should offset any increase in return complexity.

	<u>Man-years in Returns Processing</u>	<u>Tax Returns Filed</u>	<u>Returns per Man-year</u>
1974 Actual Experience	24,817	121,600,000	4,899
1975 Budget	26,610	124,000,000	4,659
1976 IRS Request	27,560	126,500,000	4,589
1976 OMB Recommendation	26,610	126,500,000	4,753

Agency Request: Provide additional resources to process larger numbers of tax returns in 1976.

OMB Recommendation: Expect increased productivity aided by additional ADP equipment to offset the projected 2.0 percent increase in tax returns filed in 1976.

Issue Paper
Department of the Treasury
1976 Budget
Issue #4: IRS Administration of Pension Reform

Statement of Issue

What should be the level of resources in 1975 and 1976 to implement IRS responsibilities under the new pension reform law?

Background

The Employee Retirement Income Security Act of 1974 completely changes the tax provisions relating to employee pension plans. Virtually all existing plans will have to be amended to comply with the new qualification requirements. The Act provides a new right of appeal to the Tax Court for a declaratory judgment as to plan qualification. To carry out these provisions the new law specifically requires the establishment of an "Office of Employee Plans and Exempt Organizations" to be headed by an Assistant Commissioner in IRS. The responsibilities of the new organization include issuing determination letters concerning the qualification of employee plans and the tax exempt status of other organizations, providing taxpayer guidance through the publication of rulings and procedures relating to the tax aspects of these plans and organizations, examining required returns and other information documents, providing administrative remedies to allow taxpayers to resolve differences with the IRS in cases involving the qualification of employee plans, and establishing and maintaining employee plans and exempt organizations master files.

Alternatives

- #1. Provide for implementation of the Employee Retirement Income Security Act by adding 389 man-years and \$10.0 million in a 1975 supplemental appropriation and an additional 637 man-years and \$13.4 million in 1976. (Agency request)
- #2. Add 221 man-years (\$6.6 million) in a 1975 supplemental appropriation to begin implementation of the pension reform law but defer additional increases beyond annualization (86 man-years; \$1.8 million) in 1976 until better workload data are available and experience is gained in administering the program; provide 112 man-years (\$2.3 million) in 1976 to strengthen tax review of exempt organizations. (OMB recommendation)

Analysis

<u>Budget Authority/Outlays</u> <u>(\$ Millions)</u>	<u>1974</u>		<u>1975</u>		<u>1975</u> <u>Supp.</u>		<u>1976</u>		<u>July 1 -</u> <u>Sept 30</u> <u>1976</u>		<u>1977</u>	
	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>
Agency request	45	44	49	49	+10	+10	73	72	19	19	75	75
OMB recommendation	45	44	49	49	+7	+7	60	59	15	15	62	62

IRS was appropriated \$23.3 million in 1975 for its pension plan program prior to passage of the 1974 Act and \$26.1 million for its ongoing review of exempt organizations. In implementing the new law, IRS has combined these two programs under a single organization. Utilizing the impetus provided by the 1974 Act, IRS seeks to strengthen both facets of the new organization through a supplemental request in 1975 and an additional increase in 1976.

The OMB recommendation is consistent with the approach already approved for the companion program in the Department of Labor to implement its responsibilities under the 1974 law. OMB and Labor agreed that no additional resources beyond a 1975 supplemental would be recommended for Labor until workload estimates become available next spring to demonstrate whether the 1975 program is adequate to carry out the Department's responsibilities. Using a similar approach, the OMB recommendation adds positions in 1975 for pension reform (and annualization in 1976), but defers further expansion in 1976 until experience is gained in administering the new Act. This action will likely result in a request for a spring supplemental. In addition, the OMB recommendation provides resources in 1976 to assist in establishing new regional organizations for reviewing exempt organizations and expanding IRS activities in this area at a slower rate than proposed by IRS.

Agency Request: Provide for implementation of the Employee Retirement Security Act and expand tax review of exempt organizations through a 1975 supplemental of \$10.0 million and new budget authority of \$13.4 million in 1976.

OMB Recommendation: Consistent with the OMB approach to the Department of Labor, submit a 1975 supplemental request of \$6.6 million and approve \$1.8 million in annualization in 1976 for pension reform, recognizing that additional resources may be required in 1976 when workload levels generated by the 1974 Act have been determined; provide \$2.3 million in 1976 for tax review of exempt organizations, but disapprove a 1975 supplemental for this purpose on the grounds that no new circumstances justify program expansion in the current year.



Issue Paper
 Department of the Treasury
 1976 Budget
 Issue #5: IRS Tax Fraud Investigation

Statement of Issue

What is the appropriate level for tax fraud investigation in 1976?

Background

The objective of tax fraud investigations is "to encourage the highest degree of compliance with Internal Revenue laws pertaining to income, estate, gift, employment and certain excise taxes by enforcement of the criminal provisions in such laws." There are two sides to this program, investigation into suspected fraud by taxpayers in general and the special enforcement activity targeted against persons believed to be engaged in organized crime or traffickers in illicit narcotics.

Alternatives

- #1. Add 8 man-years to tax fraud investigations in 1976 to offset increasing case complexity. (Agency request)
- #2. Reduce personnel by 329 man-years, but handle the same number of cases projected by IRS through more productive employment of special agents and support personnel. (OMB recommendation)

Analysis

	1974		1975		1976		July 1 - Sept 30, 1976		1977	
	BA	O	BA	O	BA	O	BA	O	BA	O
<u>Budget Authority/Outlays</u> <u>(\$ Millions)</u>										
Agency request	85	82	100	100	100	98	25	25	101	101
OMB recommendation	85	82	100	100	95	93	24	24	96	96

As the following data reflect, the estimate of tax fraud investigations to be conducted in 1975 has declined from 10,100 when the 1975 budget was prepared last fall to a current figure of 7,700. At the same time, man-years devoted to the program have increased in non-professional supporting positions. The resulting trend in declining productivity is projected to continue in 1976.

Workload - investigations	1973 Actual	1974 Actual	1975 Program		1976 Request	Change from 1975 budget	1976 Recom.
			in 1975 Budget	in 1976 Budget			
Taxpayers in general	6,742	5,750	8,200	6,300	6,300	-17%	6,300
Special enforcement	1,859	1,465	1,900	1,400	1,400	-26%	1,400
Total	8,601	7,215	10,100	7,700	7,700	-19%	7,700
<u>Man-years</u>							
Special agents	2,342	2,519	2,649	2,645	2,650	+9%	2,587
Other FTP	1,164	1,274	1,312	1,389	1,392	+5%	1,118
Total	3,506	3,793	3,961	4,034	4,042	+8%	3,705
<u>Workload Per Man-year</u>							
Special agents	3.7	2.9	3.8	2.9	2.9	-1.0	3.0
Other	7.4	5.7	7.7	5.5	5.5	-1.7	6.9

The IRS request contains a slight increase in personnel in 1976 to handle workload that will decline 19 percent from the level provided for in 1975 budget. IRS explains the decrease in productivity as a result of growing case complexity.

The OMB recommendation budgets for the same number of tax fraud investigations projected by IRS for 1976 but uses a workload standard closer to the investigations-per-man-year ratio budgeted for in 1975 and achieved in 1973 and 1974. IRS has offered no convincing justification to explain increased case complexity, however if this materializes, it would be offset in this alternative by higher productivity.

Agency Request: Add 8 man-years in 1976 to address caseload complexity in 1976.

OMB Recommendation: Reduce 329 man-years but achieve the same results by relying on investigative output comparable to the level budgeted for in 1975.



Issue Paper
 Department of the Treasury
 1976 Budget
 Issue #6: Taxpayer Service

Statement of Issue

What is the appropriate level for taxpayer service in 1976?

Background

The taxpayer service program is responsible for providing taxpayers with the quality and degree of assistance they need to meet their Federal tax filing obligations. In 1975, 3,085 man-years will respond to an estimated 10 million personal inquiries, 25.5 million phone inquiries, and 500,000 letters from taxpayers. IRS projects a total of 43 million taxpayers inquiries will be received in 1976, as contrasted to the 36 million estimated for 1975.

Alternatives

- #1. Add 279 man-years to taxpayer service in 1976. (Agency request)
- #2. Add 216 man-years to taxpayer service in 1976. (OMB recommendation)

Analysis

<u>Budget Authority/Outlays</u> <u>(\$ Millions)</u>	<u>1974</u>		<u>1975</u>		<u>1976</u>		<u>July 1 - Sept 30, 1976</u>		<u>1977</u>	
	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>	<u>BA</u>	<u>O</u>
Agency request	93	80	101	101	119	119	30	30	121	121
OMB recommendation	83	80	101	101	118	118	30	30	120	120

IRS seeks the addition of 279 man-years and \$9.2 million to taxpayer service in 1976 to handle the anticipated growth in workload and to conduct special assistance programs directed to the elderly and inner city taxpayers. The request is justified as being responsive to congressional interest in expanding taxpayer assistance and as part of a general effort to educate the public on its tax responsibilities.

The OMB alternative allows for an increase of 216 man-years to handle increased workload projected by IRS, despite the unusually large number of taxpayer contacts estimated for 1976. The growth of 7 million in 1976 far exceeds the increase of 1.6 million expected from 1974 to 1975. In the event this workload does not materialize, IRS would be able to apply additional under-utilized resources to its special assistance program for the elderly and inner city residents. Otherwise, IRS would be forced to establish new priorities for employment of its 3,956 man-years in order to accomplish this 63 man-year requirement.

The 1976 budget will reflect an increase of an additional 655 man-years in taxpayer service for 1976 attributable to shifting into the taxpayer service activity accountability for audit and collection personnel actually attached to this program. Consequently, under the OMB alternative a total increase of 878 man-years will be shown for the taxpayer service activity in 1976, representing a 28 percent increase

Agency Request: Add 63 man-years on top of the 216 man-year increase provided in the OMB alternative for taxpayer service.

OMB Recommendation: Provide 216 additional man-years for taxpayer service in 1976 and rely on the 3,956 man-years budgeted for this activity in 1976 to accomplish the expanded special assistance program requested by IRS.

Issue Paper
 Department of the Treasury
 1976 Budget
 Issue #7: U.S. Customs Service

Statement of Issue

What is the appropriate level of resources for the U.S. Customs Service in 1976?

Background

The U.S. Customs Service collects duties and other taxes on imports and enforces customs and related laws. The Customs Service has grown rapidly over the last several years. Since 1969, Customs manpower has increased by 57% to 12,918 man-years in 1975 while the two main indicators of workload, formal entries of imports and the number of persons arriving from foreign countries, have increased by 32% and 18% respectively. Customs manpower increases were achieved even though the drug investigation function and associated resources (735 positions) were transferred from Customs to the Drug Enforcement Administration in the beginning of 1974.

The past increases in manpower occurred because of the emphases placed upon the interdiction and investigation of drugs and increasing workload. Overall productivity has declined over the past few years. In 1974, an absolute decrease in formal entries of imports, the primary work indicator, further aggravated the productivity decline. The requested Customs' budget shows that productivity will continue declining in 1975 and 1976 from the 1974 level.

The Treasury Department is requesting an additional 311 man-years and \$19 M for Customs in 1976 to expand its enforcement program (\$5.8 M), to process additional workload (\$3.4 M), to maintain current staff levels (\$8.5 M) and to expand other programs (\$1.4 M).

Alternatives

- #1. Add manpower (311 man-years and \$19 M) to process imports and passenger arrivals and to increase the enforcement of laws against smuggling and fraud. (Agency request)
- #2. Reduce manpower (-323 man-years) to force a 2.5% productivity increase above the last actual year (1974), but add net increase in funds (+\$3 M) for cost increases and for additional staff for priority items which contribute to increased productivity such as marihuana detector dogs and the computer processing system for cargo. (OMB recommendation)

Analysis

<u>Budget Authority/Outlays</u> (\$ Millions)	1974		1975		1976		July 1- Sept 30, 1976		1977	
	<u>BA</u>	<u>0</u>	<u>BA</u>	<u>0</u>	<u>BA</u>	<u>0</u>	<u>BA</u>	<u>0</u>	<u>BA</u>	<u>0</u>
Agency Request	241	225	282	297	301	312	76.4	75.8	322	322
OMB Recommendation	241	225	282	297	285	290	72.6	71.8	300	300

From 1969 to 1973 Customs productivity in processing persons entering the U.S. declined by approximately 50% while productivity in processing imports rose by 4%, although it varied from year to year. In 1974, productivity declined by 10% in processing persons and by 3% in processing cargo. The 1976 request would decrease productivity below 1974.

In order to reverse this trend of declining productivity, OMB recommends a reduction of 307 man-years in 1976 which is equivalent to a 2.5% increase in productivity over 1974.

This increase will not recoup the productivity decreases which have occurred over the last five years. However, it will reverse the declining trend and provide a reasonable base for future year budget projections. Further reductions in 1976 are not considered feasible because of potential disruptive effects upon Customs' programs. Productivity increases should allow Customs to achieve its work program as projected.

OMB also recommends a 40 man-year decrease in the law enforcement activity. Productivity in law enforcement is difficult to measure but we believe that the rise in Customs agents from 350 in 1969 to 548 in 1975 is excessive when their major investigative function, drugs, has been transferred to DEA.

The Department of Treasury recommends additional manpower to maintain the current program level and maintain that the workload indicators do not capture the significant amounts of manpower devoted to searching for illegal drugs, preventing and uncovering smuggling and other fraudulent activities. The Department also points out that the OMB recommendation would reduce the expected revenue by "many millions of dollars." The Department emphasizes that these enforcement programs result in greater revenue collected, or value of drugs seized, than the costs of the program.

OMB believes that the marginal benefit of minor decreases or increases in personnel within Customs do not materially affect the availability of heroin or other drugs in the U.S. or the amount of duties collected.

Even though the OMB recommendation reduces the Customs program, it does provide 24 positions for essential increases for the opening of new ports of entry, additional detector dogs and expansion of the computer system to process cargo. These increases should result in long-term productivity gains and more effective enforcement.

Agency Request: Treasury wishes to maintain current programs and expand priority enforcement programs by adding 311 man-years and \$19 million in the Customs Service.

OMB Recommendation: Reducing Customs (-323 man-years and +\$3 million) in order to achieve a 2.5% productivity gain should not significantly affect revenues collected or drug seizures.

Smaller Agencies

ADMINISTRATIVE CONFERENCE OF
THE UNITED STATES

Comments

No change from agency request.



	Budget authority (in thousands of dollars)	Outlays (in thousands of dollars)	Full-time permanent employment
1974 actual.....	600	507	13
1975 current estimate.....	750	779	14
1976 agency request.....	790	780	16
1976 OMB recommendation...	790	780	16
Effect of OMB recom- mendation on agency request.....	---	---	---
Transition period.....	198	190	16
1977 estimate.....	790	780	16

COUNCIL OF ECONOMIC ADVISERS

<p>Comments</p> <p>No change from agency request.</p>

	Budget authority (in thousands of dollars)	Outlays	Full-time permanent employment
1974 actual.....	1,414	1,343	37
1975 current estimate.....	1,600	1,554	46
1976 agency request.....	1,575	1,562	46
1976 OMB recommendation....	1,575	1,562	46
Effect of OMB recom- mendation on agency request.....	---	---	---
Transition period.....	393	413	46
1977 estimate.....	1,575	1,524	46

THE RENEGOTIATION BOARD

Comments

OMB recommendation accepts request to continue the program at essentially the same level as 1975. Agency will not appeal.

	Budget authority (in thousands	Outlays of dollars)	Full-time permanent employment
1974 actual.....	4,805	4,709	183
1975 current estimate.....	5,163	4,995	200
1976 agency request.....	5,395	5,335	200
1976 OMB recommendation...	5,395	5,300	200
Effect of OMB recom- mendation on agency request.....	---	-35	---
Transition period.....	1,346	1,334	200
1977 estimate.....	5,395	5,400	200

COMMISSION ON THE REVIEW OF THE
NATIONAL POLICY TOWARD GAMBLING

Comments

OMB recommendation would deny personnel increases and reduce contract research program and support services. No significant program effect is expected.



	Budget authority (in thousands of dollars)	Outlays	Full-time permanent employment
1974 actual.....	250	248	8
1975 current estimate.....	1,000	951	20
1976 agency request.....	880	892	24
1976 OMB recommendation....	750	762	20
Effect of OMB recom- mendation on agency request.....	-130	-130	-4
Transition period.....	135	175	20
1977 estimate.....	100	69	---