

CHAPTER 20 SUMMARY CONTINUED**PREPARING THE FEDERAL BUDGET** (*continued*)

The Gramm-Rudman-Hollings Act of 1986, or GRH, attempted to reduce the budget deficit. GRH required that each budget item automatically be cut by a certain percentage if the president and Congress could not agree on specific program cuts. GRH failed to achieve its goal because the government kept revising the deficit reduction targets to avoid automatic spending cuts.

Some experts use the term *incrementalism* to describe the budget-making process. Incrementalism means that generally the total budget changes only in small degrees, or increments, each year. Most agencies can assume that they will receive at least the same amount of money that was appropriated the previous year.

★MANAGING THE ECONOMY ★★★★★★★★★★★★★★★★★★★★★★★★★★★★★★★★★★★★★★

Government spending includes: (1) interest on the national debt; (2) direct benefit payments to individuals; (3) national defense; and (4) grants to states and local communities.

- Almost one-half of every dollar spent by the federal government goes to support health care and social programs.
- Recently the government has reduced funding for defense, but it still accounts for 17 percent of all expenditures.
- Federal grants to state and local governments help fund services ranging from road repair to school lunch programs.

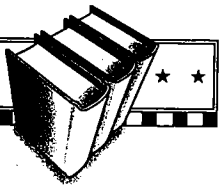
The government uses fiscal policy and monetary policy to manage the economy. Fiscal policy uses taxation and spending to influence the economy. By reducing taxes, the government gives investors and consumers more money to spend. Spending more money than the government takes in can create jobs.

Monetary policy involves influencing the economy through control of the money supply and credit. The Federal Reserve System, known as the Fed, exercises this control. The Fed, which is divided into 12 districts, is the central banking system of the United States. When people or corporations need money, they borrow from a bank. When banks need money, they go to the Fed.

A seven-member Board of Governors supervises the Fed. The president, with Senate approval, appoints these governors. Once appointed, Federal Reserve governors have extensive freedom to make economic decisions independent of political influence. The Board of Governors uses three tools to control the nation's money and credit policies:

- **The Fed can raise or lower the discount rate.** The discount rate is the interest rate that the Fed charges banks for loans. High discount rates mean banks will borrow less money and have less money to lend consumers.
- **The Fed may raise or lower the reserve requirement.** The reserve requirement is the percentage of its deposits that a member bank must keep in Federal Reserve Banks. The higher the reserve requirement, the less money banks have to lend.
- **The Fed can engage in open-market operations—it can buy or sell government securities.** If the Fed buys government securities, individual investors must turn to private ventures, which puts more money into the economy. If the Fed sells government securities, investors buy them, which takes money out of the economy.

Guided Reading Activity 20-1

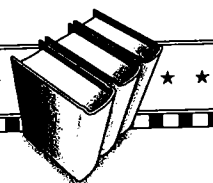


Raising Money

★DIRECTIONS Use the information in your textbook to complete these sentences.

1. Total income minus deductions and personal exemptions is one's _____.
2. A progressive tax is a tax based on a taxpayer's _____ to _____.
3. An in-depth examination of income tax returns is called an _____.
4. All the earned income of a corporation beyond its expenses and deductions is subject to a _____ tax.
5. _____ taxes pay for Social Security, Medicare, and unemployment compensation programs.
6. When people with smaller incomes pay a larger percentage of their income in taxes than do people with higher incomes the tax is _____.
7. Taxes on the manufacture, transportation, sale, or consumption of goods and the performance of services are called _____ taxes.
8. Customs duties, tariffs, or import duties are taxes levied on _____.
9. Customs duties protect the nation's industry, business, and agriculture from _____.
10. A high customs duty that makes foreign goods less competitive compared to American goods is called a _____.
11. Before the income tax was utilized, _____ provided a significant source of federal income.
12. A tax on the assets of a person who dies is called an _____ tax.
13. A _____ tax is a tax on money in excess of \$10,000 received from a living person.
14. People who believe that provisions favoring certain groups are unfair often call these exemptions _____.
15. Congress passed the Tax Reform Act of 1986 in order to reduce or end a confusing variety of tax _____, tax _____, and tax _____, as well as the number of tax _____.
16. Tax credits to people in lower income brackets allow them to reduce their _____ liability.
17. Government securities are financial instruments that include _____, _____, and _____.
18. The total accumulated amount the federal government has borrowed is the _____.

Guided Reading Activity 20-2



Preparing the Federal Budget

★DIRECTIONS Use the information in your textbook to complete this chart on the federal budget.

STEPS IN PREPARING AND PASSING THE FEDERAL BUDGET

Step 1:

Step 2:

Step 3:

Step 4:

Step 5:

Step 6:

★DIRECTIONS Use the information in your textbook to match the terms in Column A with the definitions in Column B. Write the correct letter in the space provided.

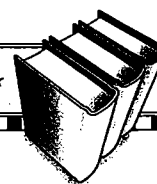
Column A

- _____ 1. federal fiscal year
- _____ 2. Budget and Accounting Act of 1921
- _____ 3. Office of Management and Budget
- _____ 4. Council of Economic Advisers
- _____ 5. uncontrollables
- _____ 6. entitlements
- _____ 7. Congressional Budget Act of 1974
- _____ 8. Balanced Budget and Emergency Deficit Control Act (GRH)
- _____ 9. reconciliation
- _____ 10. incrementalism

Column B

- A.** the group that confers with the president on budgetary matters
- B.** benefits that Congress provides by law, including Social Security, government pensions, Medicare, Medicaid, and veterans' benefits
- C.** law aimed at forcing the president and Congress to work together to reduce federal budget deficits
- D.** a 12-month accounting period that extends from October 1 of one year to September 30 of the next year
- E.** a term that refers to each year's budget changing only a little from one year to the next
- F.** made the president responsible for directing the preparation of the budget and making major decisions about budget priorities
- G.** a process whereby House and Senate committees adjust spending and taxing plans to fit existing programs
- H.** analyzes the nation's economic situation and gives the president the first set of budget figures
- I.** expenditures required by law or resulting from previous budgetary commitments
- J.** set up House and Senate Budget Committees and the Congressional Budget Office

Guided Reading Activity 20-3



Managing the Economy

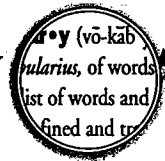
★DIRECTIONS Use the information in your textbook to complete these sentences.
Circle the letter of the correct answer.

1. The government spends \$2 trillion a year on four major programs: direct benefit payments to individuals, national defense, discretionary spending, and
 - A. foreign aid.
 - B. interest on the national debt.
 - C. the space program.
2. In a recent year, payments for Social Security benefits totaled
 - A. \$50 billion.
 - B. \$150 billion.
 - C. \$350 billion.
3. Grants to states and localities include money for road repair, public housing, police equipment and training, and
 - A. national defense.
 - B. parks and greenways.
 - C. school lunch programs.
4. Fiscal policy involves using government spending and taxation to influence
 - A. foreign governments.
 - B. the economy.
 - C. stockholders.
5. Monetary policy involves controlling the supply of money and
 - A. credit.
 - B. exports.
 - C. imports.
6. If the government needs to stimulate the economy, it spends more money than it takes in or
 - A. reduces taxes.
 - B. increases taxes.
 - C. reduces spending for entitlements.
7. The sum of all goods and services produced in the nation for a year is known as the
 - A. IRA.
 - B. FCC.
 - C. GNP.
8. The Federal Reserve System controls the money lent to
 - A. science and technology companies.
 - B. other banks.
 - C. foreign countries.
9. The group that controls the largest share of total bank deposits in the United States is
 - A. member banks in the Federal Reserve system.
 - B. the House and Senate.
 - C. private enterprise.
10. Members of the Federal Reserve Board are independent of Congress and the president in order to
 - A. raise or lower spending by the federal government.
 - B. control the amount of money that flows to states and localities.
 - C. make economic decisions without political pressure.

★DIRECTIONS Use the information in your textbook to complete this diagram.

How the Federal Reserve System Controls United States Monetary Policy				
Major Responsibilities		Tools Used for Control		

Vocabulary Activity 20



Taxing and Spending

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DIRECTIONS → Complete the crossword puzzle by spelling out the term defined by each clue.

dependent	reserve requirement	taxable income	incrementalism
securities	taxes	entitlement	monetary policy
uncontrollable	fiscal year	national debt	

Across

1. An expenditure required by law or resulting from a previous budgetary commitment
3. The accounting period that extends from October 1 of one year to September 30 of the next year
4. A way to influence the economy by controlling the supply of money and credit
6. Financial instruments that include bonds, notes, and certificates
8. The total accumulated amount that the government owes as a result of borrowing
9. The idea that generally, the national budget changes only a little from one year to the next
10. One who relies primarily on another person for things such as food, clothing, and shelter
11. A benefit provided by law to individuals

1.							2.												
							3.												
							4.												
5.																			
							6.												
							7.												
							8.												
							9.												
							10.												
							11.												

Down

2. The percentage of a member bank's total money which must be kept in the Fed
5. Total earnings of an individual minus certain deductions and personal exemptions
7. Payments by individuals and businesses to support the activities of the government

★ ★ ★ ★ ★ ★ ★ ★ ★ ★ ★ ★ ★ ★ ★ ★

DIRECTIONS → Use the following terms correctly in complete sentences. More than one term can be used in each sentence. Write the sentences on a separate sheet of paper.

fiscal policy	gross national product	discount rate	open-market operations	withholding
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Reteaching Activity



Taxing and Spending

DIRECTIONS

Complete the diagram related to the raising and spending of money by the federal government. Write the answers on the line in each box.

The federal government raises money with these six kinds of taxes:



Number the steps in sequence for preparing the federal budget:

- ___ **A.** The president makes decisions about the impact of the preliminary budget on the administration's general economic policy and goals.
- ___ **B.** Changes from reconciliation process are put into a bill that both houses must approve.
- ___ **C.** The president returns his decisions to the agencies.
- ___ **D.** Each federal agency draws up spending plans and sends requests to the OMB.
- ___ **E.** The OMB submits a complete budget document to the president for final review and approval.
- ___ **F.** The OMB issues a final report and may make cuts if needed to fit deficit-reduction targets.
- ___ **G.** The president's budget is printed and formally sent to Congress.
- ___ **H.** The House passes an appropriations bill.
- ___ **I.** The OMB and the agency heads negotiate cuts and additions to budget plans.
- ___ **J.** House and Senate budget committees review major features of the president's budget proposals, then prepare a concurrent resolution.
- ___ **K.** The director of the OMB takes the figures and an analysis of the economy to the president.
- ___ **L.** House and Senate committees fit the concurrent resolution with existing programs.



Most of the federal government's money is spent in these four areas:



The federal government primarily uses these two devices to control the economy:



The Federal Reserve System uses these three main tools to control the nation's financial policies:

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CHAPTER SUMMARY Activity



Taxing and Spending

★DIRECTIONS Match each term in Column A with the statement that best applies to it in Column B. Write the correct letters in the spaces provided.

COLUMN A

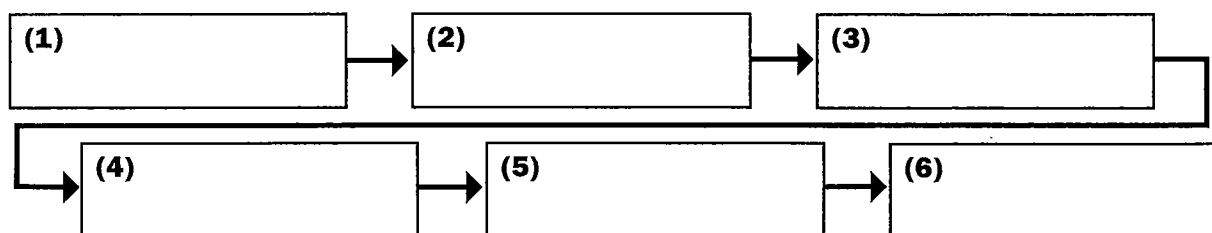
- _____ 1. taxable income
- _____ 2. social insurance taxes
- _____ 3. excise taxes
- _____ 4. estate taxes
- _____ 5. loopholes
- _____ 6. Gramm-Rudman-Hollings (GRH)
- _____ 7. fiscal policy
- _____ 8. monetary policy
- _____ 9. Federal Reserve System
- _____ 10. discount rate

COLUMN B

- A. Levied on the assets (property and money) of a person who dies
- B. Pay for programs such as Social Security and Medicare
- C. The government influences the economy through control of the money supply and credit
- D. Every budget item must automatically be cut if the president and Congress cannot agree on reductions
- E. The interest rate that the Federal Reserve System charges banks for loans
- F. The total income of an individual after certain deductions and personal exemptions are subtracted
- G. Special exemptions in tax laws that favor specific groups
- H. Levied on the manufacture, transportation, sale, or consumption of many goods and services
- I. The central banking system of the United States
- J. Taxation and spending used to influence the economy

Organizing Information Write each step in the correct order on the flow chart.

FEDERAL BUDGET PROCESS



- concurrent resolution
- appropriations bill
- OMB/agency negotiations
- president's guidelines
- reconciliation bill
- initial agency spending plans

Critical Thinking Answer the following question on a separate sheet of paper.

11. How do you think banks and consumers might react if the Federal Reserve System lowers the prime interest rate?