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INSIGHT

The FY2025 Budget in Historical Context

March 28, 2024

The Biden Administration submitted its budget for FY2025 on March 11, 2024. The budget calls for increased federal revenues, continued growth in mandatory outlays, and decreased discretionary outlays relative to the size of the economy. This Insight discusses these fiscal proposals in the context of longer-term budgetary trends and highlights selected events and legislation.

Revenues

Figure 1 shows federal receipts by major category as a share of gross domestic product (GDP) since FY1962. Federal receipts exceeded outlays (grey line) in five years (FY1969, FY1998-FY2001). In every other year the government ran a deficit, which required borrowing through the sale of Treasury securities. Economic conditions and employment levels affect tax receipts, as do major tax measures.

Individual income taxes and payroll taxes, such as for Social Security and Medicare, have long been the largest revenue components. Corporate income taxes as a share of GDP fell from 3.5% in FY1962 to 1.6% in FY2023.

The 1964 Kennedy tax reduction act lowered high Korean War-era marginal tax rates. Other acts adjusted the tax code to offset bracket creep, where inflation pushed households into higher tax brackets. The 1981 Kemp-Roth act indexed brackets and cut marginal rates by about a quarter. In 1986, the Tax Reform Act lowered marginal rates and curtailed many tax preferences while aiming to be budget neutral. A 1993 omnibus act increased certain taxes, helping to reduce deficits. Major tax acts in 2001, 2003, 2013, and 2017 reduced various tax rates.

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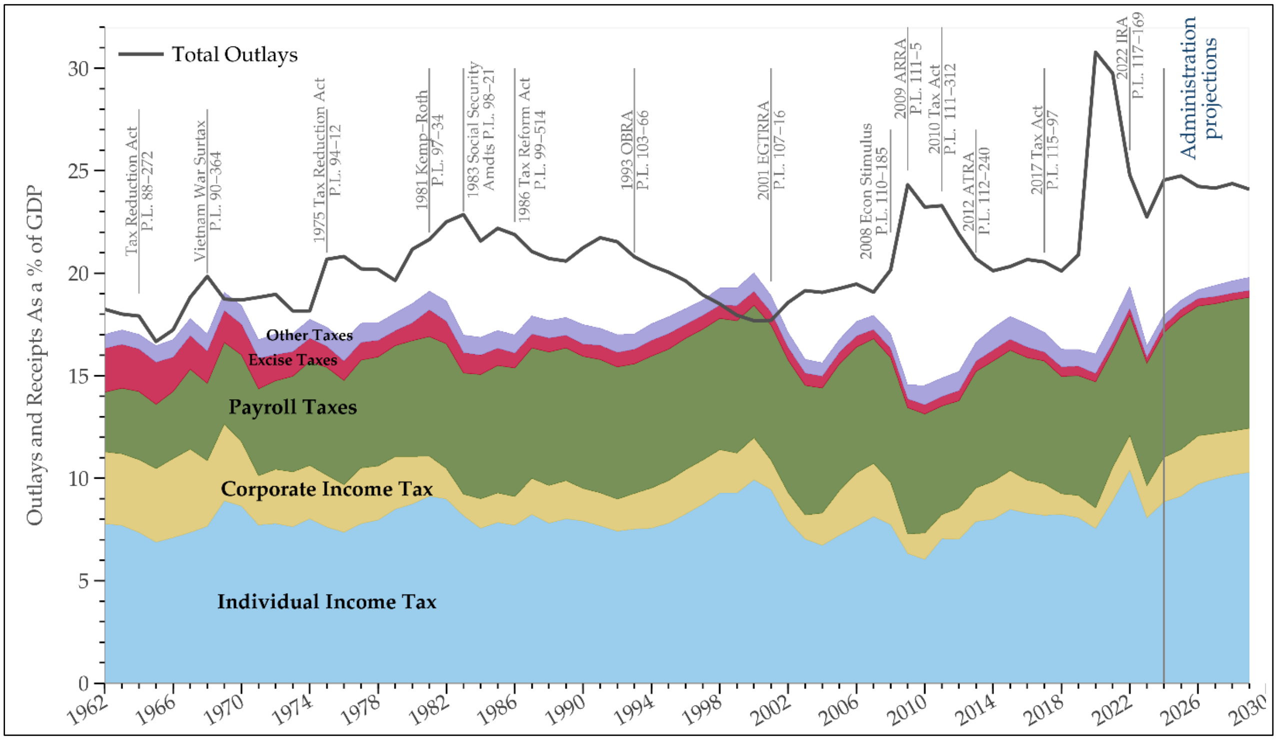
Figure 1. Federal Receipts by Major Category As a Percentage of GDP, FY1962-FY2029



Sources: CRS calculations based on OMB and Bureau of Economic Analysis (BEA) data.

Most individual tax provisions of the 2017 tax act are scheduled to expire at the end of FY2025, providing an opportunity for Congress and the President to revisit federal tax policy. The 2017 act permanently lowered the corporate income tax rate to 21% and temporarily lowered some individual income tax rates, among other changes. The act also capped the state and local tax (SALT) deduction, which resulted in tax increases for some households.

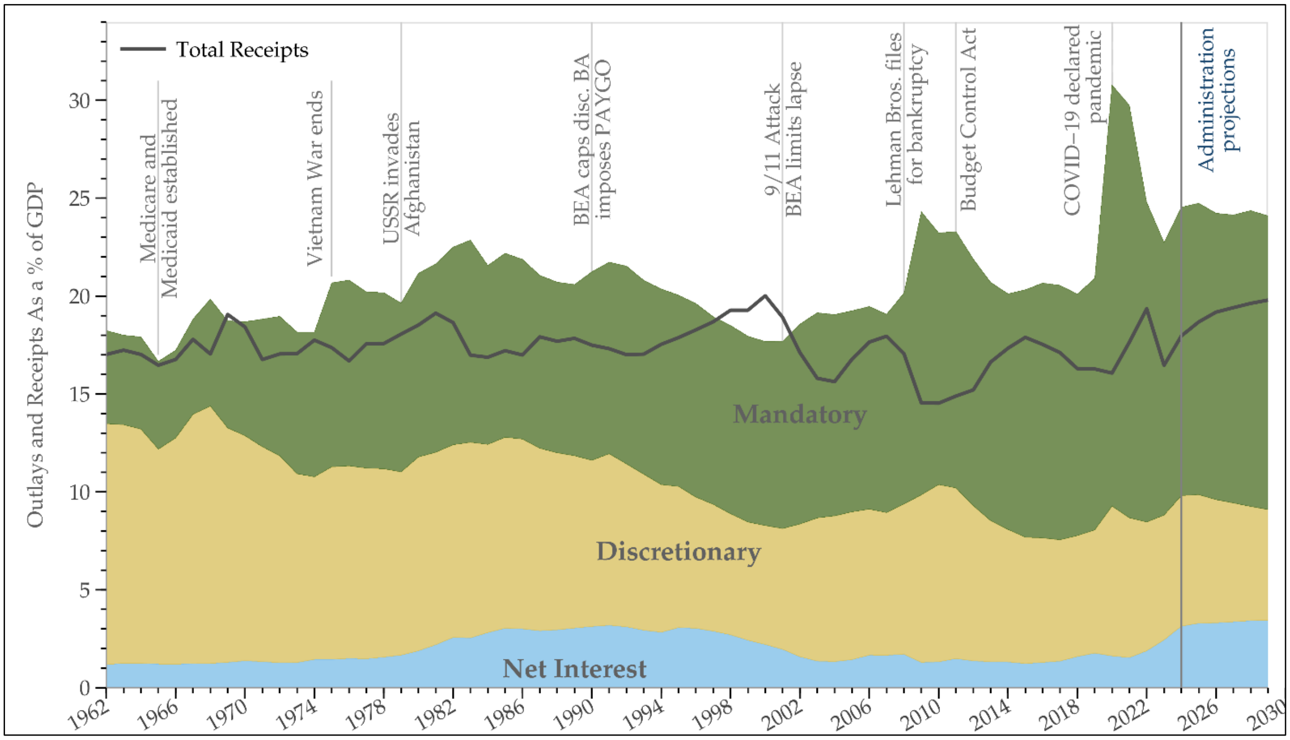
The Biden Administration's FY2025 budget proposes increasing the corporate income tax rate to 28% and setting higher tax rates on high-income households, among other provisions. The Administration also proposes an expanded Child Tax Credit. It projects federal receipts as a share of GDP would rise from 16.5% in FY2023 to 19.8% in FY2029.

Outlays

Figure 2 shows federal outlays by Budget Enforcement Act (BEA; P.L. 101-508) categories since FY1962 and total receipts (grey line), both measured as shares of GDP. Annual appropriations acts fund and control discretionary outlays. Other laws fund mandatory outlays. Discretionary spending mostly supports federal agencies' operations, including those of the Department of Defense. Mandatory spending mostly supports social insurance, health, and retirement programs. Over time, mandatory spending's share of federal outlays has grown, while discretionary spending's share has declined.

Rising federal deficits in the 1980s spurred Congress to set constraints on deficit levels through the 1985 Gramm-Rudman-Hollings Act. In 1990, the BEA set statutory caps on discretionary budget authority (BA) and established pay-as-you-go (PAYGO) limits on mandatory spending and tax cuts. PAYGO and discretionary caps expired shortly after the attacks of September 11, 2001 (9/11 attacks). The Budget Control Act (P.L. 112-25) reimposed caps on discretionary spending through FY2021, for the most part setting separate limits on defense and nondefense BA. The Fiscal Responsibility Act of 2023 set new caps on defense and nondefense discretionary spending for FY2024 and FY2025.

Figure 2. Federal Outlays by BEA Category As a Percentage of GDP, FY1962-FY2029



Sources: CRS calculations based on OMB and Bureau of Economic Analysis (BEA) data.

Mandatory Outlays

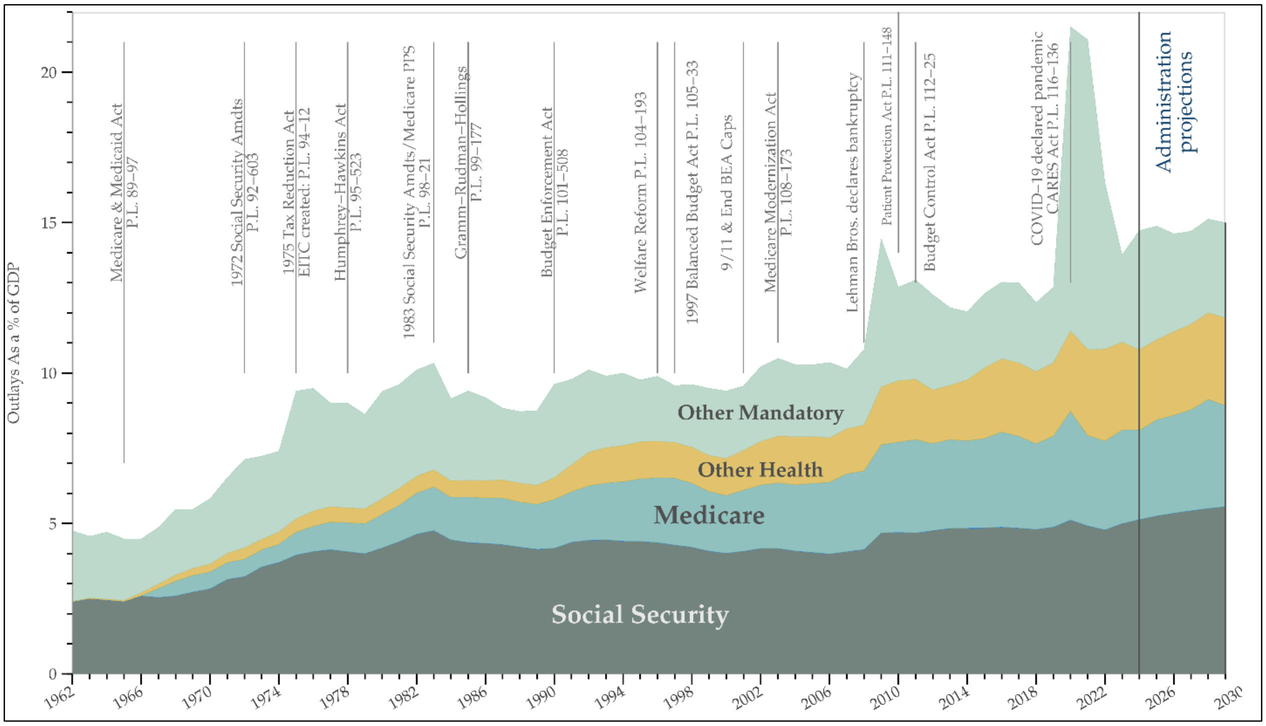
Figure 3 shows major components of mandatory outlays. Social Security, created in 1935 during the Great Depression to provide for old-age retirement, is now the largest federal program. A 1972 act raised Social Security benefits, tied them to a cost-of-living index, and created the Supplemental Security Income program. Financial concerns prompted a 1983 act limiting certain benefits and raising employee and employer contribution rates. Baby Boom retirements have increased Social Security outlays in the past decade and will continue to raise them in coming years.

In 1965, Medicare and Medicaid (shown within *Other Health*) were established to provide health care to the elderly and to low-income individuals. As beneficiary populations and health care costs rose, so did federal health outlays. Major legislation in 1996 and 1997 limited certain income security and health care programs.

Many mandatory programs act as automatic stabilizers that mitigate macroeconomic fluctuations. When incomes drop during recessions, more households become eligible for social benefits and tax collections fall. Other economic shocks—including the 2007-2009 financial crisis, exemplified by the failure of the Bear Stearns and Lehman Brothers investment banks; the ensuing Great Recession; and the COVID-19 pandemic—led to robust federal fiscal responses.

Net interest costs as a share of GDP fell in the late 1990s as falling interest rates outpaced debt accumulation. In recent years, however, large COVID-19-era debt increases and rising interest rates combined to raise net interest costs.

Figure 3. Mandatory Outlays by Category As a Percentage of GDP, FY1962-FY2029



Sources: CRS calculations based on OMB and Bureau of Economic Analysis (BEA) data.

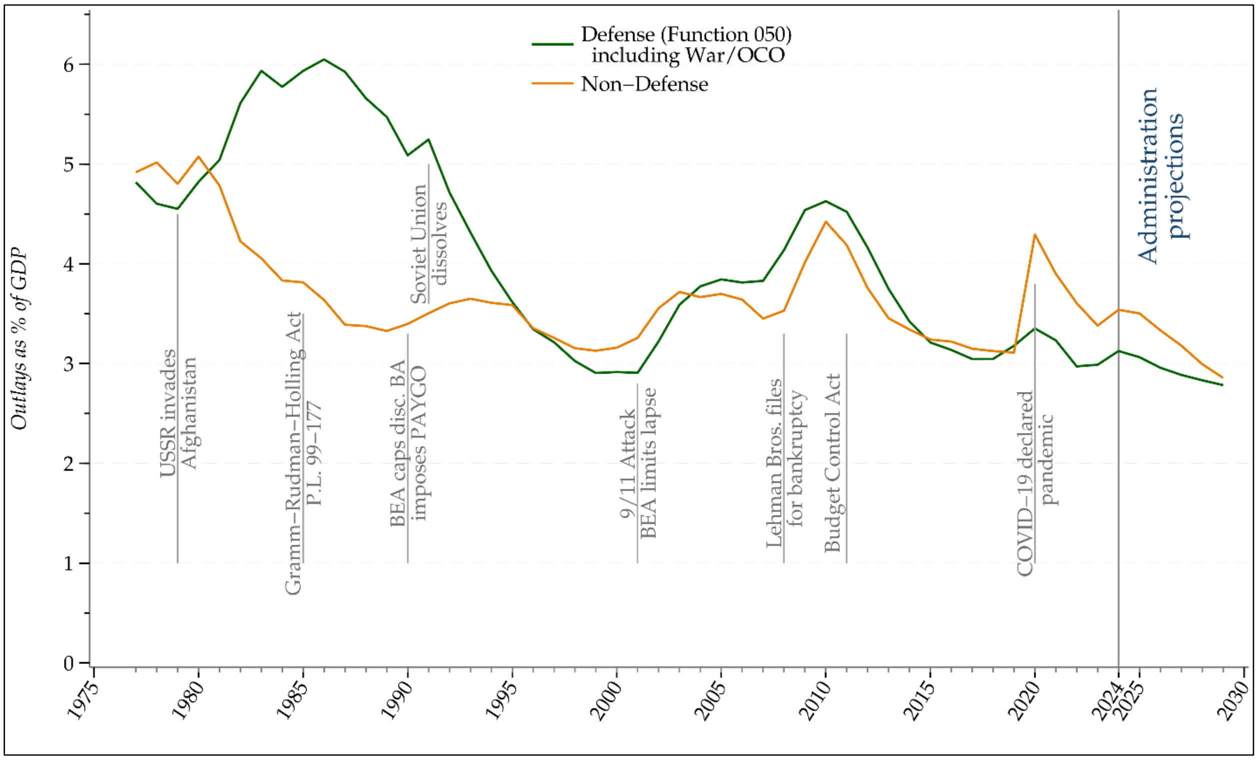
The Administration's FY2025 budget opposes reductions in Social Security and Medicare, but proposes measures aimed at reducing drug and health care costs. The Administration would also expand paid family and medical leave and spend more on public health programs. Mandatory spending, according to Administration projections, will be below pandemic-era levels but above pre-pandemic levels.

Discretionary Outlays

Figure 4 shows discretionary defense and nondefense outlays measured as shares of GDP. After the Soviet Union invaded Afghanistan in 1979, defense outlays rose dramatically, reaching 6% of GDP in the mid-1980s. The Soviet Union's 1991 dissolution yielded a "peace dividend" and falling defense outlays. The 9/11 attacks, lapsing of BEA budgetary limits, and wars in Afghanistan and Iraq all increased discretionary outlays in the aughts. After elevated spending responding to the 2007-2009 Great Recession, the 2011 Budget Control Act reestablished caps on discretionary spending through FY2021. The 2023 Fiscal Responsibility Act restored caps for FY2024 and FY2025.

According to Administration projections, both defense and nondefense discretionary outlays will continue to fall as a share of GDP in coming years. Defense discretionary outlays are mostly projected to rise, but more slowly than GDP growth. The Administration proposes a 2.8% increase in nondefense discretionary outlays for FY2025 over estimated FY2024 levels, and small reductions for later years.

Figure 4. Discretionary Defense and Nondefense Outlays As a Percentage of GDP, FY1977-FY2029



Sources: CRS calculations based on OMB and Bureau of Economic Analysis (BEA) data.

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