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By

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The Kentucky State Budget
System

By

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and

VERA BRISCOE, *Research Associate*

Bureau of Business Research



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EDITORIAL NOTE

This monograph reports the results of another investigation in the Bureau of Business Research series in financial administration. As in the case of other related publications, the primary purpose is to discover means of improving financial practice, that is, of finding out how limited finances may be used to secure the greatest possible public service. This end should be achieved by direct assistance to state officials and by diffusing more widely among the citizenry a knowledge of the purposes and procedures of financial planning and management. The Bureau hopes that this study will directly aid public officials and employees and give the people of the commonwealth more insight into the operations of their state's agency for fiscal control.

The Bureau initiated this analysis early in 1944. Mr. Martin planned the work and defined its scope. Under his direction Miss Briscoe did the original research and drafted the report. Mr. Martin, with Miss Briscoe's close collaboration, refined the manuscript and prepared it for publication.

The writers are indebted to Mr. Frank D. Peterson, former Director of the Division of Accounts and Control, Kentucky Department of Finance, and now Comptroller of the University of Kentucky, and to Mr. Warren M. Van Hoose, present Director of the Division of Accounts and Control and Assistant Budget Director, Kentucky Department of Finance, both of whom generously supplied information and both of whom offered valuable suggestions after reading a draft of the manuscript.

JAMES W. MARTIN, *Director*
Bureau of Business Research

August, 1945

THE KENTUCKY STATE BUDGET SYSTEM

CHAPTER I

INTRODUCTION

The adoption of a budgetary system is basic to an efficient and economical management of public affairs. Few public administration authorities would dissent from the statements that no government can have an efficient execution of public activities unless it has developed an efficient financial system through which the activities of the government are fed and that no financial system can prove satisfactory if it is not based securely on what is known as a budget.

A promiscuous use of the word "budget" makes a precise definition of the term difficult. The word has been loosely applied to everything and every phase of the budget reform process. Many writers have identified a budget with a collection of papers showing the estimated expenditures and revenues, or what is more properly called the "budget document;" others have made it synonymous with a revenue or appropriation act. "Budget," as used throughout the following pages, corresponds to neither of these conceptions.

The Kentucky statute defines the budget as "the *complete financial plan* for each fiscal year as proposed in the budget report and modified and adopted by means of the appropriation and revenue acts" (italics supplied).¹

The essence of a budget is that it is a financial plan; it is a government's work program translated into terms of dollars and cents. Budgeting embraces both planning future public activities and executing these plans. The President of the United States in his budget message of 1941 gave this description:

"The Budget of the United States Government is a statement that reflects in money terms what the Government does for the people and what the people contribute to the Government.

"In these figures over a course of years are mirrored

¹ Act 1934, chap. 25, art. 1, sec. 2(c); *Kentucky Revised Statutes*, 1944 (hereinafter these statutes will be referred to as KRS), sec. 45.010(3).

the changing attitudes of the people toward the growing needs which they expect their Government to meet. . . ."

A government's plan of action involves, in a broad sense, deciding what portion of the citizens' income is to be spent collectively and how it is to be spent. The budget has the same objective in planning and administering public finance policy as it has in private finance, that is, getting the most value from the dollar, in this case the tax dollar.

The *budget system* is the continuous chain of operations and procedures by which the financial plan, or budget, is formulated, adopted, and put into action. The *budget document* is the collection of statements which presents the plan in a printed form. Budget systems as they operate today did not spring into existence full grown, but they have evolved gradually and have expanded with changing conceptions of the responsibilities of government. If a budget had existed 150 years ago, it would have been a small one; and the budget system would have had a narrow range of activities to cover, consistent with the precept that "that government is best which governs least." That conception no longer obtains, and budget systems now seem to operate under a philosophy of "that government is best which serves most." Certainly, government today extends to its citizens not only more protection but more service than it did a century ago.

As the title indicates, this study concerns the Kentucky state budget system. The primary objective is to describe and evaluate the operations of the present system. An attempt is made at different points to appraise budgeting in Kentucky with a view of determining whether it is rendering maximum service to the governors, their administrative officials, the legislatures, and the citizens of the state themselves in designing and executing the work program of the state. One method of appraisal is to indicate the progress which has been achieved in budgeting practice by summarizing the changes in the procedure from the time of the adoption of the first budget law in 1918 up to the present. Authoritative literature on budgeting provides another basis of evaluation. Finally, the Kentucky system is compared in some instances with practices and experience in the federal govern-

²*The Budget of the United States Government, for the fiscal year ending June, 1941, p. v.*

ment and in other states, since an important yardstick for any one government unit is the achievement of other government units. In short, this study is concerned with the budgetary process rather than with the budgetary product in terms of dollars and cents. It is concerned with administrative practices, not with the financial results of these procedures.

CHAPTER II

THE DEVELOPMENT OF THE KENTUCKY BUDGET SYSTEM

For the first century and a quarter of Kentucky's independent existence the state's financial management was decidedly unsystematic. Not only was financial planning largely lacking but so also were means of effectuating orderly control over current revenue and expenditures. As in many other states, the Kentucky¹ legislative body did not vote appropriations for each agency at every regular session, but permitted expenditures on blanket authorizations often many years old.² This method continued as the principal one employed in Kentucky until 1934.³ Under the policy of setting apart special revenues the various items of expenditure included in the cost of government were usually financed in three ways: (1) Certain functions were provided for by dedicating certain taxes, or portions of general taxes; (2) departments or functions of a regulatory or public service character were authorized to exact fees or other charges and to use the revenues so derived for their own support; and (3) the general or administrative cost of government, as well as smaller expenditures of a miscellaneous character, were provided for currently by appropriations from any funds in the treasury not otherwise appropriated.⁴

THE PRE-BUDGET PERIOD

Financial practices prior to budgeting

The early fiscal practice of the Kentucky state government is not surprising in the light of contemporary federal usage. Our national government at the turn of this century was the only

¹ It appears that Kentucky was neither better nor worse than the average state in the matter of financial management. Cf. William Franklin Willoughby, *The Movement for Budgetary Reform in the States, 1918*, *passim*.

² A. E. Buck, *Public Budgeting, 1929*, p. 11.

³ In 1934 several of the state's largest revenue-raising taxes were diverted from apportionment to specific revenue funds to the general fund. See pp. 23, 24.

⁴ Report of the Efficiency Commission of Kentucky, *The Government of Kentucky, 1924*, p. 68.

great nation without a budget system.⁵ Congress raised and voted in a more or less haphazard manner the many millions of dollars required annually to operate the federal government. The basic defect in the pre-budget practices was a failure to consider the problem of financing government activities as a whole. The lack of a prepared plan which would shape and control policies of action was evidenced in the federal procedure in numerous ways. In the first place, the estimates of expenditures were prepared by the heads of the various spending agencies without adherence to any uniform principle. The Secretary of the Treasury was required to compile the departmental requests in a so-called "book of estimates;" but he was merely a compiling authority and had no power to modify the proposals transmitted to him by the heads of the administrative departments, who, indeed, often submitted modified estimates at a later date and lobbied with the committees of Congress until they were approved.⁶ The President could exercise his general powers to secure a coordination of the estimates and their conformity to a general policy, but he had no staff through which he could effectively exercise the authority.⁷ There was neither a uniform system of accounts which would produce information needed to devise a financial plan nor an agency to utilize the information if it had been available; no standard expenditure classification by units of organization, functions, or activities, or according to character and object had been officially adopted.⁸ Procedures were irregular with respect to getting before Congress statements of financial needs of the government, and congressional treatment of estimates disintegrated still further the process of making appropriations. Neither house made any effort to review the expenditure and revenue estimates together. In fact, the book of estimates was split up and parceled out to numerous committees in each house. At one time eight distinct committees in the House of Representatives, each acting independently of the others, reviewed what were known as the general appropriation bills; if a department were refused an appropriation by one

⁵ A. E. Buck, *The Budget in Governments of Today*, 1934, chap. 2, and *op. cit.*, p. 10.

⁶ William Franklin Willoughby, *The Problem of a National Budget*, 1918, pp. 55, 56, and *The National Budget System*, 1927, pp. 4-12.

⁷ *Loc. cit.*

⁸ *Loc. cit.*

committee, it sometimes applied to another for the same item and not infrequently met with success.⁹ Under these circumstances it can be readily seen that both administrators and legislators failed to sense the significance of formulating a comprehensive plan of financing, of comparing expenditures of one agency with those of another in the light of estimated revenues, or vice versa; of determining the relative merits of the demands on the treasury; and of coordinating the various activities of government to prevent duplication. Responsibility for the success, or lack of it, of the voted appropriations in fulfilling financial needs could be attributed to no one except for the indefinite, general responsibility always attaching to Congress as a body.

The laws governing the assignment of revenues to funds in Kentucky were involved and numerous. Many provisions seemed to be inspired by the belief that to provide funds without assigning them to a designated purpose would be contrary to good practice, a policy which is irreconcilable with the budget idea of planning expenditures periodically. To illustrate the complexity of the system of determining the amounts to be expended on particular activities, the following law is quoted:

"An annual tax of forty (40) cents upon each one hundred dollars (\$100) of value of all property directed to be assessed for taxation, as herein provided, shall be paid by the owner, person or corporation assessed. Of the aggregate amount of tax realized by all assessments under this forty (40) cent rate, fifteen cents shall be for the use of the ordinary expenses of the government, eighteen cents for the support of the common schools, one cent for the use of the sinking fund, one and three-quarter cents for the support and erection of buildings for the University of Kentucky at Lexington, five-eighths of one cent for the support and erection of buildings for the Eastern State Normal School located at Richmond, five-eighths of one cent for the support and erection of buildings for the Western State Normal School located at Bowling Green, and three cents for the State road fund, and the Auditor of Public Accounts will make distribution of said tax in accordance with the said apportionment at the end of each month. . . ."¹⁰

This example describes the allocation of the property tax revenues only; other taxes were distributed according to varying formulas. In addition certain revenues and receipts, such as fees, sales of materials, interest, contributions, etc., were credited

⁹ Willoughby, *The National Budget System*, op. cit., p. 14.

¹⁰ 1918 Supplement to *Carroll's Kentucky Statutes*, 1915, sec. 4019.

directly to a departmental fund to be spent by the agency receiving the same. Any revenues not specifically dedicated were considered a part of the general fund, available for legislative appropriations.

An apparent purpose of this method of financing was to reduce the labor and responsibilities of current financial administration to the minimum. However, trying to minimize effort in administering the finances had unfortunate results. The finances proceeded according to the formula of apportionment set down by law, producing surpluses here and deficits there. There was no annual or biennial summing up of resources and adjustments of expenditures taking place in order to make every dollar go as far as possible and to see that none of the money was spent extravagantly.

Kentucky not only failed to plan expenditures in advance, but the state also lacked proper organization for controlling expenditures. In the first place, the Treasury Department did not have custody of all the state's cash. Although a number of departments and institutions made use of the Treasury, numerous agencies maintained their own treasuries and their own bank accounts.¹¹ This disintegration not only made the problem of supervision and auditing a more difficult one because the institutional accounting staff and the State Treasurer kept separate books and documents, which did not always correspond; but it also meant that miscellaneous income could be retained and spent without authorization.

Second, there was no unified control over the finances. Six principal offices, working independently of each other, had important duties in connection with financial administration. These were:

1. The Office of the Auditor of Public Accounts, which kept one set of state accounts, issued warrants for the payment of claims, prepared receipts for money paid into the

¹¹ Efficiency Commission of Kentucky, *op. cit.*, pp. 57, 58 reported in 1924 the following state agencies which maintained independent treasuries: University of Kentucky, Western Normal School, Eastern Normal School, School for the Deaf, School for the Blind, Western Kentucky Industrial College, Kentucky Normal and Industrial Institution for Colored Persons, Confederate Home, Department of Health, and several smaller units like the State Board of Accountancy. Although this report relates to a date later than the period under discussion, it is apparent from the language of the report that a similar, and possibly worse, situation prevailed at an earlier period.

Treasury, audited settlements of county officers sent in to the capitol, and performed other related duties.¹³

2. The Office of the State Treasurer, which kept another set of state accounts, had custody of the funds of the commonwealth, and had control over the actual drawings from the state depositories.¹⁴

3. The Office of the State Tax Commission, which had general supervision over the assessment and collection of many of the important revenues of the state, including supervision over the local assessment of property taxes.¹⁵

4. The Office of the State Inspector and Examiner, which was required to audit the Auditor's and Treasurer's accounts once a year and investigate them monthly and was authorized to investigate the conduct of any other officer of the state who received state monies or managed or controlled any state property.¹⁶

5. The Office of the Governor, which had general responsibility for seeing that the work to be done by the other state officers was properly performed.¹⁷

6. The Office of the Sinking-Fund Commission, which was responsible for handling the transactions necessitated by the bonds of the commonwealth and for installing a uniform system of accounting and reporting.¹⁸

The budget idea is very nearly the exact opposite of the system just described. In the first place, the budget is a *plan* of expenditures aiming to appropriate only for needs that are clearly demonstrated to exist and to make no money available before the needs have been thoroughly examined. Second, a budget system aims to give control of the resources to those to whom such control properly belongs, namely, the representatives of the people, by means of a periodical review of expenditures and revenues. At the same time the budget system lodges control in the representative assembly, it aims to place definite responsibility upon each administration to plan and manage the finances for each fiscal period, so that money available may be used to the greatest possible advantage in meeting current demands on the treasury within the limits prescribed by the General Assembly.

Development of the budget concept

In the first decade of the twentieth century the machinery of administration was not a subject of popular interest, and the

¹³ Carroll's Kentucky Statutes, 1915, secs. 143 et. seq.

¹⁴ Carroll's Kentucky Statutes, 1915, secs. 4686-4688, 4697.

¹⁵ 1918 Supplement to Carroll's Kentucky Statutes, 1915, secs. 4114-11

et. seq.

¹⁶ Carroll's Kentucky Statutes, 1915, secs. 4623, 4630.

¹⁷ Kentucky Constitution, sec. 81.

¹⁸ Carroll's Kentucky Statutes, 1915, secs. 4592 et. seq.

word "budget" was seldom used by the American people. It had no news value in itself; but other stories of the rising tax rate, money wasted, the rapid rise in the cost of government, and abuses of public officials did attract the attention of the press and the public. So it was that the results of slipshod and systemless financial practices set a few individuals to thinking in terms of administrative reform and a budget—a budget as a means of holding officers accountable for their actions, a budget as a means of telling the people in advance why money was wanted, a budget as a means of planning for services and locating responsibility for the plans, a budget as a community program to be financed.¹⁸

At this stage in the development of public interest bureaus of municipal research were organized to study the financial procedure, organization, and management of city governments.¹⁹ The oldest of these, the New York Bureau of Municipal Research, established in 1906, immediately inaugurated a study of local budgetary needs.²⁰ The campaign generally spread from the cities to the national government and from there to the states. Perhaps the largest single contribution to the promotion of public interest in the budget system was made by President Taft's Commission on Economy and Efficiency. This notable Commission, composed of five experienced authorities, was organized in 1910 under the chairmanship of Frederick A. Cleveland of the New York Bureau of Municipal Research.²¹ One of its most important inquiries resulted in a report, "The Need for a National Budget," which President Taft sent to Congress with a message of approval in 1912, the first occasion that any responsible officer of the national government had advocated the budget idea.²² The Commission also went so far as to prepare a budget for the President to submit; but both the report and the budget went no further than the committee on appropriations,

¹⁸ Frederick A. Cleveland and A. E. Buck, *The Budget and Responsible Government*, 1920, p. 75.

¹⁹ A. E. Buck, "The Development of the Budget Idea in the United States," *Annals of the American Academy of Political and Social Science*, May, 1924, p. 31; Frederick A. Cleveland, "Evolution of the Budget Idea in the United States," *Annals of the American Academy of Political and Social Science*, Nov., 1915, p. 32.

²⁰ Buck, *loc. cit.*

²¹ *Ibid.*, p. 32.

²² *House Documents*, 62nd Cong., 2nd sess., 1911-1912, vol. 118, doc. 854; and Cleveland, *op. cit.*, pp. 26, 27.

largely because the President had lost much of his support in Congress.²³ However, the work of the Taft Commission had far-reaching effects on the states. This report, fiscal reform organizations, certain local financial conditions, and far-sighted leadership favored improved financial planning. So several of the state legislatures began making studies of their administrative methods and considering budget systems as a means of improving the management of government finance.

Although Kentucky was not the first state to adopt a budget plan, it was not the last.²⁴ In 1918 in the following message Governor A. O. Stanley recommended that the legislature enact a budget law:

"The new tax system bids fair to raise sufficient revenue to meet the current expenses of the State and to afford a balance for a sinking fund, to be applied in the liquidation of the State's existing indebtedness. In order that this income may be economically and judicially expended, a budget system should be inaugurated without delay. . . .

"The General Assembly cannot very well estimate the expenses of the Commonwealth under our present methods of making expenditures. The General Assembly should have before it at each regular session a complete list of all acts providing for the payment of money from the treasury of the State. The needs of the various institutions and departments of the government may not remain the same from year to year. If the legislature should assemble all acts appropriating money into one act and re-enact such law with such changes as might be necessary at every regular session, the General Assembly could intelligently estimate the expenses of the Commonwealth and fix the tax rate for each fiscal year. . . . Under this plan the General Assembly could have control over the expenditure of the public funds of the State and could economize by reducing appropriations so as to bring them within the estimated revenue when such step might be found necessary."²⁵

In the same year Senator J. W. Harlan introduced an act creating a Budget Appropriation Commission and providing for a budget method of ascertaining the expenditures of the various agencies of the state government.²⁶ The act passed in both the House of Representatives and the Senate with practically no negative votes.²⁷

²³ Willoughby, *op. cit.*, pp. 22, 23.

²⁴ Twenty-three states enacted budget laws prior to 1918. Cf. Cleveland and Buck, *op. cit.*, p. 124.

²⁵ *House Journal*, 1918, vol. 1, p. 36.

²⁶ *Senate Journal*, 1918, vol. 1, p. 68.

²⁷ The vote was 75, affirmative, and 2, negative, in the House and 26, affirmative, in the Senate. *House Journal*, 1918, vol. 2, pp. 1327, 1328; *Senate Journal*, 1918, vol. 1, p. 423.

THE FIRST KENTUCKY BUDGET LAW

*Provisions of the 1918 act*²⁸

The first provision of the budget law was one creating a Budget Appropriation Commission composed of the Governor as chairman, the chairman of the State Tax Commission, and the State Auditor, all of whom served without additional compensation. The Commission had but one function, namely, the preparation of budgets and the drafting of appropriation bills—both for submission to the General Assembly.

To accomplish its purpose, the law required the various offices and departments receiving or expending state money to file statements of receipts and disbursements for the two preceding fiscal years and estimates of expenditures required and of revenues expected for the next two ensuing years with the Budget Commission on January 1 of each year in which the General Assembly convened. The estimated receipts were to be shown by "source" and the estimated expenditures by "purpose" as follows (however, a different classification could be prescribed by the Commission): salaries, maintenance and operation, supplies, repairs, and permanent improvements. The heads of each of the spending agencies were designated as the responsible officials to compile these statements, except that the State Auditor filed the statements of the legislative and judicial branches. Likewise on the first of January of every other year the State Treasurer furnished the Budget Appropriation Commission with a summary of the financial condition of the state as of the end of the last fiscal year, showing the total amount of receipts and expenditures of the Treasury Department, total state debt, sinking fund requirements, and an estimate of income for each year of the ensuing biennium. The Commission met on or before the fifth of January of the assembly year and continued meeting until a budget report was prepared. In examining the statements submitted by the spending agencies the Commission could avail itself of the assistance of the State Inspector and Examiner, who had power to subpoena witnesses and who, because of his other duties, was familiar with the operations and conditions of the various departments.

²⁸ Acts 1918, chap. 12.

The Commission submitted the result of its work in the form of a report with accompanying appropriation bills, one for each of the fiscal years next ensuing, to the General Assembly before the third Monday of its session. These dates indicate that the whole task of budget preparation was consummated in the period of less than a month. In the event of failure of the Assembly to pass appropriation bills in any year, the law authorized expenditures on the basis of the preceding year's appropriations until new appropriations were made.

Limitations of the law

Although the budget law of 1918 indicated that Kentucky had expressed approval of the budget idea of periodically planning and reviewing the finances of the state, in actual fact the law failed to accomplish the management of its finances according to a budget plan, first, because it left the resources tied up under the statutory apportionment scheme, second, because it made no provision for controlling expenditures according to "budgeted" appropriations, and third, because it failed to develop the budget staff sufficiently so that it could effectively bring in information and control expenditures.

For the year ending June 30, 1923, the gross revenues of the state amounted to approximately \$21 million; of this amount over \$13 million was automatically set apart by prior legislation into six major special funds, leaving a balance of less than \$8 million in the general fund to which the budget in reality applied.²⁹ And even in the general fund there were several minor special accounts consisting of revenues which were available only for certain uses as already prescribed by the statutes of prior years.³⁰ But this is not the whole story; the \$21 million gross revenues mentioned above comprised only such revenues as were taken into the Treasury with the receipts of departments and institutions which were not reported to the Auditor and deposited with the State Treasurer wholly unaccounted for. It is apparent that in essence the new budget procedure fulfilled just the function of the old annual appropriation act, providing for the general and miscellaneous expenses of government, and no more.

²⁹ Efficiency Commission of Kentucky, *op. cit.*, pp. 70, 71.

³⁰ *Loc. cit.*

No mention was made in the law of a scheme of allotting appropriations, keeping a budget ledger, or otherwise providing methods of controlling expenditures. The old system of submitting claims to the Auditor of Public Accounts, who issued warrants to the State Treasurer for their payment, continued without alteration. So far as spending agencies were concerned, the new "budget system" meant only that they were required biennially to submit certain information to the Budget Commission; and after appropriations were made, they proceeded under the old methods.

The plan followed in the 1918 law was that of having a commission of three administrators responsible for the preparation of the budget. Although most budget authorities writing in the early period of budget development had advocated making the chief executive the responsible official for preparing the financial plan,³¹ several of the first state laws, like Kentucky's, did not recognize the need for gubernatorial leadership.³² The membership of administrative officials on the Kentucky Commission indicates that the framers of the law had the idea of an executive budget system, for such a system is based on leadership by executive officials. However, a commission form of budget-making authority makes for divided and hence dissipated responsibility. The personnel of the Budget Commission was not suitable for the supervision of the budget machinery. Arguments could be readily advanced for obtaining the advice of the Auditor of Public Accounts, the principal financial officer of the state, and of the chairman of the Tax Commission, the principal revenue officer, in preparing the budget; but whatever

³¹ Cf., for example, Buck, *loc. cit.*; Cleveland and Buck, *op. cit.*, pp. 126-129; Cleveland, *op. cit.*, pp. 71 ff.; S. Gale Lowrie, "The Proper Function of the State Budget," *Annals of the American Academy of Political and Social Science*, Nov., 1915, p. 49; Emerson C. Harrington, "The Executive Budget," *Proceedings of the Governor's Conference*, 1916, pp. 25 ff.; Rufus E. Miles, "The Budget and the Legislature," *Annals of the American Academy of Political and Social Science*, Nov., 1915, pp. 42-44; Willoughby, *The Movement for Budgetary Reform in the States*, *op. cit.*, p. 182 and *The Problem of a National Budget*, *op. cit.*, pp. 30, 31. Edward A. Fitzpatrick, *Budget Making in a Democracy*, 1918, *passim* was one outstanding authority who endorsed preparation of the budget by the legislature. For a summary of a debate on the relative merits of an "executive budget" and a "legislative budget" see Frederick P. Gruenberg, "The Executive vs. the Legislative Budget," *National Municipal Review*, Mar., 1918, pp. 167-173.

³² Seven of the first twelve laws enacted in 1911 and 1913 fixed responsibility for preparation of the budget plan either upon a board or commission or upon the legislature. Cleveland and Buck, *op. cit.*, p. 124. It may be significant that under Kentucky's 1918 law two of the three Budget Commission members were the Governor and his appointee, the Chairman of the State Tax Commission.

information these officers could give could be completely set forth in typewritten statements without conferring upon them equal authority with the Governor in making decisions upon the estimates. It was, according to the Efficiency Commission of Kentucky, "practically a farce for the heads of great departments like Roads, Education, Charities, and Health to have to bring their requests to the Auditor of Public Accounts and the chairman of the Tax Commission."³³

One of the most serious faults of the first budget law was failure to provide for adequate staff assistance. It is impossible for anyone who is at all familiar with the difficulties of budget making to imagine a successful budget without a staff to handle the problems of form and content and to do investigational work. The Kentucky law not only failed to make provisions for such a staff, but also stipulated that no extra clerical expenses incident to the work of preparing the budget report could be incurred. The Commission served without additional compensation, and its members were aided only in that they could direct the State Inspector and Examiner to make investigations for them.

Administration of the act

After the budget act was passed, it would have been possible to develop forms and procedures supported by a more or less adequate accounting system which would have produced the information necessary for the control of state finances *within* the limits of control covered by the budget. Moreover, by the development of the budget within its legal limitations it should have been possible to present clearly and convincingly the difficulties under which the system labored and possibly to have obtained relief from some of these limitations. Apparently, none of this was done; the duties imposed upon the Budget Commission were performed in the most perfunctory manner.³⁴

A first essential in producing a budget report is the compilation of some general statements, summarizing revenues, expenditures, treasury conditions, indebtedness, and all other elements entering into the financial situation, for use in laying out a financial program for the ensuing year. In the report of the Budget Commission relative to the years ending June 30, 1923,

³³ *Op. cit.*, p. 77.

³⁴ *Ibid.*, p. 73.

and June 30, 1924, the only statement of a general character was a brief one of 1921 treasury receipts and disbursements and outstanding warrants, as compared with the "probable amount of revenue" and "approximate need of revenue" for the fiscal years ending in 1923 and 1924.³⁵ Except for a reference to the omission of federal grants the statement gave no indication of what was included in the revenue estimate figure; it wholly ignored the special fund problem and so opened the way for the grossest sort of misconception; there was no suggestion as to what functions the expenditure estimate figure covered.³⁶ As a summary statement it was not only inadequate but misleading. The law required the State Treasurer to supply the Budget Commission with information concerning the state's financial condition. However, both his accounts and those of the Auditor of Public Accounts recorded only cash receipts and disbursements, and not transactions at the time obligations were incurred.³⁷ Furthermore, no appropriation accounts were kept in the Auditor's office.³⁸ In short, the accounting system was not geared to produce the essential information upon which to build the budget plan.

The detailed schedules of estimates were not much more helpful than the general summary statement, since they failed to differentiate between expenditures from special funds and from the general fund, failed to classify requests as prescribed in the law, and failed to recapitulate revenues according to source and fund.³⁹ In brief, the problem of obtaining detailed information that would materially assist the legislature in finally arriving at the correct amounts to appropriate was not solved, and probably could not have been completely solved without provision for a qualified budget staff to make an extended study of financial conditions and needs and without an accounting system to produce budgetary information. The Commission did not have the staff and did not take the opportunity to make the most of the State Inspector and Examiner's service, but instead the already

³⁵ *Ibid.*, p. 74. Also note that the two fiscal years were treated in the one statement despite the legal stipulation that a budget plan be prepared for each fiscal year of the biennium.

³⁶ *Loc. cit.*

³⁷ Conference with Mr. Warren Van Hoose, Assistant Budget Director, Kentucky Department of Finance, Sept. 6, 1944.

³⁸ Efficiency Commission of Kentucky, *op. cit.*, p. 162.

³⁹ *Ibid.*, pp. 75, 76.

overworked Assistant Auditor of Public Accounts was selected as the clerical assistant to the Budget Commission.⁴⁰

Kentucky, however, was not a singular example of state failure to install a thoroughgoing budget system. Mr. A. E. Buck, writing in 1924, said:

"Although several states have had budget legislation on their statute books for almost ten years, they have made very little progress in the direction of a real budget system, that is, one that makes for careful planning and establishes control over expenditures after appropriations have been authorized."⁴¹

His explanation of this lack of progress is much like that which applied to Kentucky, namely, the failure to spend enough time on budget work, lack of staffs to gather essential budget information, and the failure to recognize the budget as a complete plan.⁴²

REVISIONS MADE BY THE LAW OF 1926

*Contents of the law*⁴³

Two changes effected by the 1926 law indicate that the 1926 General Assembly was making an effort to correct the fundamental faults of the first budget law.

In the first place, an attempt was made definitely to center responsibility for the preparation of a budget plan upon some officer. The Budget Commission was retained, but the Office of State Budget Officer was created to perform all the duties relative to preparing a budget report. The State Inspector and Examiner was designated as the Budget Officer and made ex-officio secretary of the Budget Commission. In addition to preparing the budget report at the direction of the Commission, the Inspector and Examiner was required to enforce the provisions of the 1926 law and to make a regular investigation of all state offices. This latter requirement was obviously meant to make the budgeting procedure more than a biennial conference and to provide for studying the needs of the spending agencies to a fuller extent. The law on this point read:

"In addition to his duties as hereinbefore prescribed, the State Budget Officer shall make regular investigations

⁴⁰ *Ibid.*, p. 77.

⁴¹ "Progress in State Budget Making," *National Municipal Review*, Jan., 1924, pp. 24, 25.

⁴² *Loc. cit.*

⁴³ *Acts 1926*, chap. 170.

of all State offices. He shall report to the Governor on each and every budget unit at least once each year, and under the direction of the Governor, shall prepare the material for a report to the General Assembly concerning each budget unit for the use of the Governor. The Governor shall submit a full and complete report to the second session of the General Assembly during his administration as to the development, functions, organization, business methods, expenditures and operations of each budget unit and as to the State administration as a whole, together with any recommendations he may have for improvements in administration."⁴

The Budget Officer, however, had no vote on any matter which came before the Commission; his position was that of an advisor and of a staff assistant. He was required also to serve the General Assembly in the same capacity, for the law stipulated that:

"From the time of the submission of the budget to the General Assembly until the appropriation bills shall have been finally disposed of, the Budget Officer shall be at the disposal of the General Assembly or any of the appropriation committees thereof, and shall devote his entire time to the work of the appropriation committees under the direction of the respective chairmen."⁵

A second fundamental aspect of the 1926 law evidenced the recognition on the part of its framers of the need of setting up machinery to control expenditures to keep them within the bounds of the appropriations. The Auditor of Public Accounts was required to keep a budget ledger as a part of the records of his office. At the beginning of each fiscal year he was to credit the budget ledger with the funds set apart and appropriated by the budget appropriation act to each budget unit; all warrants thereafter drawn were to designate the budget fund from which the same were payable and the amount entered upon the budget ledger. The Auditor had no authority to issue a warrant in excess of any budget fund, and any warrants so issued were illegal. The Auditor also had the power to decide any issues as to the meaning of the terms used in the appropriation act, but the budget units could appeal to the Commission in cases of complete disagreement. The law was emphatic on the point that the terms and provisions of the budget and appropriation act should constitute binding limitations upon expenditures from the

⁴ *Acts 1926*, chap. 170, sec. 2.

⁵ *Acts 1926*, chap. 170, sec. 16.

treasury. Transfers between classes of expenditure for any one budget unit were permitted upon the written approval of the Budget Commission, and appropriations for contingencies and special items were made available only after approval by the Governor of the individual items of the proposed expenditures.

Other provisions designed to facilitate the budget procedure were: shifting back the date on which the estimates were submitted by the heads of the departments to November 15 of the assembly year and the date on which the Commission met to consider such estimates to December 21, in order to allow more time for preparation of the budget report; and stipulating in more exact language the contents of the budget document in order to assure its preparation in a useful form. It is interesting that the law required the Governor to "prepare recommendations as to each budget item for two fiscal years next ensuing, which shall be presented in the budget report presented to the General Assembly. . . ."46 although the Commission was retained in much the same capacity as the 1918 law.

"New wine in old bottles"

The 1926 budget law was adequately described by one administrator in these words, "The law had teeth in it, but it was like putting new wine in old bottles."⁴⁷ Continuation of the old scheme of assigning tax revenues to specific functions and permitting the retention of other receipts by the various budget units for their own use made the stipulation that no expenditures could be made except by virtue of an appropriation act a superficial one. Until the biennial appropriation act really appropriated money to the spending agencies according to a preconceived plan which took into consideration the relative needs, instead of appropriating according to an outworn formula of tax apportionment, the budget system could be no more than a half-way measure, which did not function in practice according to the theory of its purpose.

The control by the Auditor of Public Accounts over the expenditures was perfunctory. There was no carefully kept and adequate record of all financial transactions to exercise compul-

⁴⁶ Acts 1926, chap. 170, sec. 13.

⁴⁷ Conference with Mr. Warren Van Hoose, Sept. 6, 1944.

sion on the various departments and agencies to abide by the budget as adopted until after 1936. Prior to fiscal 1935, in fact, no budget ledger was kept; but instead the vouchers were merely filed as they came into the Auditor's office; to ascertain the charges against a particular budget fund at any given moment required adding all the vouchers filed under the fund up to that time.⁴⁸ Because there was necessarily some delay in the receipt and payment of bills for supplies after they had been ordered and because the status of a given fund was not readily accessible, purchase orders were often placed without available money to pay the bills.⁴⁹ When the warrants came to the Treasurer's office and there was no money on which to write a check, he stamped the warrant "interest-bearing," and it was returned to the claimant.⁵⁰ As a consequence of those conditions, the interest-bearing warrants outstanding against the state were over \$25 million by 1936.⁵¹

Finally, the State Inspector and Examiner could devote only a part of his time to the budget function. Although the creation of the post of State Budget Officer may have been an effort to assure adequate preparation of a budget report, which would be based on a thorough and continuous investigation of financial needs and practices according to sound budget theory, other duties of the State Inspector and Examiner consumed most of his time; and he could devote little attention to budget work.⁵² At any rate, budget recommendations based on an exhaustive study of departmental needs would have had "no teeth" as long as most appropriations resulted from tax allocation formulas.

In short, the 1926 law failed to reach to the roots of the difficulties embedded in Kentucky's system of fiscal administration. It superimposed a comparatively sound budget system upon a financial structure which prevented its effective operation.

⁴⁸ *Loc. cit.*

⁴⁹ *Loc. cit.* Also see Gov. A. B. Chandler, *Kentucky Government, 1935-1939*, p. 17.

⁵⁰ Conference with Mr. Frank D. Peterson, former Director of the Division of Accounts and Control, Kentucky Department of Finance, now Comptroller of the University of Kentucky, Oct. 18, 1944.

⁵¹ Commonwealth of Kentucky, *The Executive Budget, for the biennium 1940-42*, p. 47.

⁵² Conference with Mr. Warren Van Hoose, Sept. 6, 1944.

LEGISLATION OF 1934 AND 1936

The Budget and Financial Administration Act of 1934 and the Governmental Reorganization Act of 1936 are the two principal bulwarks of legislation under which the Kentucky budget system now operates. The functioning of the present system is developed at length in the subsequent chapters; the analysis of these two and related laws at this point serves to introduce the setting.

*The Budget and Financial Administration Act and the Administrative Reorganization Act of 1934*⁵³

The 1934 budget act embraced budgeting, accounting, pre-auditing, treasury administration, post-auditing, and fiscal reporting. It was a thoroughgoing reform in financial legislation, and it operated in conjunction with a nominally changed administrative structure.

(1) *Organization for financial administration.* On the face of the Administrative Reorganization Act of 1934, far-reaching change in the structure of the state government was effected. Purportedly financial administration was a good deal modified. The reorganization was rendered innocuous by the terms of the law however; for each pre-existing officer was directed to "exercise all the powers, duties, and functions now vested in his office by the Constitution and laws of the State . . ."⁵⁴

(2) *Budget legislation.* The 1934 budget act provided that the Governor, by and with the advice and assistance of the State Budget Officer and the Board of Finance, should prepare and submit a budget report presenting a complete financial plan for each fiscal year of the ensuing biennium to the General Assembly at each regular session. The act outlined the procedure to be followed in preparing the report and the contents of the document.⁵⁵

A system of allotments to distribute expenditure of appropriations over the entire fiscal period was installed; and a con-

⁵³ Acts 1934, chaps. 25 and 155.

⁵⁴ Acts 1934, chap. 155, art. 3, sec. 1, art. 4, sec. 1, art. 5, sec. 1, art. 6, sec. 1, art. 7, sec. 1, art. 13, art. 14, sec. 1, art. 19, art. 21, sec. 1, art. 22, sec. 1.

⁵⁵ Subsequent Chapters IV and V describe the operations of the law on this point in full.

control over the incurring of obligations was established by a method of pre-auditing purchase orders, payrolls, and other vouchers to ascertain whether they were legal and whether there was an allotted appropriation to cover the expenditure. The apportionment and pre-audit scheme is an elementary prerequisite to effective budget control, and the adoption of these methods in 1934 was a progressive step in Kentucky budget procedure. The successful operation of the allotment method necessitated introducing new methods of accounting. The law took note of this fact and directed the State Budget Officer to install a unified and integrated system of accounts for the state, exclusive of the accounts required to be maintained by the Auditor of Public Accounts, which were provided for under the provisions of the Budget and Financial Administration Act. However, although the Auditor set up a simple hand-kept budget ledger which greatly improved earlier procedures, an effective accounting system was not made a part of the state's financial structure until after 1936. The statute required current administrative reports to provide a measure of the amount and the tempo of the work done, as well as the efficiency of the various agencies, to be furnished to the Governor, the Board of Finance, and the budget units.

*The Governmental Reorganization Act of 1936.*⁵⁶

To change or not to change the existing structure of Kentucky state government was an important issue in the gubernatorial campaign of 1935. It was alleged that there had been a fake governmental reorganization in 1934, and candidate A. B. Chandler promised the people of Kentucky a reorganization "from top to bottom," which would result in economical management of the affairs of the commonwealth.⁵⁷ One of his early acts after election was to appoint an unofficial reorganization commission, the chairman of which was the Honorable J. C. W. Beckham, a former Governor of Kentucky.⁵⁸ The Commission worked closely with the General Assembly on the bill for reorganization, which produced the following results. The existing

⁵⁶ Acts 1936, 1st spec. sess., chap. 1.

⁵⁷ James W. Martin, "State of Kentucky Reorganizes its Finances," *The Tax Magazine*, May, 1936, p. 278.

⁵⁸ *Loc. cit.*

agencies and departments were consolidated into seven constitutional administrative departments—the Governor's Office, Department of State, Department of Law, Department of Treasury, Department of Agriculture, Labor, and Statistics, Department of Education, and Department of Military Affairs; ten statutory administrative departments—Department of Finance, Department of Revenue, Department of Highways, Department of Welfare, Department of Health, Department of Industrial Relations, Department of Business Regulation, Department of Conservation, Department of Library and Archives, and Department of Mines and Minerals; and six independent agencies—Auditor of Public Accounts, Legislative Council, Board of Election Commissioners, Railroad Commission, State Racing Commission, and Public Service Commission. The least desirable changes were the retention of the Department of Mines and Minerals, which might have been coordinated with the general Department of Industrial Relations, since both agencies performed functions of a regulatory nature pertaining to industrial relations, and the retention of an independent state school for the deaf at the same time that all other such institutions were integrated with some general administrative department.⁵⁹ In the process of integration, too, the act made use of the single-head administrator principle, except that in the cases of agencies having quasi-judicial or quasi-legislative functions, boards were created. Except for the offices supervised by elective officials, the departments were directed by the Governor's appointees according to the principle that the Governor should be responsible for managing the administration.

A pre-eminent place was given to the Department of Finance in the reorganization plan. Only the Illinois, Ohio, and a few other state plans approached the Kentucky scheme in the extent to which it assigned to the Department financial control over the work of the state administration.⁶⁰ The Department was legally set up for administrative purposes in four divisions to perform the functions of budgeting, accounting control, purchasing and managing public properties of the state, and personnel supervision. The old Board of Finance was superseded, and the

⁵⁹ *Ibid.*, p. 280. Subsequently the work of the State Department of Mines and Minerals has been somewhat extended.

⁶⁰ *Loc. cit.*

Division of the Budget in the new Department of Finance replaced the State Inspector and Examiner as the budget staff agency to assist the Governor in preparing and executing the budget plan according to the procedure adopted in the Budget and Financial Administration Act of 1934. Another contribution to sound budgeting made in 1936 was the provision for adequate record-keeping facilities. The Public Administration Service was employed by the Governor to install modern accounting mechanisms, such as machine posting, to replace the pen budget ledger used from 1934 to 1936.⁶¹

Under the new arrangement the Auditor of Public Accounts was no longer charged with comptroller functions. The reorganization gave him the status of a real post-auditor, so that after the term of the Auditor then in office he would review all financial transactions after they had been completed and report on their correctness to the Governor, the General Assembly, and the people.

It is fair to say that the governmental set-up after 1936 was, for the first time in Kentucky's history, such as not to impede effective administration of the public finances. The modernized structure for administering the finances in general and the accounting and budgetary control machinery in particular established the possibility of having good financial administration; however, these mechanisms could not guarantee smooth functioning. The next task was to utilize the techniques provided by the General Assembly to effect an efficient public finance operation in the state. The degree to which this has been done is discussed in the following chapters.

Changes in the disposition of revenue

The old system of apportioning tax receipts to specific functions was materially altered by 1934 legislation. The General Assembly in that year provided:

"The aggregate amount of State tax realized by the assessment made of and levied upon real estate, all assessments of franchise, shares of stock, money in hands, notes, bonds, accounts and other credits, whether secured by pledge, mortgage or otherwise, or unsecured, and the tax on bank deposits and upon shares of building and loan associations and upon funds realized from the collection of

⁶¹ *Loc. cit.*; Gov. A. B. Chandler, *loc. cit.*

inheritance tax levied in Kentucky and the aggregate amount of all other state revenue realized from every other source whatsoever, excepting operating receipts and/or revolving fund accounts . . . and further excepting the gasoline tax, automobile license, motor bus license, truck license and drivers' license, shall be credited to the General Fund for the use of the expenses of government."⁶³

This provision was fundamental in making the Budget and Financial Administration Act of value. In substance, it meant that the state adopted the policy of budgeting, or planning, the allocation of all its income with the exceptions provided in the act.⁶³ The appropriation act henceforth could represent an actual appropriation based on a budget plan, instead of a mere review of tax apportionment formulas.

⁶³ Acts 1934, chap. 154.

⁶⁴ It is important to point out that the exceptions amount to more than half of the total. See Table I in the following chapter.

CHAPTER III

THE CURRENT CONCEPT OF BUDGETING

The foregoing chapter has shown how Kentucky, like other states, turned to budget making in the search for responsible government and has described the developments in Kentucky's budget procedure. This and the following chapters attempt to describe in detail the operations of the present budget system of the state.

Three aspects of budget theory which merit special attention because of their influence on the effective operation of a budget system are: (1) emphasis on the central position of the chief executive in formulating and controlling the financial policy of the state; (2) a trend toward a more systematic use of budgeting as a tool of planning and management; and (3) recognition of the principle that a budget system must comprehend *all* revenues and *all* expenditures in order to prevent fiscal maladjustments. These precepts are highly correlated in their influence on the management of public finances. In other words, effective gubernatorial leadership depends upon the degree to which the budgeting procedure and the budget staff agency are developed to serve as tools of planning and management; and, conversely, a highly developed budget system may stalemate if the executive does not recognize the service it can be to him. Finally, both of these factors are potent only with respect to that amount of the state's finances which are subjected to budget processes.

THE EXECUTIVE BUDGET¹

Executive budgets were a part of a process of unifying authority in the executive branch of government to combat irresponsible government. The extreme doctrine of the separation of executive from legislative and judicial branches of government with its emphasis on "checks and balances" interfered with executive responsibility for governmental administration.

¹This term is used most commonly to refer to the delegation of the responsibility for budget preparation to the chief executive, but the executive budget system may also grant special powers with respect to the adoption and execution of the budget program.

In fact, some political thinkers believed that government could best be kept responsible to the people by: (1) diffusing the power in the representative legislatures and curbing the executive; and (2) making the government weak in the scope of its activities in accordance with the *laissez-faire* principle.²

Experience over a period of a few decades discredited both these conceptions. The practice of "log rolling," the extravagance of the "pork barrel," the frequent absence of effective fiscal leadership, and the slowness of legislative action indicated that it was a mistake to make the legislature responsible for details of activities and methods of administration—that that body could propose, discuss, decide, but it was seemingly disqualified for "doing." At the same time the change in the economic development of the country from an agrarian to a predominantly urban population, from individual to large, impersonal corporate enterprises, created a social environment which necessitated making new and complex regulations in the interest of liberty. The need was gradually felt for the state to widen its sphere of activities. As new functions were assumed, they were first assigned to the elective officials, the secretary of state, the state treasurer, the state auditor, etc.; also independent offices were created to administer a part of these new activities. Because these agencies were relatively irresponsible, the lawmakers strengthened the chief executive's authority over them and then sought comprehensive reorganizations of the state governmental machinery.³

The need to re-examine and rebuild the structure eventuated in recognition of the governor's responsibility for directing the administrative activities of the state. The executive budget has, perhaps, contributed more than any other single factor to this end. To a large extent, subjecting to the chief executive's financial control officers who are not appointed by the governor re-

² John A. Perkins, *The Role of the Governor in Michigan in the Enactment of Appropriations*, 1942, p. 1 and Leslie Lipson, *The American Governor from Figurehead to Leader*, 1939, chap. 1.

³ Lipson, *op. cit.*, chap. 2; John M. Mathews, "The New Role of the Governor," *American Political Science Review*, 1912, pp. 220 ff. Since 1910 more than half of the states have reorganized their administrative framework. A. E. Buck, *The Reorganization of State Governments in the United States*, 1938, pp. 7-12. For the nature of the arguments of those who opposed the movement see F. W. Coker, "Dogmas of Administrative Reform," *American Political Science Review*, 1922, pp. 399-411.

duces their sense of independence and contributes toward the unification of the state's management.

The essential characteristic of an executive budget system is that each line of work in every department and institution of the state be carried out according to a carefully considered plan and that this plan be integrated under the governor's direction. At the same time the governor's power and authority are increased, so is his responsibility. The budget procedure forces the governor to come before the legislature, not only to give an account of past acts, but also to make known his plans for the future before further support is given. The representatives, and at election time the voters, review his budget plan, including its execution.

The chief executive, by virtue of his authority over administration, is in a key position to prepare the financial plan. A convincing statement on this point, which is frequently quoted, is that of René Stourm, the noted French writer on the budget:

"The executive alone can and should do this work. Situated at the center of government, reaching through its hierarchial organization to the smallest unit, the executive more than anybody else is in a position to feel public needs and wishes, to appreciate their comparative merits, and accordingly to calculate, in the budget, a just appropriation which each of these needs and wishes deserves. Others may know certain details as well, possibly better than the executive, but nobody can have so extensive and impartial a view of the mass of these details, and no one can compromise the conflicting interests with so much competence and precision. Moreover, the executive, charged with the execution of the budget, is compelled, through concern as to his future responsibility, to prepare as well as possible the plan."⁴

The principle of integrating authority in the executive branch has frequently borne the brunt of attack; but the executive budget has been fully endorsed by American writers on budgeting and public administration,⁵ because it measures up to two essential requirements of the budget-making authority, namely, (1) that it should be an administrative rather than a

⁴ *The Budget*, 1917, pp. 53, 54.

⁵ See Chapter II, p. 16, especially footnote 31; also cf. A. E. Buck, *Public Budgeting*, 1929, pp. 284-286, *The Budget in Governments Today*, 1934, p. 80; Arthur N. Holcombe, *State Government in the United States*, 1926, p. 327; Harley Leist Lutz, *Public Finance*, 1936, p. 867; Austin F. MacDonald, *American State Government and Administration*, 1940, p. 355; John M. Pfiffner, *Public Administration*, 1934, p. 300; J. Wilner Sundelson, *Budgetary Methods in National and State Governments*, 1938, pp. 297-301; and Leonard D. White, *Introduction to the Study of Public Administration*, 1933, chap. 13.

legislative agency, and (2) that it should be the same agency which is responsible for the execution of the budget.

Although the theory of executive budgets is as old as any theory on budgeting in this country, it was not until 1936 that Kentucky began to operate an executive budget system definitely under the Governor's control. The Budget and Financial Administration Act of 1934 authorized the Governor to prepare a budget, but it was not until the Governmental Reorganization Act was passed in 1936 that pointed responsibility was placed upon him through a change in the administrative structure, which made the heads of the most important departments directly responsible to the Governor; and not until then was provision made for adequate financial and technical assistance.⁶ In recent years the Kentucky Governors have taken advantage of the control over finances vested in them and have made marked progress in state financial administration. When Governor Chandler became chief executive in 1936, the total debt of the state, which had been accumulating since 1908, approached \$28 million.⁷ In March 1942 the last of the interest-bearing state warrants were called for payment.⁸ The disorderly operating deficits which accumulated between 1908 and 1936 were wiped out largely by gubernatorial control over the finances through the effective use of the budget machinery together with revision and administration of the revenue laws. The Governor exercised control through planning the finances for each fiscal period, through effective leadership in getting each General Assembly to adopt the plan, and through active administrative management of the plan as it was approved.

There is, however, some evidence of a relinquishment of gubernatorial leadership in budget matters in the current administration. Before the General Assembly convened, the Governor, like his immediate predecessors, referred the budget problem to the Legislative Council; but, whereas earlier executives had sought *advice* regarding the executive budget, he seemed to ask that the Council *prepare* the budget. For the first time since 1934, the 1944 plan, as the Governor submitted it,

⁶ See Chapter II, pp. 21-23.

⁷ Gov. A. B. Chandler, "Message to the General Assembly," *Senate Journal*, 1938, vol. 1, pp. 15, 16. Over \$25 million was in the form of warrant debt.

⁸ Gov. Keen Johnson, *Kentucky Government, 1939-1943*, p. 51.

contemplated a current deficit. Some weeks after presenting his financial program, the chief executive modified his recommendations materially, saying that he had not had time originally to reach a mature judgment. Besides all these factors, executive leadership was not aided by the fact that a majority of legislators belonged to the opposition party.⁹ The General Assembly failed to pass the budget bill during the regular session, and a special session had to be called for the purpose. Kentuckians interested in sound budget practice and accustomed for some years to seeing the general appropriation bill passed under executive leadership early in the session are much concerned about the manner in which the current appropriations were passed in the face of opposition to the Governor.¹⁰ The 1944 budget snarl may be only a temporary condition growing out of the present administration's reaction against alleged "dictation" from the Governor's office.

THE BUDGET AS AN INSTRUMENT OF PLANNING AND MANAGEMENT

While the term "budgeting" frequently connotes a technical system by means of which the policies of the legislature and executive will be determined and carried out, the idea that the budget process is more than a neutral agent is evidenced by much of the current literature on the subject,¹¹ which is

⁹ James W. Martin, "Current Developments in Kentucky State Budgeting," *Southwestern Social Science Quarterly*, Dec., 1944, pp. 197 ff.

¹⁰ *Loc. cit.*

¹¹ See Arthur N. Holcome, "Over-All Financial Planning through the Bureau of the Budget," *Public Administration Review*, 1940-41, pp. 225-230; Catheryn Seckler-Hudson and Cynthia H. Moore, "Budgetary and Fiscal Theory as Reflected in Presidential Budget Messages, 1921-44," in Catheryn Seckler-Hudson, *Budgeting: An Instrument of Planning and Management*, Unit I, 1944, *passim*; J. Weldon Jones, *The Execution of the Federal Budget*, reprint of an address given at the 26th annual meeting of the American Accounting Association, Dec. 30, 1941, pp. 1, 2; Allen D. Manvel, "The Philosophy and Essentials of Budgeting," in Catheryn Seckler-Hudson, *op. cit.*, pp. 63, 64; Fritz Morstein Marx, "The Background of the Budget and Accounting Act," and "The Bureau of the Budget Since Dawes: Stability and Reorientation," in Catheryn Seckler-Hudson, *op. cit.*, pp. 20-26 and 52-57; Harvey S. Perloff, "Budgetary Symbolism and Fiscal Planning," in C. J. Friedrich and Edward S. Mason, *Public Policy*, 1941, pp. 37 ff.; Donald C. Stone, *Planning as an Administrative Process*, reprint of an address presented to the National Conference on Planning, May 12, 1941, p. 10; Harold D. Smith, *The Budget as an Instrument of Legislative Control and Executive Management*, reprint of an address for the Municipal Finance Officers Association, June 9, 1944, *passim*; *The Bureau of the Budget as an Instrument of Management*, reprint of an address given at a joint meeting of the American Political Science Association and the American Society for Public Administration, Dec. 29, 1940, *passim*; "The Bureau of the Budget," *Public Administration Review*, 1940-41, pp. 106-115, *The Role of the Bureau of the Budget in Federal Administration*, reprint of an address given at a joint meeting of the American Political Science Association and the American Society for Public Administration, Dec. 28, 1939, *passim*; *Some Budget Problems*, reprint of an address delivered before the Economic Club of Detroit, April 29, 1940, *passim*; Robert A. Walker, "The Relation of Budgeting to Program Planning," *Public Administration Review*, 1944, pp. 97-127.

shifting emphasis from the "watch dog over the treasury" idea stressing accounting techniques to a view that the budget can best serve financial policy if it is used as an instrument of planning management.

The budget was first officially conceived in this country as a tabulation of contemplated expenditures. In keeping with this earliest American view, many of the first so-called budget laws required merely tables showing planned expenditures. The guiding thought seemed to be that the specific expenditure plan (often of the "general fund" only) ought to be worked out before the beginning of each fiscal year. This primitive conception is retained in Kentucky language usage even though actual budget-making has advanced beyond it. For example, the newspaper correspondents commonly refer to "the budget bill" when the general state appropriation measure is meant; they exclude other appropriation bills and all revenue legislation.

The budget developed in a period when fiscal soundness was a part of the ideal of minimum government interference with the private economy; the demands for economy and efficiency were rooted in the prevailing social ethic and became a part of the conception of budgeting. "Soundness" in governmental finance was interpreted as calling for a limitation of public activities and expenditures to a minimum; and the budgetary principles emphasized equilibrium, which insisted on a balance between government expenditures and current revenues annually, which came from the theory that a year was the maximum of time over which legislatures could afford to let the control of the purse out of their immediate supervision and so would limit the expansion of governmental activities from long-term projects, and unity, which demanded that all fiscal material be presented in a single budget.¹² When social needs demanded that government bring about a more equitable distribution of wealth, regularize employment and care for the unemployed, control industries affected with a plain public interest, and prevent private economy from breaking down under the weight of too severe crises, government spending on a larger scale was inevitable. A new fiscal policy appeared, but this policy was frustrated to a

¹² Smith, *The Budget as an Instrument of Legislative Control and Executive Management*, loc. cit.; Perloff, op. cit., pp. 40-43.

considerable extent as a result of being pressed into a budgetary system which had been built on principles contradictory to the new policy.¹³ Budget practice in the states and in the national government has not kept pace with the changing fiscal policy, and the systems are still largely geared to the principle that budgeting is primarily an instrument of restricting and controlling expenditures.

The Kentucky system, for example, has made superior provisions for executing and controlling the budget plan which is adopted by the General Assembly;¹⁴ however, there is no place either in the Division of the Budget or in any other agency where a staff makes studies of administrative organization and management in order to aid the Governor in obtaining a more efficient and economical administration. The function of the budget as a means of preventing extravagance and of keeping expenditures within appropriations is an important one; but if the purpose of the budget is limited to merely this control operation, the budget system does not contribute maximum service to the management of finances. There is a positive role for the budget system of Kentucky to perform.

The budget is the crucible into which the manifold issues of collective action, economic intervention, tax justice, allocation of resources to various functions, etc. are poured; and, if wise decisions are to be made on these issues, significance must be attached to the budget as an instrument of implementing public policy and guiding governmental activities. Budgeting is a form of planning, and planning is the basis of progressive budgeting.¹⁵ Professional planning groups think of budgeting and planning as interrelated functions in connection with capital outlay and physical construction but have overlooked the planning necessitated by the annual budget process. Administrators who carry out public policies, budget officers, executives, and legislators, who review the budget requests, are all forced to think of future operations in order to determine the proper allocation of revenues. The budget is a plan of action and must be considered as

¹³ Evidence the attempts at balanced budgets, the "pump-priming," and the "compensatory" and "extraordinary" budgets of the current administration in the federal government.

¹⁴ See Chapter VII.

¹⁵ A good statement of this idea is presented in Walker, *op. cit.*, *passim*.

essentially a means of assisting the officials responsible for public activities in carefully appraising the program requirements. This view calls for making a place in the budget staff agency for studying administrative organization and techniques and appraising the various needs and demands for extending or limiting governmental services. It also calls for drawing on personnel with general administrative training or with first-hand knowledge of the needs and problems of operating agencies in selecting budget staffs in addition to those in the accounting profession.

While he was director of the budget in Virginia, Mr. Rowland Egger wrote this of the budget function:

"The budget, in fact, is not fundamentally a fiscal document at all, nor is the budgetary process a financial procedure. To be sure, it frequently utilizes the mechanisms of fiscal control, but it also utilizes other types of control of a non-fiscal character, and even fiscal controls are more often than not used for other than strictly financial purposes. A budget is a work program, and to the extent that it reflects purely fiscal considerations it fails in its most important objective."¹⁶

BUDGETARY COMPREHENSIVENESS

Principle of budgetary comprehensiveness

Comprehensiveness is one of the most widely recognized of budgetary principles, and one that has been recommended as a feature of good budgeting regardless of the nature of the approach to budgeting in general. The concept of comprehensiveness presents the demand that the budget system cover *all* receipts and *all* disbursements of a particular government unit which it serves.¹⁷ It does not imply that all fiscal activities should be subjected to a uniform treatment at all times. What is meant is that the existing practice should be known and understood so that it can be relied upon to give a true interpretation of the fiscal operations of the state, and that no items of expenditure or receipt lie outside the procedure of planning, voting, and controlling fiscal operations. In general, practices of earmark-

¹⁶ "Power is Not Enough," *State Government*, Aug. 1940, p. 150.

¹⁷ Sundelson, *op. cit.*, chaps. 4 and 10 differentiates between budgetary comprehensiveness and budgetary unity. According to his viewpoint, budgetary unity precludes segregation within the budget system of certain financial operations for particular treatment, while comprehensiveness precludes complete exclusion of some transactions from the budget system. However, since both these elements are involved in determining whether a government unit's budget procedure includes all receipts and expenditures, the distinction is ignored.

ing revenues for specific purposes, omitting some operations from the budgetary procedure, and maintaining a multiple fund system are conducive to fiscal maladjustment and are associated with efforts to mask the true fiscal impact of economic policies. On the other hand, these practices *per se* cannot in every instance be condemned as being fiscally unsound. For example, the existence of a special fund for the amortization of debt cannot be deprecated as defeating the proper administration of the budget system.

In 1934 Kentucky made a definite step toward the goal of a comprehensive budget system when she diverted the receipts from a number of the principal taxes from special, restricted funds to the general fund to be used to defray expenses of government as distributed by a budget plan; but the step was by no means complete. Several practices still exist which hamper the operation of the budget system. The areas of fiscal administration in Kentucky which are virtually void of budgetary management are discussed in the following paragraphs.

Assignment of tax revenues

The variations in assignment devices are almost innumerable, and depend largely upon the purpose of the assignment and the general circumstances that surround it.¹⁸ There are various motives that inspire assignment of tax revenues—a desire to limit expenditures to assure revenue adequacy, to grant independence to a segregated function, and to gain the popular support of a particular revenue measure by tying the yield up with a lofty purpose; a belief that categories of taxes are levied for a specific service; or even a tradition of assigning a particular levy which hangs on even under altered circumstances.

The most universally earmarked taxes in the states are those of the motor vehicle family and payroll taxes, although inheritance, poll, severance, and probably almost every other type of tax imposed are assigned in some jurisdiction or another.¹⁹

¹⁸ Cf. Sundelson, *op. cit.*, pp. 193-198 for a complete discussion on assignment motives and devices.

¹⁹ *Ibid.*, pp. 213-227; Tax Research Foundation, *Tax Systems* (eighth ed.), 1940, the columns "Distribution of revenue" in the various tax tables of the 48 states.

Kentucky is one of the few states that limit their tax assignments to the usually dedicated automotive and payroll levies.²⁰

Certain revenues of Kentucky are payable into the state road fund and become immediately available for financing the activities of the Department of Highways. All revenues collected from the gasoline and other motor fuel excises and from the license and permit taxes on motor vehicles (except that one-half the revenues from truck licenses are distributed equally among counties for county road funds²¹) go into the state road fund.²² In addition the fund receives the receipts of certain departmental fees (such as contractors' prequalification fees²³), sales, and rentals, some county and court fees, and various subventions. The fund operates with few statutory restrictions as to the amounts that may be expended for the various activities of the Department of Highways. By enactment of the 1936 General Assembly \$2 million are appropriated annually out of the state road fund to be used by the Department of Highways for the improvement, reconstruction, and maintenance of county roads and bridges which have not been accepted by the Department for maintenance.²⁴ Also in the biennial appropriation acts the legislature stipulates the maximum amount to be expended for ordinary recurring administrative expenses of the Department and of the highway patrol. This restriction is not so binding, however, in view of the fact that the term "administration" is broad in scope and may embrace varying amounts and types of expenditures. Finally, appropriations are made out of the road fund to the Department of Revenue and to the Division of Motor Transportation, Department of Business Regulation, for covering costs of administering some of the automotive taxes. All other money received and placed to the credit of the state road fund are appropriated to the State Highway Department "for use and benefit of the State Road System in construction, maintenance, and repair of roads, and for all the activities and duties of said Department, as prescribed by law."²⁵ This money is

²⁰ N. Y., Me., Mass., and Va. are other limited assignment states. Sundelson, *op. cit.*, pp. 237-239.

²¹ KRS 47.020. The Motor vehicle usage tax is a general fund revenue measure (3rd spec. sess., 1936, chap. 14, sec. 8).

²² KRS 47.010.

²³ KRS 47.010.

²⁴ Acts 1936, chap. 5, sec. 1; KRS 179.410.

²⁵ See Acts 1942, chap. 1, part 3, sec. 1.

spent at the discretion of the State Highway Commissioner, who is appointed by the Governor;²⁶ but it is not subjected to the regular executive budget planning.

At the fourth special session of 1936 the General Assembly enacted the Unemployment Compensation Law, which established a special fund to be known as the "unemployment compensation fund" to be administered "separate and apart from all public monies or funds of the State."²⁷ The fund operates in conjunction with the federal Social Security Act. Three separate accounts are maintained within the fund: (1) a clearing account which receives all money payable to the fund, mainly employees' and employers' contributions from payroll taxes; (2) an unemployment trust fund account recording the deposit of the payroll tax receipts with the United States Secretary of the Treasury; and (3) a benefit account consisting of money requisitioned from the federal government for the payment of benefits.²⁸ The fund also includes interest, fines, and penalties collected under the Unemployment Compensation Law.²⁹ The law designated the State Treasurer as custodian of the fund and created an Unemployment Compensation Commission, composed of an executive director and two associate directors, all appointed by the Governor, to administer the fund.³⁰ The unemployment compensation administration fund was created in the state treasury to defray costs of administration.³¹

The states have little choice with respect to unemployment compensation arrangements, since the federal statute coerces the earmarking of payroll taxes. However, the existence of autonomous highway funds is unessential and undesirable. A survey of assignment policies indicates that earmarking motor fuel and vehicle tax yields can be traced to inherent tax factors, that is, that the taxes are levied on the basis that the motorist is paying for the roads.³² However, highway maintenance is not a self-

²⁶ KRS 12.040, 176.020.

²⁷ Acts 1936, 4th spec. sess., chap. 7, sec. 9(a); KRS 341.490.

²⁸ Acts 1936, 4th spec. sess., chap. 7; KRS 341.500.

²⁹ Acts 1936, 4th spec. sess., chap. 7, sec. 9(a); KRS 341.490.

³⁰ Acts 1936, 4th spec. sess., chap. 7, secs. 9(c) and 10(a); KRS 341.500, 341.110.

³¹ Acts 1936, 4th spec. sess., chap. 7, sec. 13; KRS 341.240.

³² See Harold M. Groves, *Financing Government*, 1939, chap. 14 and Ray H. Garrison, *The Taxation of Commercial Motor Vehicles in Kentucky*, unpublished master's thesis, University of Kentucky, 1944, chaps. 2 and 3. The view stated in the text follows the findings of the National Tax Associa-

balancing category for which independent funds are essential. The need to coordinate and plan all public works activities, of which road construction and maintenance is a part, militates against the separation of highway expenditures from other capital outlays. A greater degree of budgetary unity in planning, voting, and executing a fiscal program can be achieved when all revenues of the state are allocated in relation to the relative financial requirements of each function. The receipts of the Kentucky state road fund amount to nearly 25 per cent of the total revenues of the state³³ and could be made a part of the general fund subject to biennial appropriation based on a budget plan without jeopardizing the maintenance of the highways.

Assignment of non-tax revenues

The practice of assigning both tax and non-tax revenues has led to the creation of specific-use funds which are sometimes linked with the normal budgetary process, but more often given an extra-budgetary status. The extent to which the assignments of non-tax revenue interfere with budgeting is not as great as the extent to which tax dedications do so. (See Table 1.) The special fund system and the modern budget idea are incompatible; and, as long as resources are set aside for the purpose of carrying on specific activities, the state will reap disadvantages irrespective of the kind of budgeting methods it may adopt. The Public Administration Service in reporting on financial administration in Michigan wrote:

"The inelasticity inherent in a complex fund structure impedes the allocation of resources according to relative needs. . . .

"A simplification of the fund structure would tend to obviate the possibility of one agency having available an excess of funds while at the same time other departments may be inadequately financed due to the condition of the fund from which their activities must be financed."³⁴

tion committee to investigate highway finance, Jacob Viner and others, "Problems of Highway Finance," *Proceedings of the National Tax Association*, 1924, p. 430 and James W. Martin and others, "Taxation of Motor Vehicle Transportation," *Proceedings of the National Tax Association*, 1930, p. 151.

³³ See Table 1. In spite of the progress made, the General Assembly has submitted a constitutional amendment for the approval of the voters in the fall of 1945 which would perpetuate road fund earmarking. The amendment proposes to divert the revenues derived from the motor usage tax and the operators' license from the general fund to the road fund.

³⁴ *Report on Financial Administration in the Michigan State Government*, 1938, pp. 72, 73.

Table I
Revenue Receipts of Kentucky for the Fiscal Year Ending
June 30, 1943

Fund*	Amount	Percentage of Total
General	\$32,692,006.18	40.2
Revolving, trust and agency	13,265,918.52	16.3
State road ^b	19,814,288.87	24.4
Highway bridge bond sinking	1,150,995.66	1.4
County road trust	37,470.00	.1
Unemployment compensation insurance	13,714,688.45	16.9
Teachers retirement	662,667.46	.8
Total	\$81,298,035.14	100.1

Source: Kentucky Department of Finance, *Biennial Report*, for the fiscal year ending June 30, 1943, pp. 166, 222, 256, 266, 270, 281, 290.

a. The special deposit trust fund and the county road sinking funds were omitted on the basis that the monies placed in these two funds are not state revenue; the state is merely custodian of these funds. The state fire and tornado insurance fund was omitted because it represents disbursements by various departments of money already counted under the general fund. The state contributions were subtracted from the teachers' retirement fund and transfers from the federal government were subtracted from the unemployment compensation insurance fund.

b. Fiscal year ends March 31.

Neither the Budget and Financial Administration Act nor any other statute contains an inclusive list of the funds of the commonwealth of Kentucky. There are four types of funds within the state's fiscal structure: general, revolving, trust and agency, and sinking.

(1) *The general fund.* Authoritative treatises on governmental accounting describe the general fund as one which finances most of the government's expenditures other than construction, operation of public service enterprises, and sinking fund payments, and further that its revenue resources are typically more varied and bulk larger than those of any other fund.⁸⁵ The general fund in Kentucky does not support all the regular activities of the commonwealth. A few departments, Law, Finance, and Treasury, are financed entirely out of the general fund; most of the departments and their subdivisions are financed through both the general and revolving funds; while still other divisions, such as the Fish and Game Commission and the professional examining boards attached to the Department

⁸⁵ Carl H. Chatters and Irving Tenner, *Municipal and Governmental Accounting*, 1940, pp. 33, 34.

of Business Regulation, are handled entirely through revolving funds.³⁶ The revenue receipts for the fiscal year ending June 30, 1943 totaled \$81,298,035.14.³⁷ Of this amount the general fund received \$32,692,006.18, or approximately 40 per cent.³⁸ Thus, it appears that the Governor and the legislature could budget little more than 40 per cent of the revenue receipts without authority to divert the revenues of the special funds from their dedicated purposes.

(2) *Revolving funds.* A revolving fund ordinarily means one established for carrying on a specific activity the receipts of which replenish the outlays from the fund so that it is self-supporting; this type of fund is generally established by appropriation from the general fund, by the sale of bonds, and in some cases, by capital advances from other governments.³⁹ In Kentucky, however, the revolving funds are in reality special revenue funds. The Budget and Financial Administration Act defines the term as "a State treasury account accruing to the credit of a budget unit from operating receipts, fees, gifts, or appropriations which may be used in defraying maintenance and operating expenses of activities and agencies which are in whole or in part self-supporting."⁴⁰ Revolving fund accounts may be established for financing the operations of industries, farms, hospitals, dormitories, dining halls, etc. by depositing the operating receipts of such activities and agencies in the state treasury to the credit of the respective revolving fund account.⁴¹ Such deposits may represent amounts received from every other source, including tuition and incidental fees, federal grants, gifts, and donations. In short, these provisions permit budget units, upon statutory authorization, to deposit their operating and other receipts in a special fund subject to disbursement by only that particular budget unit.

The use of such funds has resulted in a degree of instability in planning activities of the commonwealth. To the extent that departments are financed through these special funds, there is

³⁶ Commonwealth of Kentucky, *The Executive Budget* for the biennium 1944-46, pp. 39-119.

³⁷ See Table 1.

³⁸ *Loc. cit.*

³⁹ Chatters and Tenner, *op. cit.*, p. 79.

⁴⁰ *Acts* 1934, chap. 25, art. 1, sec. 2(q).

⁴¹ *Acts* 1934, chap. 25, art. 3, sec. 14; KRS 45.140.

little budgetary control over their expenditures. Nearly every function of the state is partially financed thus. In some instances the use of such funds is not an illogical assignment of receipts, such as the board and room fees of the state colleges, which are deposited in revolving funds to be used in maintaining the dormitories. Moreover, the agencies partly supported by revolving funds usually have responsibility for collecting, and often for prescribing the rate of revenues which replenish the fund. This fact argues strongly in favor of such funds. For example, the board of trustees of the state colleges prescribe most of the fees and charges; and these collections doubtless would be reduced if they did not condition support of the institutions. As long as activities are largely financed through general fund appropriations and only partly operated by revolving funds, there can be a margin of budget planning through modifying the general fund appropriations in accordance with the amount of revolving fund receipts. In this way an excess of funds in particular agencies could be obviated. The assignment of receipts is especially to be deprecated where an entire budget unit is financed by special revenue assignment. The elimination of special revenue funds in Kentucky, as far as practicable, would greatly aid in both budgeting and accounting, besides contributing tremendously to the citizens' understanding of state finances.

The state road fund, described in the preceding section, the highway bridge bond fund, which receives money for the sale of bridge bonds to be used for specific purposes,⁴² and the state fire and tornado insurance fund are in the nature of revolving fund accounts, as described by the Kentucky law, but are large enough to require special treatment in the accounting system and in financial reporting.

(3) *Trust and agency funds.* Trust and agency funds are established to account for assets received and held by the government in the capacity of trustee or agent for individuals or other governmental units. The Budget and Financial Administration Act makes special provision for trust funds by providing that any agency of the state government having private funds available for its support or for the purpose of defraying the expense

⁴² KRS 180.240.

of any work done under its direction shall deposit such funds or contributions with the State Treasurer.⁴³ With the exception of the county road trust, special deposit trust, and the unemployment compensation funds, the Kentucky trust and agency funds are consolidated within the general grouping of revolving, trust, and agency funds. This consolidation has been found feasible for reporting since separate accounts are maintained for each of the funds, which are relatively small in amount, and since the trust funds received by the state are handled as are the revolving funds, that is, they do not require appropriation by the legislature. The revolving, trust, and agency funds receive over 16 per cent of the total state revenues.⁴⁴

(4) *Sinking funds.* A sinking fund is established to accumulate resources for the retirement of bonds. The highway bridge bond sinking fund is the only sinking fund handled through the State Treasury in Kentucky at present. This fund was created for the purpose of paying the principal and interest on bridge revenue bonds. The income of this fund is derived from bridge tolls, such tolls being fixed by the Department of Highways.⁴⁵ In general, the assignment of receipts to sinking funds does not constitute a serious infraction of the principle of comprehensiveness, provided the operations of the funds are fully reported and understood.

Other extra-budgetary elements

The discussion up to this point has attempted to differentiate between the financial transactions of the state and its departments which are subjected to the scrutiny of budget planning and control through the central budget office and those which are substantially independent of the budget procedure. All the funds previously mentioned are cleared through the state Department of Treasury. It is virtually impossible to ascertain the degree to which state agencies receive monies which do not reach the central Treasury Office. It will have to suffice to say that some trust funds, revenue bond sinking funds, federal grants, and gifts are retained by various spending agencies over

⁴³ Acts 1934, chap. 25, art. 6, sec. 9; KRS 41.290. As to the University, see also KRS 164.160, which some attorneys believe constitutes this agency a "special case"

⁴⁴ See Table 1.

⁴⁵ KRS 180.090.

which there is no central supervision. Possibly federal grants constitute the largest proportion of these monies, since the federal government, like private donors, usually makes grants directly to spending agencies for specific purposes.⁴⁶ Although there may be no justification for giving authority to the Governor to make recommendations regarding the expenditure of grants and gifts made directly to the spending agencies, there is cause for reporting *all* receipts and *all* expenditures if a valid picture of the state's fiscal operations is to be obtained.

STEPS OF THE BUDGETARY PROCESS

For the more comprehensive analysis of the present budgetary practices in the following chapters the conventional stages of budgetary procedure as first designated by the French authority, René Stourm,⁴⁷ and followed by A. E. Buck⁴⁸ have been accepted: (1) the formulation, which takes up the estimates at their inception and carries them through the executive heads of the spending agencies to the budget staff agency for revision and to the chief executive for final review; (2) the authorization, which deals with the legislative body and its committee where the financial plan is given legal status by legislative enactment; (3) the execution, which extends into the domain of financial administration and through which the financial plan is actually carried out; and (4) the accountability for the budget as executed, which is the check to determine whether the administration has complied with the terms and conditions imposed by the legislature.⁴⁹ A section dealing with the budget document has been added.

With respect to these stages of the budgetary procedure, it now appears to be the opinion that the executive should control the first, third, and fifth, and the legislature should dominate

⁴⁶ The University of Kentucky receives annually about \$1.5 million in federal payments, most of which are not deposited in the State Treasury or regularly reported to the Department of Finance (conference with Mr. Frank D. Peterson, Comptroller of the University of Kentucky, Sept. 11, 1944). The federal grants of Morrel-Nelson funds made to the University and to the Kentucky State College for Negroes do clear through the Department of Finance to the Treasury (conference with Mr. Warren Van Hoose, Assistant Budget Director, Kentucky Department of Finance, Sept. 4, 1944).

⁴⁷ *Op. cit.*, p. 52.

⁴⁸ *Public Budgeting, op. cit.*, p. 47.

⁴⁹ As the Bureau of Business Research has published recently *The State Auditor*, no extended consideration is given here to accountability.

the second and fourth. The division into stages, however, should not obscure the fact that there is a continuity in the whole process and no procedures are isolated from any of the others.

CHAPTER IV

FORMULATION OF THE BUDGET

ORGANIZATION FOR BUDGET PREPARATION

The budget-making authority

The practices of budget making in the states, as well as the theory concerning it, show the marked preference for delegating the responsibility of preparation to the executive. All but nine states¹ have executive budget systems. The alternatives to budget preparation by the executive are preparation by an administrative board,² by a board composed of both administrators and legislators,³ or by a board composed solely of members of the legislature.⁴ In all states having a board type of budget-making authority, except Indiana and Arkansas, the governor is not only a member of the board, but the *ex officio* chairman.

There are several practices in the various states which dilute the governor's authority in budget making. All the states, except Kansas, which does not exempt legislative costs, and Indiana, which dispenses with the usual immunity of the judiciary, give the governor no authority to revise agency estimates for legislative and court expenditures.⁵ Nebraska and Vermont require the governor to communicate his reasons for changes in the estimates to the legislature.⁶ This provision casts doubt on the governor's ability and reduces his work to that of clerical compilation.⁷ In Michigan a state administrative board composed of various state officers has general supervisory control over all administrative departments and institutions.⁸ This may not be objectionable provided the Governor is left free to make

¹ Ark., Del., Fla., Ind., Mont., N. D., S. C., Tex., and W. Va.

² Del., Fla., Mont., Tex., and W. Va.

³ Ind., N. D., and S. C.

⁴ Ark.

⁵ J. Wilner Sundelson, *Budgetary Methods in National and State Governments*, 1938, p. 299.

⁶ *Compiled Statutes of Nebraska*, 1929, chap. 81, art. 3, sec. 81-310 and *Public Laws of Vermont*, 1933, chap. 30, sec. 559.

⁷ Sundelson, *loc. cit.* This author interprets the requirement as a futile effort to keep political motivations out of the expenditure revisions.

⁸ *Mason's 1940 Cumulative Supplement to the Compiled Laws of Michigan*, chap. 11, secs. 201, 203.

decisions regarding expenditure estimates.⁹ In all states the legislative practices of dedicating funds to specific purposes and of detailing appropriations so that there can be no flexibility in expenditures restrict the governor in both planning and executing the budget. The governor can be greatly handicapped by a disintegrated administrative structure which places popularly elected officials outside of his control and similarly by the existence of a large number of boards and commissions substantially independent of the governor. Lack of proper staff assistance can weaken the governor's power to the point of being perfunctory. Another limitation to effective executive budget planning suggested by one writer¹⁰ is the fact that in some states where the term of office is short and where the governor is not eligible for re-election there is less inducement to make an outstanding record in fiscal policy matters. Unless the governor aspires to a political career, this factor may decrease his sense of responsibility to the people.

Although much has been accomplished in recent years toward establishing an effective executive budget system in Kentucky, there are, as is true in other states, some limitations on the Governor's power to utilize the budget system to its fullest extent. Some of these are discussed more completely in connection with other phases of the budgetary process and are mentioned only briefly here. The segregation of the commonwealth's resources into numerous, restrictive funds reduces the Governor's discretion in allocation of resources to the functions of government according to relative needs; unrestricted legislative power to modify the Governor's budget leaves the door open for the executive plan to be partially or completely replaced by a legislative budget;¹¹ the lack of adequate staff assistance weakens the Governor's ability to maximize the budget as an instrument of planning and management.

⁹ According to local interpretations, the preparation of the budget is essentially an executive responsibility, while the Board retains considerable authority over its execution through control over allotments and approval of transfers within appropriations. George C. S. Benson, *The State Administrative Board in Michigan*, 1938, pp. 22, 65, 66 and John A. Perkins, *The Role of the Governor in Michigan in the Enactment of Appropriations*, 1942, pp. 97, 98.

¹⁰ Denzel C. Cline, *Executive Control over State Expenditures in New Jersey*, 1934, p. 2.

¹¹ In actual practice Kentucky has made a definite contribution toward establishing a satisfactory relationship between the legislative body and the executive on the voting of appropriations through the use of the Legislative Council as an advisory body. See Chapter VI.

The budget staff agency

The Governmental Reorganization Act of 1936 integrated financial functions in a Department of Finance and provided that the Division of the Budget within the Department act as the Governor's staff agency in the actual work of collecting the necessary information, compiling and arranging the material in a report, and controlling appropriations.¹²

An examination of the state laws indicates that there are four general types of staff agencies.¹³ Fifteen states¹⁴ have departments of general financial administration which have powers covering the important phases of fiscal management—budgeting, the maintenance of control accounts and pre-audit functions for other state spending agencies, the installation of a uniform accounting system, centralized purchasing duties. Sometimes nonfiscal functions, such as general personnel control, are included. These departments are generally subdivided into divisions or bureaus which have charge of one general function. All of these states have an executive budget system.

A more popular form of staff agency is the budget bureau, office, or officer connected with or subordinate to the executive department. The functions of these agencies are more limited than the departments of finance above described. Such offices deal mainly with the preparation of the budget, although in many cases they also exercise some supervision over its execution. Seventeen states,¹⁵ all with executive budget systems, employ this type of staff agency. In Nevada also the Governor prepares the budget without the aid of any other office.

In some states in which the budget-making authority is the board type the accountants and clerical workers in the offices of the members of the board often serve as the staff agency. Sometimes additional assistants are employed for the purpose of doing the routine work connected with budget preparation. Nine states are in this group.¹⁶

¹² Acts 1936, 1st spec. sess., chap. 1, art. 10, secs. 1, 3; KRS 42.030, 42.040.

¹³ Also See A. E. Buck, *Public Budgeting*, 1929, pp. 291-300 and Sundelson, *op. cit.*, pp. 302-318.

¹⁴ Ala., Calif., Conn., Ill., Ky., La., Me., Mass., Minn., N. J., Ohio, R. I., S. D., Utah, and Wash. Mo. will presumably belong in this category after July 1, 1945.

¹⁵ Colo., Ga., Idaho, Kan., Md., Mich., N. H., N. Y., N. C., Okla., Ore., Pa., Tenn., Vt., Va., Wisc., and Wyo.

¹⁶ Del., Fla., Ind., Miss., Mont., N. D., S. C., Tex. and W. Va.

Six states¹⁷ make no provision in their laws for a budget staff agency, but assign the duties of supplying information for budget preparation to one or several of the state financial officers. Assignment of budget-making duties to an officer of the state having duties other than budget preparation is usually unfortunate in that it imposes a task which is worthy of full-time attention upon an official who can devote only part-time to the duty. As a consequence both functions must be partially neglected.¹⁸

The assignment of each state¹⁹ to these categories is somewhat arbitrary. In many cases hybrid forms occur. For instance, in Texas the Board of Control, the members of which are appointed for long overlapping terms, prepare expenditure estimates; the elective Comptroller prepares revenue estimates and performs certain other duties incident to budget administration; and the Governor submits appropriation bills and approves minor deficiencies. All budget staff agencies rely on other state fiscal officers for information, and the laws frequently stipulate that certain officers assist the agency. States in the first category are not subclassified to indicate whether financial administration functions have been completely or only partially integrated.

The extent to which a staff agency aids in the determination of financial policy is more important to all states than the administrative organization for budgeting. The Governmental Reorganization Act of Kentucky in providing a staff agency prescribes:

"The division of the budget, under the direction of the Commissioner of Finance, shall perform such functions relating to the preparation and administration of the State budget as may be required by the Commissioner of Finance. In general, this division shall be responsible for all matters relating to the State budget as provided in Chapter twenty-five (25), Acts of the General Assembly of 1934, Articles III, IV, V, VI, and IX, and elsewhere in the statutes. The division of the budget shall be headed by a director of the budget, who shall be a person acquainted with the methods

¹⁷ Ariz., Ark., Iowa, Mo., Neb., and N. M. Missouri, under the new constitution, will no longer occupy this position after July 1, 1945.

¹⁸ See James G. Robinson and Edwin O. Griffenhagen, *Financial Administration of the State of Missouri*, 1929, p. 38 for a statement of the result of making the Chairman of the Tax Commission of Missouri the chief budget officer.

¹⁹ The facts respecting Nevada are not sufficiently complete to make accurate classification of that state.

and techniques of public budgeting. Subject to prior approval of the Governor in writing, the Commissioner of Finance may serve as director of the budget, or he may appoint a director of the budget, as provided in this Act, who shall serve under his supervision and direction."²⁰

The Commissioner of Finance is responsible to the Governor for the administration of the Department of Finance and is appointed by the Governor to serve at his pleasure.²¹

The duties of the budget officer as director of the staff agency are mainly: (1) to assist the Governor in preparing a biennial budget report presenting a complete financial plan for each fiscal year of the ensuing biennium to be submitted to the legislature; (2) to keep "in continuous process of preparation and revision, in the light of his direct studies of the operations, plans, and needs of budget units and of existing and prospective sources of income, a tentative budget report for the next ensuing biennium for which a budget report is required to be prepared;" and (3) to administer the budget as approved by the legislature.²² Of these three it is the second function which has received the least attention in Kentucky.

Since the creation of the office of Budget Director, there has been no appointment to the position; that is, the Commissioner of Finance has retained the titular post and the work connected with preparing and executing the budget has been largely delegated to the Director of the Division of Accounts and Control, or to the chief accountant in this Division, the Commissioner retaining the final authority.²³

Thus, the Division has never been set up as a distinct unit as contemplated by law. Although the Commissioner of Finance continually administers allotments, there is a definite budget staff only in the four-to-six months period prior to the biennial legislative session. During this time when the budget document is in the process of being compiled, the Director of the Division of Accounts and Control serves as Acting Budget Director working under the supervision of the Commissioner of

²⁰ Acts 1936, 1st spec. sess., chap. 1, art. 10, sec. 3; KRS 42.040.

²¹ Acts 1936, 1st spec. sess., chap. 1, art. 10, sec. 2; KRS 42.020.

²² Acts 1934, chap. 25, art. 3, secs. 2, 7, 12, 13, 17, 18, 19, and art. 4, sec. 7; KRS 45.030, 45.080, 45.120, 45.130, 45.160, 45.170, 45.180, 45.190, 45.200, 45.270, 45.320.

²³ Conference with Mr. Frank D. Peterson, former Director of the Division of Accounts and Control, Kentucky Department of Finance, now Comptroller of the University of Kentucky, May 11, 1944.

Finance as Budget Director; and clerical assistance is recruited by shifting employees within the Department of Finance and hiring additional employees if necessary.²⁴ This temporary type of staff agency is at best only a make-shift and satisfies neither the apparent requirements of the Kentucky law nor the demands of good budget practice. The law envisioned a permanent budget staff operating throughout each year when it said that the budget officer "shall have in *continuous* process of preparation and revision . . . a tentative budget report for the next ensuing biennium" (italics supplied). Moreover, administration of the state budget needs the attention of a full-time staff.

The responsibilities of the Division of the Budget are broader than mere fiscal control. Although it is necessary to compile the estimates of the financial requirements of the state in one report, to analyze these estimates in terms of dollars and cents, and to check the financial conduct of the spending agencies, the work of budget making is not limited to the short period between the time of the submission of the budget estimate forms to the spending agencies and the presentation of the completed budget report to the legislature. In order to prepare a well conceived financial plan the budget staff agency should equip itself beforehand with information about operating practices and administrative costs.

The federal government has recently taken the lead in establishing a budget staff agency which looks beyond the mere assembling of money items for the budget document. The idea of a budget system which relates the entire budget process to the over-all responsibility of administrative planning and management centered in the President was implicit in the movement of reform which immediately preceded the enactment of the federal Budget and Accounting Act of 1921, although it was not put into operation immediately.²⁵ When the Bureau of the Budget was created in 1921, it was placed in the Treasury Department, but

²⁴ *Loc. cit.* Commenting on a draft of this study, Mr. Warren Van Hoose, Assistant Budget Director, Kentucky Department of Finance, wrote: "The greatest mistake in setting up the reorganization in 1936 consisted in making the budgeting process an incidental function of accounts and control."

²⁵ Fritz Morstein Marx, "The Background of the Budget and Accounting Act," in Catheryn Seckler-Hudson, *Budgeting: An Instrument of Planning and Management*, Unit I, 1944, pp. 8-33.

was transferred to the Executive Office of the President in 1939.²⁶ Various functions in addition to the work of preparing the federal budget document are now assigned to the Bureau, such as making studies looking toward improving management in the federal government, advising the departments and agencies with respect to the relationship between pending legislation and the President's program, clearing executive orders and proclamations, receiving enrolled bills that are to go to the White House, and preparing executive veto messages.²⁷

Two states which have followed the lead of the federal Bureau of the Budget in providing for research studies to aid the governor in efficient administration are New York and Virginia. In 1939 Governor Price of Virginia sought the assistance of a philanthropic foundation interested in the improvement of government machinery in order to expand the Division of the Budget, and at this time a section on administrative planning was created to undertake, either by itself or in collaboration with the departments, survey studies of internal departmental organization to develop specific plans and programs for long-term improvements.²⁸ New York has in its budget staff agency both a management unit to service budget examiners and heads of departments in matters of organization, personnel, etc., and a research unit to determine state needs.²⁹

In both these states the staff agency is a part of the executive office, and the director of the budget is appointed by the governor to serve at his pleasure. The close connection with the chief executive not only facilitates the work of preparing estimates but also enhances the prestige of the budget office and of its director. For the most part department heads resent an investigation by an outside man concerning the mechanics of their

²⁶ President Franklin D. Roosevelt, "First Plan on Governmental Reorganization," *House Documents*, 76th Cong., 1st sess., 1939, doc. 262.

²⁷ Daniel W. Bell, "The Functions of the Bureau of the Budget," *A Forum on Finance*, edited by George B. Roberts, 1940, pp. 48-70; Gustave A. Moe, "The Bureau of the Budget and Governmental Budgeting in Wartime," in Catheryn Seckler-Hudson, *op. cit.*, Unit V, pp. 50-64; Harold D. Smith, *The Role of the Bureau of the Budget in Federal Administration*, reprint of an address given at a joint meeting of the American Political Science Association and the American Society for Public Administration, Dec. 28, 1939, *passim*; Horace W. Wilkie, "Legal Basis for Increased Activities of the Federal Budget Bureau," *The George Washington Law Review*, Apr., 1942, pp. 276, 277, 287 ff.

²⁸ Rowland Egger, "Constructive State Economy," *Commonwealth, the Magazine of Virginia*, Jan., 1940, pp. 13 ff.

²⁹ John E. Burton, "Budget Administration in New York State," *State Government*, Oct., 1943, pp. 205-207.

operations. The head of a division of the budget under a department of finance is not as high in the administrative hierarchy as is a department head; and, consequently, he would have less influence than a direct representative of the governor.

Although the President's Committee on Administrative Management³⁰ emphasized the importance of strengthening the budget office as a managerial arm of the President and of making the budget officer a direct representative of the President, Mr. A. E. Buck,³¹ as a member of the Committee's staff, held the view that the Bureau should be a part of the Treasury Department because of the intimate relationship of the work of the two agencies. The accounting agency of a government unit's finances must cooperate with the budget agency in supplying information, but there does not seem to be convincing evidence that the budget staff must be physically connected with the controlling agency in order to obtain aid from it; and the advantage which a staff agency clothed with the prestige of the executive office has over a subdivision of a department in making contacts throughout the administration is highly compensatory.

If the budget function is to be viewed as something more than policing the treasury, collecting and compiling figures, and performing routine clerical tasks, then it follows that the personnel of the budget staff should include personnel trained and experienced in a variety of public administration areas other than accounting. The budget director especially should be a man of foresight and should be qualified to evaluate the relative worth

³⁰ *Report with Special Studies*, 1937, pp. 4, 6, 52. This opinion has been endorsed in principle by Bernard L. Gladieux, *Administrative Planning in the Federal Government*, reprint of an address delivered before the annual conference of the Governmental Research Association, Sept. 8, 1939, p. 23; J. Weldon Jones, *The Execution of the Federal Budget*, reprint of an address delivered before the 26th annual meeting of the American Accounting Association, Dec. 30, 1941, p. 1; Daniel T. Selko, *The Administration of Federal Finances*, 1939, pp. 2, 47-49; *The Federal Financial System*, 1940, p. 116; Efficiency Commission of Kentucky, *The Government of Kentucky*, 1924, p. 208; Robinson and Griffenhagen, *op. cit.*, pp. 27-29, 42; and Tipton R. Snaveley, *A Study of the Fiscal System of Tennessee*, 1936, p. 17.

³¹ "Financial Control and Accountability," President's Committee on Administrative Management, *op. cit.*, pp. 141, 142. Concurrence with this view is apparent in other studies of state organization, although in most cases the advocacy of placing the budget function in a department of finance was secondary to the primary issue of integrating the scattered financial functions. See The Brookings Institution, *Report on a Survey of Organization and Administration in Oklahoma*, 1935, pp. 220, 231; Griffenhagen and Associates, *Report Made to the Special Legislative Committee on Organization and Revenue*, State of Wyoming, 1933, pp. 337, 338; James Karl Coleman, *State Administration in South Carolina*, 1935, p. 76; Institute of Public Administration, *Report on a Survey of Organization and Administration of the State Government of New Jersey*, 1930, p. 49; and Public Administration Service, *Report on Financial Administration in the Michigan State Government*, 1938, p. 28.

of programs and activities and relate them to the whole administrative framework and policy if he is to advise the governor.

It is of equal importance to stress that the director's attitude toward administrative officials should be that of a counselor and not of a crusader. Neither the governor nor his budget assistants can achieve the desired goal if harmonious relationships with administrative officials are not maintained. Naturally enough, the heads of the various offices resent an outsider who presumes to know far more about the business of each and every department than does anyone else and who "takes up the cudgels" in trying to tell administrators how to run their businesses.

Departmental organization.

The exact budget functions in the departments and other establishments of Kentucky vary according to the types of individuals who perform the work, the volume and complexity of the work, size of the organization, and the degree to which the functions are developed. Two primary functions in any department are: (1) to obtain the funds necessary for effective operation of the various activities of the department; and (2) to maintain an effective relationship between the allotment and prudent expenditure of these funds. In most of the state departments the decisions relative to these two functions are made by the department head, and the routine work of compilation and maintaining control accounts is delegated to a clerk in the executive office of the department.³² For example, when estimates of expenditures are prepared in the Department of Revenue, the budget clerk in the Commissioner's office first prepares them using the financial records showing previous years' expenditures; then they are given to the executive assistant, who reviews them and confers with the division heads upon their needs for the ensuing biennium; and finally, they are received by the Commissioner himself, who makes the final requests for appropriations basing his decisions on the information supplied him by the executive assistant and on his own work policy for the entire department. In some departments, the Department

³² Conference with Mr. Frank D. Peterson, Aug. 5, 1944, and personal observation. The departmental budget organization in a larger governmental unit is necessarily more elaborate; cf. Verne B. Lewis, *Budgetary Administration in the United States Department of Agriculture, 1941*, pp. 10-13.

of Finance and the Department of Business Regulation for example, the practice is to make the division chiefs responsible for the general financial administration of their units, including the preparation of estimates. They make decisions, presumably, in compliance with the department head's general policy of expanding or contracting activities.³³

This is probably a good point at which to emphasize that budgeting is not bottled up in a vacuum in the central budget office, but that it permeates the whole administrative structure. It is found at the first link of the administrative chain where the person in charge of the service division, and even the unit supervisors, of the Department of Revenue, for example, must decide whether the addition of two more stenographers is necessary to maintain an efficient level of performance and goes on through decisions on the same question by the Commissioner of Revenue, the Director of the Division of the Budget, the Governor, and the General Assembly. Once the appropriations are made, determination of an effective balance between allotments and expenditures is especially important to the bureau chief and his assistants, since these officials are held responsible for the results obtained in their respective fields. At the same time, under the budget system, nothing that involves the expenditure of money is outside the purview and interest of the department head and the central budget office, so that there exists a fusion of responsibility.

PROCEDURE IN PREPARING THE BUDGET DOCUMENT

The call for estimates

The first formal step in preparing the Governor's budget is the preparation of the budget estimate sheets by the Division of the Budget and their distribution to the budget units. All agencies of the state which receive state money should submit expenditure estimates. However, in view of the fact that a policy has been adopted of making the highway function independent of regular budget procedure, the Kentucky Department of Highways does not submit the usually required estimates.³⁴

The Division of the Budget is required to furnish such forms as it may prescribe to the heads of the budget units for their use

³³ *Loc. cit.*

³⁴ Conference with Mr. Frank D. Peterson, Oct. 18, 1944.

in preparing estimates, to furnish a statement of the expenditures of the unit for the current year, and to instruct them on the procedure to be followed in making estimates.³⁵ In addition the Division is responsible for estimating expenditures for county officials and court costs, debt and interest, and other expenditures which are not the result of activities of specific departments or agencies.³⁶ Estimates of all revenues and receipts are prepared by the Division of the Budget with the aid of collecting agencies.³⁷

In order to complete the budget plan in time for submission to the General Assembly not later than the third Monday of its biennial session, the estimate forms must be distributed on or before October 15 of each year preceding the regular session.³⁸ This means that expenditures must be estimated eight months before the beginning of the budget period on July 1 and thirty-two months before the end of the period. The length of the period makes estimation a difficult problem, but the preparatory stage in Kentucky is not as far removed from the beginning of the fiscal period as it is in most states.³⁹

When estimate forms are distributed, they are ordinarily accompanied by a statement of the general fiscal policy of the administration in order that the departments may adjust their expenditure requests in advance of submission. The following statement accompanied the budget forms distributed for the 1942-44 biennium:

"In the matter of estimates, economy is urged. It is the purpose of the Administration to maintain the present sound financial basis of operations. While a complete liquidation of the present State indebtedness by January 1, 1942 is contemplated, yet the completion of improvements now in progress is urgent. The estimate of receipts for the current year is approximately \$2,500,000 less than actual receipts during the last completed fiscal year and due to economic conditions resulting from the present world affairs a probability of further decreases exists. This probable decrease in revenue together with the necessity for completing the improvement and rehabilitation program in progress at the respective charitable and eleemosynary in-

³⁵ Acts 1934, chap. 25, art. 3, sec. 5; KRS 45.060.

³⁶ Public Administration Service, *Handbook of Financial Administration*, Commonwealth of Kentucky, 1937, pp. 23, 24.

³⁷ *Loc. cit.* In practice the Division simply adopts tax and license estimates which the Department of Revenue prepares. The Department of Finance forecasts other revenues.

³⁸ Acts 1934, chap. 25, art. 3, secs. 5, 10; KRS 45.060, 45.100.

³⁹ Sundelson, *op. cit.*, p. 363.

stitutions will prevent any increases in ordinary, operating expenses. Therefore, I earnestly solicit the full and hearty cooperation of all agencies to the end that we continue our fundamental policy of keeping expenses within the limits of income."⁴⁰

Another aid to department heads accompanying the estimate forms is a bulletin issued by the Division of Purchases and Public Properties of the Department of Finance.⁴¹ This Division, as the state's centralized purchasing agency, is conversant with price trends and is best equipped to make price forecasts. The bulletin which it prepares is intended to serve as a guide to prices to be used in estimating future expenditures for materials, supplies, and equipment.

Estimate Forms

The forms prescribed by the Division of the Budget may vary from year to year, but a comparison of those used for the 1938-40 biennium⁴² with those used for the 1942 biennium⁴³ indicates that they are similar. The procedure is virtually the same for each biennium—two copies of each form are prepared, the duplicate copies for the departmental files and the original copies for submission to the Division of the Budget; and before the forms are sent to the several departments, the data for the past biennium are tentatively entered by the Division of the Budget on the basis of the records of the Division of Accounts and Control and the personnel roster maintained by the Division of Personnel Efficiency. The forms are arranged to show expenditures for the past year, estimates of current year expenditures, requests of the departments for the ensuing two years, recommendations of the Governor for the ensuing two years, and a column for comments. Revolving funds are separated from the general fund,⁴⁴ since the Governor and his budget staff have no authority to alter the former. The forms include: (a) detail of expenditures for personal services showing the number of persons employed in each agency by class of position; titles and salary rates must be in conformity with the classification plan and salary schedule adopted by the Division of Personnel Effi-

⁴⁰ Kentucky Department of Revenue file copy of Department of Finance budget estimate forms for the 1942-44 biennium.

⁴¹ Public Administration Service, *op. cit.*, p. 24.

⁴² *Ibid.*, pp. 24-32.

⁴³ Kentucky Department of Revenue, file copy.

⁴⁴ Acts 1934, chap. 25, art. 3, sec. 14; KRS 45.140.

ciency; (b) detail of expenditures for services other than personal broken down according to the subsidiary classification of postage, telephone, freight charges, etc.; this analysis by type of service and commodity makes for more careful preparation of estimates and facilitates review analysis; (c) a summary of expenditure estimates by budget units arranged under each department or institution; (d) a form which details and explains any estimates required for capital outlay and replacements; the explanation sets forth the description of the item or project, detailed reasons for the proposed expenditure, how and when the item is to be purchased or constructed, and any other pertinent data necessary to describe fully the need for the appropriation; and (e) a form on which the head of each spending agency supports and justifies his requests; this justification is quite frequently put into a letter which accompanies the estimates when they are returned to the Division of the Budget.

The revenue estimates show figures by source for the past year, current year, and next ensuing two years, the latter shown by quarterly periods. Forms for earlier years called for estimates of accruals, but this practice has been dropped since the bulk of revenue receipts is derived from income and excise taxes⁴⁵ which are received when assessed; any accruals resulting from additional assessments, such as delinquencies and corrections after audit, are minor in amount, and collections usually occur within the fiscal year.

Estimating expenditures

Expenditure estimates are an essential foundation of the budget, and the care with which they are made largely determines the success with which the budget is administered. If the objective of those responsible for the administration of public affairs is to secure the greatest benefits to the citizenry in relation to the taxes imposed, it is essential that expenditure estimating be considered of vital importance, and not merely a routine clerical task.

No exact rules have been formulated for judging expenditure needs in Kentucky or elsewhere. Budgetary laws contain no provisions on this point. It is for this reason that estimating

⁴⁵ Kentucky Department of Finance, *Biennial Report*, for the fiscal years ending June 30, 1942 and June 30, 1943, pp. 35, 86, 121.

must be left to the discretion of the department heads and their budget aides. The estimates will be good or bad in direct proportion to the amount of experience in the work, the foresight, sagacity, and integrity of the estimators. Although the task of estimating cannot be reduced to an exact science, it can be accomplished so that estimates are more than bad guesses.

In the first place, breaking the expenditure analysis down by function, organization unit, activity, character, and object⁴⁶ will produce a set of figures which more accurately approaches exact estimates than a lump-sum figure for a budget unit will do. Second, estimates can approach real needs more accurately if based upon work programs, rather than upon previous year's expenditures and if cost accounting is used for studying personnel, material, and equipment requirements.⁴⁷ Most of the administrators in Kentucky do not keep written and exact records of work loads in their departments, but depend upon a general mental picture of the quantity of service performed and upon past year's requirements in making their requests.⁴⁸ However, work norms have been developed in some instances. The Department of Revenue, for example, keeps records of work loads (the number of tax forms filed in each unit, etc.) and also utilizes cost accounting techniques in determining the cost of collecting specific taxes.⁴⁹

Records which show work loads in quantitative terms not only aid the administrator in estimating, but provide information which he can utilize in many other instances, for example determining personnel requirements. These same records again would benefit the Division of the Budget and the Governor in determining the best allocation of the resources. Such specific information could be required of the budget units in Kentucky, for the law states:

"The head of each budget unit . . . shall submit to the Department of Finance estimates of the financial require-

⁴⁶ Municipal Finance Officers Association, *Municipal Budget Procedure and Budgetary Accounting*, 1942, p. 22.

⁴⁷ *Ibid.*, p. 23; E. O. Griffenhagen, "Utilizing Unit Costs to Measure Governmental Efficiency," *Proceedings, Citizens Conference on Government Management*, 1940, pp. 133 ff.; and William E. Mosher, "The Development of Work Units in Public Administration," *Public Administration Service, The Work Unit in Federal Administration*, 1937, pp. 3-7.

⁴⁸ Conference with Mr. Frank D. Peterson, Aug. 5, 1944.

⁴⁹ See Kentucky Department of Revenue, *Twenty-fifth Annual Report*, 1943, pp. 21-24.

ments and receipts of his budget unit for the next two fiscal years, on the forms and in the manner prescribed by the Department of Finance, *with such explanatory data as is required by the department. . .*" (italics supplied).⁵⁰

The truth is that the budget staff agency in Kentucky is too small and works as an entity for such a short time that it has neither the time nor the personnel to make use of more detailed information. In addition, the staff of the Department of Finance itself is adequate neither to aid departments in the installation of cost accounting procedures nor to utilize cost information if it could be obtained.

Estimating revenues

The bulk of the work of estimating state revenues and receipts is done in the Department of Revenue. Table 2 shows for one fiscal year both the amounts and types of receipts which are estimated by the Department of Revenue and the Department of Finance. As is evidenced by the table, the Department of Revenue estimates all tax receipts, which covers more than 75 per cent of the total. The job of estimating is begun by the head of the Division of Research and Statistics within the Department of Revenue about a month before the date on which the estimate forms are sent out by the Division of the Budget, and considerable time and energy are applied to the task. The Director of Research and Statistics collaborates with the Commissioner of Revenue and his assistant, who reach final judgments. The Division of the Budget accepts these revenue estimates without revision.

The non-tax receipts are estimated by the Division of the Budget in cooperation with the collecting agencies.⁵¹ The departmental fees, sales, and rentals for the general fund include such items as legal process agents' fees and corporation filing and recording fees for the Secretary of State, textbook sales of the Department of Education, examining and inspection fees for other departments, etc.; for the revolving, trust, and agency funds the largest items are tuition and board and room fees of state colleges and examination and registration fees for various

⁵⁰ Acts 1934, chap. 25, art. 3, sec. 6; KRS 45.070.

⁵¹ Public Administration Service, *loc. cit.*

state boards; and for the state road fund, they include such items as truck permit fees, sales of junk, etc.⁵²

Table 2
ESTIMATED REVENUE RECEIPTS IN KENTUCKY, 1944-45

Estimated by Department of Revenue		Estimated by Department of Finance	
GENERAL FUND			
Property and inheritance taxes (except franchise corporations)	\$ 8,276,000.00	Departmental fees, sales, and rentals.....	\$ 90,000.00
Income and special corporation taxes	11,056,000.00	County and court costs	1,150,000.00
Alcohol taxes and licenses	6,037,000.00	Miscellaneous revenue..	40,000.00
Excise taxes (other than alcohol)	5,169,000.00		
License taxes (other than alcohol)	1,737,750.00		
Total	\$30,275,750.00		\$1,230,000.00
REVOLVING, TRUST, AND AGENCY FUNDS			
Special corporation and property taxes... \$	265,000.00	Departmental fees, sales, and rentals...\$	2,567,781.00
Licenses (other than alcohol)	905,200.00	Subventions and grants	8,155,800.00
		Miscellaneous revenue..	34,080.00
Total	\$1,170,200.00		\$10,757,661.00
STATE ROAD FUND			
Excise taxes	\$10,490,000.00	Departmental fees, sales, and rentals ...	\$21,600.00
Licenses and permits..	2,379,250.00		
Total	\$12,869,250.00		\$21,600.00
Grand total	\$44,315,200.00		\$12,059,261.00

Source: Commonwealth of Kentucky, *The Executive Budget*, for the biennium 1944-46, pp. 20-22, 28, 29.

Review and revision of estimates

The spending agencies are required to return their estimates to the Division of the Budget by November 15, one month after they receive them.⁵³ At this time the Division of the Budget

⁵² Kentucky Department of Finance, *Biennial Report*, *op. cit.*, pp. 29, 86, 123.

⁵³ Acts 1934, chap. 25, art. 3, sec. 6; KRS 46.070.

studies the individual estimates for error, and aggregates all requests to compare with total anticipated receipts. In order to enforce the provisions of the budget and financial administration act and to get full information, the Commissioner of Finance or a representative of the Department of Finance as designated by the Commissioner has free access during business hours to all books, reports, papers, and accounts in any budget unit and may compel the attendance of witnesses and the production of testimony touching upon the subject under investigation.⁵⁴

As a matter of good politics the budget officer in Kentucky does not revise and reduce estimates himself, but he has private conferences with the Governor at which time they go over the original requests together.⁵⁵ The Governor assumes personal responsibility for the budget as it is finally revised. The Governor-elect has the prerogative of examining the budget report in process and attending all hearings thereon.⁵⁶

The review is one of the most vital steps in the budgetary process and one which is criticised as being non-scientific, partisan, and neglected. Expenditure estimates generally have to be revised downward and the review process is one of determining how "scarce means shall be allocated to alternative uses."⁵⁷ Since department heads are frequently over-ambitious in the expansion of services for their particular department and since they are not familiar with the entire field of government operation and do not know the limitations of financial resources, it is imperative that the Division of the Budget study the total picture—the variations in volume of work, the effectiveness of organization within the spending agencies, the utilization of new methods and machinery, and the adoption of work measurement standards, including cost accounting techniques—as an effective means of giving the taxpayer the most service from his tax dollar.

For the most part standards for the evaluation of performance are yet undeveloped in Kentucky, partly because there is not time to analyze the work programs of each department extensively in the short time allotted to budget preparation. The

⁵⁴ Acts 1934, chap. 25, art. 9, sec. 2; KRS 45.330.

⁵⁵ Conference with Mr. Frank D. Peterson, May 11, 1944.

⁵⁶ Acts 1934, chap. 25, art. 3, sec. 9; KRS 45.090.

⁵⁷ V. O. Key, Jr., "The Lack of a Budgetary Theory," *American Political Science Review*, 1940, p. 1138.

fiscal year in Kentucky, as in most states, begins on July 1, and the budget document must be ready for submission to the legislature six months prior to this date. In order to minimize the time elapsing between the preparation of the financial plan and the opening of the financial year, the formulation stage is squeezed at both ends.

At the present time in Kentucky the review is considerably influenced by the personality and information of the reviewers—the Governor, the members of the Legislative Council, and the Budget Director.⁵⁸ This is always true to some extent since each of these persons, except perhaps the Budget Director, lacks information regarding the detailed needs of every department and so is inclined to be most concerned with the limited number he does know and to be influenced by conferences with particular department officials. For this reason again it would be profitable to equip the Governor with a full-time budget staff agency, which would continuously study the needs of the government, the possibilities of preventing waste, etc., and for the reviewers to utilize the information such a budget staff agency could supply.

Another fault of the Kentucky review process is the failure to analyze adequately the revolving fund receipts of the various departments before the general fund appropriations are recommended. The Governor does not give this factor adequate attention in the first place, and the legislature follows the same line of least resistance; one budget officer, when asked if the legislature considered the dedicated receipts of the agencies as a factor influencing a just and economical appropriation answered: "They don't know and for the most part they don't care."⁵⁹

Kentucky has made one valuable contribution to the review process. Although the whole budgetary procedure is characterized by exactness and finality at certain points, the stage between the Governor's review and the authorization by the legislature is one which includes highly developed elements of cooperation and collaboration. The budget calendar provides that conferences attended by the Governor, the representatives of the

⁵⁸ Conference with Mr. Frank D. Peterson, May 11, 1944; conference with Mr. Warren Van Hoose, Assistant Budget Director, Kentucky Department of Finance, Sept. 6, 1944.

⁵⁹ Conference with Mr. Warren Van Hoose, Sept. 6, 1944.

Division of the Budget, and the individual department heads be held during the month of November, at which time the estimates can be discussed and final decisions made.⁶⁰ The Governors since 1936 have invited the members of the Legislative Council to attend these hearings and to give advice with respect to policies which should be reflected in the budget plan. For the most part the Governors have incorporated the recommendations of the Council in their executive budget proposals.⁶¹ This practice indirectly gives the public, through its representatives, an opportunity to be heard and works advantageously for the Governor as well in that he is able to feel the temper of the General Assembly before making his decisions.⁶² The budget is one of the most important pieces of legislation the Governor must consider; if he cannot get his financial plan accepted, his whole plan of administration may crumble. In Kentucky at the budget hearings the administration and the legislature "get together," so to speak, to give their opinions. The result of such collaboration is noticeable. The passage of a general appropriation bill reflecting the Governor's expenditure program was made with practically unanimous vote from 1938 through 1942,⁶³ which is a strange proceeding in most states and which is certainly foreign to the Congress of the United States.

⁶⁰ Public Administrative Service, *op. cit.*, p. 32. In practice these conferences are largely held in December.

⁶¹ Gov. Keen Johnson, *Kentucky Government, 1939-1943*, p. 54.

⁶² The effectiveness of the Governor's use of the Legislative Council in this connection is allegedly impaired by the jealousy of members of the General Assembly who are not members of the Council. Kentucky experience suggests, moreover, that the plan reaches maximum efficiency only if the Governor adopts a policy of close collaboration with legislators. See James W. Martin, "Current Developments in Kentucky State Budgeting," *Southwestern Social Science Quarterly*, Dec., 1944, pp. 197 ff.

⁶³ Johnson, *loc. cit.*

CHAPTER V

THE BUDGET DOCUMENT

LEGAL PROVISIONS RELATIVE TO THE BUDGET DOCUMENT

The budget takes shape in the form of a document, which is a collection of summary and detailed statements setting forth the financial plan, schedules showing the past and present operations, and, sometimes, the bills required for legislative authorization. By means of this document the executive's financial policy is presented to the legislature for consideration and action.

On the whole, the legal provisions throughout the states are not very specific as to the form of the budget document. Most state laws prescribe the general content and require certain financial statements, but permit the budget information to be set up in various ways. The degree of specificity can be illustrated by dividing the states into three groups.

1. In Arkansas the Budget Committee of the General Assembly prepares the necessary appropriation bills and a budget document is not required. The Kansas law provides that the Governor submit his recommendations in a budget message, and no further requirements relative to the preparation of a document are made. In North Dakota the State Budget Board sends its recommendations for appropriations to the Legislature but does not prepare a complete document. Georgia, Illinois, Mississippi, Oregon, and Pennsylvania make only a general requirement that a budget plan be submitted to the legislature and do not make definite stipulations as to the contents.

2. In more than half of the states¹ the laws prescribe the contents of the budget document, but the amount of data required and the exactions of the law in making the requirements vary from state to state.

3. The Alabama, Colorado, Connecticut, Iowa, Maine, Maryland, Minnesota, Missouri, Montana, and New Hampshire

¹ Ariz., Calif., Del., Fla., Idaho, Ind., Ky., La., Mass., Mich., Nebr., Nev., N. M., N. J., N. Y., N. C., Ohio, Okla., R. I., S. C., S. D., Tenn., Tex., Utah, Vt., Va., Wash., W. Va., Wis., and Wyo.

laws not only prescribe certain contents but also stipulate in what form they shall be compiled.

As a practical matter it may be wise for budget officers to be legally compelled to produce certain information for the benefit of the legislatures and the public; it does not follow that requirements of law always make for the most comprehensive and understandable document, nor does it mean that the law is followed to the letter. Detailed legal provisions, especially as to form, may hinder rather than aid in the preparation of a simple and clear document. For example, the law of Maryland has a provision dividing the budget into two parts; one part is called "governmental appropriations" covering interest and principal due on state debt, salaries prescribed by law, appropriations for the legislative, judicial, and executive branches, or, in other words, expenditures which might be termed obligatory; the second part is designated "general appropriations" and includes all other expenditures, which are more or less optional.² The division on such a basis means cutting across organizational units and splitting the requirements for current purposes into two parts. As a practical arrangement this was regarded as unsatisfactory; so an arbitrary division of the budget document was made along organizational lines.³

Kentucky

Kentucky's law relative to the contents of the budget document is neither as specific as that of Maryland nor as general as that of Kansas or North Dakota. Viewing the document in the light of compliance with statutory provisions is not an attempt to evaluate these provisions, but more a basis of approach in examining and revealing the contents of the Kentucky document. In abbreviated form the legal requirements are as follows:

1. A budget message signed by the Governor.
2. Summary statements of the Commonwealth's financial condition to include:
 - (a) a comparative consolidated balance sheet showing surplus or deficit, as the case may be, at the close of the last two fiscal years concluded;
 - (b) summary statements of fund balances showing in detail for each fund the current account surplus or deficit at the beginning of each of the two fiscal

² *Maryland Constitution*, art. 3, sec. 52.

³ A. E. Buck, *Public Budgeting*, 1929, p. 54.

years last concluded actual income of each year, total net appropriations for each year, and total expenditures of each year;

- (c) similar summary statements of the estimated fund balances for the current fiscal year and each of the next two fiscal years.

These statements shall be accompanied by such other schedules as the Governor deems advisable.

3. Statements of receipts for each of the last two fiscal years concluded and estimates of the same for the current and each of the next two fiscal years, to be itemized by organization units and sources and by funds and sources, and to show further current income, refunds, sale of assets, and collections of prior years' revenue. Existing sources of receipts shall be analyzed and proposed new sources explained.
4. Summary statements of expenditures and disbursements for the two fiscal years last concluded, itemized by budget units under functional heads.
5. Statements analyzing changes in surplus by funds for the last two years concluded.
6. A statement as of the last completed fiscal year and an estimate as of the current fiscal year, showing total funded debt, value of sinking fund assets, net funded debt, and floating liabilities.
7. Detailed comparative statements of expenditures and requests for appropriations by funds, budget units, and budget classes, showing expenditures for each of the two fiscal years last concluded, budget of the current year, and requests of the budget units and recommendations of the Governor for each of the next two fiscal years—all subdivided according to budget classes of ordinary recurring expenses of operation and maintenance, and of extraordinary expenses and capital outlays. Following the list of actual and proposed expenditures should be a brief explanation of the functions of the unit and comments on its policies and plans.
8. A summary statement for each fund of the cash resources estimated to be available at the beginning of each of the next two fiscal years and estimated cash receipts of those years as compared with the recommended appropriations for the same years with recommendations as to how deficiencies are to be met, if they are present.
9. A draft of a proposed appropriation act or acts, embodying the Governor's recommendations for the next two fiscal years to be itemized by budget units for ordinary recurring expenses and by budget classes for extraordinary expenses and capital outlays, which are to be supplemented by such wording as will limit each appropriation to the specific purpose intended. Drafts of such revenue and other acts as may be recommended for putting into effect the proposed plan are to be included.
10. A certificate of the State Auditor as to the accuracy of the statements of financial condition, of receipts, and of disbursements.⁴

⁴ Acts, 1934, chap. 25, art. 3, sec. 4; KRS 45.040.

Both the physical make-up and the contents of the first budget document for the biennium 1938-40 differ from the succeeding three.⁵ The following comments relate to the budget documents from 1940 to date, all of which have the same form.

A more complete discussion of the commonwealth's funds appears in an earlier chapter,⁶ but a few remarks on this point are necessary for the clarity of the subsequent paragraphs. Although the statutes specify that information of various kinds be supplied relative to *each* fund and the law further requires that a separate account be maintained for each revolving, trust, and agency fund,⁷ for fiscal reporting purposes in the budget document and in the Department of Finance reports a group of small funds of the nature of accounts are treated together under the heading "revolving, trust, and agency funds." This method of treatment has practical value, since these funds are numerous and small in amount.⁸ Reference to "revolving, trust, and agency funds" in the following paragraphs includes this whole group of small funds. The remaining funds as titled in the budget documents and other financial reports are: general fund, road fund, National Industrial Recovery Act fund, (no longer used) highway bridge bond fund, highway bridge bond sinking fund, county road trust fund, county road sinking fund, special deposit trust fund, state fire and tornado insurance fund, unemployment compensation fund, and the teachers' retirement fund. The law contemplates the inclusion of all these funds in the budget report, but many of them have been set up to receive dedicated revenue; generally speaking, only the revolving, trust, and agency funds and the general fund are given full treatment in the budget reports. This fact is obvious from the following statements regarding compliance with the law.

Requirements 1 and 2(a) above are fulfilled. In addition to showing a consolidated balance sheet for all funds, separate balance sheets are shown for each fund. Consolidated balance sheets of particular funds are also exhibited. For example, the

⁵ A good description of the 1938-40 budget document appears in Public Administration Service, *Handbook of Financial Administration*, Commonwealth of Kentucky, 1937, pp. 32-34.

⁶ See Chapter III.

⁷ Acts 1934, chap. 25, art. 3, sec. 14, art. 6, sec. 9; KRS 41.290, 45.140.

⁸ Kentucky Department of Finance, *Biennial Report*, for the fiscal years ending June 30, 1942 and June 30, 1943, pp. 223-229 lists 183 of these small funds.

general fund is combined with the revolving, trust, and agency funds in one statement; and the N. I. R. A. fund, while it existed, was combined with the state road fund in another statement.

The operating statements as required in 2(b) are shown for the general fund, the state road fund, and the group of revolving, trust, and agency funds for the bienniums 1940-42 and 1942-44; but in the 1944-46 document these statements are not separated from the analysis of surplus.

Requirement 2(c) is missing entirely. Estimated fund balances and operating statements by funds for the current fiscal year and the coming biennium are nowhere shown.

Receipts of three classes of funds, the general, the road, and the revolving, trust, and agency group, are itemized by fund and source according to requirement 3 and are further itemized for the general and road funds by quarterly periods for each year of the coming biennium. Receipts of the remaining funds of the commonwealth are not shown. Further, itemization by organization unit and fund, as the statute requires, is not included except for the biennium 1940-42, when the receipts of the revolving, trust, and agency group were shown by organization unit. It would seem to be worthwhile, quite aside from the fact that it is required by statute, to continue this statement so that it may serve as a guide in determining general fund appropriations to organization units which also have revolving fund receipts available for expenditure.

Requirement 4 so far as it relates to expenditures is met for the general fund only.

Requirement 5 is met in each document; as to revolving, trust, and agency funds it is most clearly met in the 1944-46 document.

The only statement regarding debt included in the budget documents is one which shows total warrants outstanding for the general and the state road funds for each fiscal year from 1908 to date. A debt statement as prescribed in requirement 6 is not necessary since the state at present is, legally speaking, free from debt (except for the constitutional debt to educational agencies). The final call for interest-bearing warrants was made in March,

1941; a nominal amount of warrants were not presented for payment.⁹

Requirement 7 above is met for disbursements from the general and the revolving, trust, and agency funds as a group.

One of the most regrettable failures to meet statutory requirements adequately is non-compliance with requirement 8 above. The total estimated receipts and expenditures should be combined in one statement in order to present a one-page summary of the budget plan. A suggested form for this purpose is presented below.

Inclusion within the budget report proper of the acts required to put the financial plan into action would seem to bulk the document unnecessarily and be repetitious, although this opinion is not consistently held.¹⁰ Many of the states¹¹ require that the budget makers prepared drafts of appropriation and sometimes revenue bills, and it is customary for budget agencies to perform this task whether the law requires it or not, but the drafts are not usually bound with the rest of the document.¹² The Division of the Budget in Kentucky prepares drafts of appropriation bills, although they are not bound with the budget document.

A certificate by the Kentucky State Auditor as to the accuracy of the financial information as required in the statutes is not presented, although this statement with the Auditor's cooperation could easily and properly be included.

SUGGESTED FORM AND CONTENT

Nothing approaching a uniform method of compiling budget documents has yet been developed among the states. In physical appearance budget documents exemplify all sizes from regular octavo to large atlas and vary in length from 18 pages, as in the Nebraska report for the 1941-43 biennium, to over 700 pages, as in the current New Mexico and California documents.

⁹ Commonwealth of Kentucky, *The Executive Budget*, for the biennium 1944-46, p. 34. This small amount was charged off July 1, 1944.

¹⁰ Buck, *op. cit.*, p. 57 makes the following statement: "While the inclusion of these measures in the budget document is not widely sanctioned by present usage, it is nevertheless quite desirable."

¹¹ Ala., Ariz., Ark., Calif., Colo., Conn., Iowa, Ky., La., Me., N. H., N. Y., N. C., Okla., Tex., Va., Wisc., and Wyo.

¹² Current or recent budget documents for well over half of the states have been personally examined.

New York's executive budget is printed in two volumes, each of which contains over 500 pages. Sometimes the budget documents contain only expenditure data without even a brief statement of governmental income.¹³ Some states do not publish their budgetary plan for general circulation in any form; no effort is made to issue the estimates for public information.

Although it is not possible to develop standard forms on which to present the budget data in view of the fact that the states' financial structures, their tax systems, and their laws are widely divergent, minimum criteria of contents are necessary to make the document of value to legislators and citizens.¹⁴ This type of budget is discussed in subsequent pages with reference to Kentucky.

Budget message

The Governor is afforded the opportunity in the budget message to vitalize the financial plan. He can break away from technical, financial terminology and present his proposals in a vernacular understandable to laymen. The plan when summarized in such a budget message is news, and the papers will rarely fail to give it first-page space.

Obviously, the message will change from period to period as do the general conditions to which it relates, but a comprehensive message will include discussions on the financial condition of the government—whether one of surplus or deficit; an enumeration of the outstanding current revenue and expenditure problems; a complete discussion of the future policy, emphasizing any changes in the tax structure, shifts in expenditures, new outlays, major modifications in departmental or institutional organization, salary standardization, and the social aspects of governmental expenditures; detailed consideration of capital outlay payments; an account of the state's indebtedness; and a discussion differentiating between the non-budgeted expenditures (i. e., expenditures which are authorized by virtue of collection as in the case of the receipts of the Kentucky state road fund and also expenditures which are fixed and uncon-

¹³ See the Ind., Neb., N. D., and Utah documents.

¹⁴ Cf. Buck, *op. cit.*, pp. 56 ff.; Municipal Finance Officers Association, *Municipal Budget Procedure and Budgetary Accounting*, 1942, pp. 30, 31; F. D. Jones, "In Defense of the Budget," *Toward Better Budgeting*, 1941, pp. 12, 13.

trollable, such as interest on debt, maturing serial bonds, actuarial requirements of sinking funds, and any other payments required by existing law) from the budgeted items in order to make clear to the public that part of the total expenditures for which the Governor is responsible by virtue of his recommendations.

Many of the state budget messages are no more than letters of transmittal from the governor or from whoever is responsible for budget preparation.¹⁵ Sometimes a letter of transmittal from the governor is supplemented by a more complete analysis of the budget plan by the chief budget officer.¹⁶

Recent Governors of Kentucky have done a commendable job of presenting the budget plan in their messages. Taking the 1942-44 budget document as a sample, the contents of the Governor's message therein included a full description of the state's financial condition, its indebtedness, and its activities; a discussion of the general financial policy relating anticipated income to estimated expenditures showing why and where increases in expenditures were required; an analysis of the possible fluctuations in the tax resources; and recommendations for legislation which would increase the service of government. Although distinctions were not drawn between budgeted and non-budgeted funds, the message generally was comprehensive. The fusion of a general message with the budget message tends to confuse citizens and thereby to impair the effectiveness of popular control over fiscal policy. That is, the practice sacrifices some of the purposes of the budget message—and by the same token renders the general nonfiscal policy statement more obscure in the mind of the public. Only once, under existing financial control machinery, has a Kentucky Governor thus failed to take maximum advantage of his opportunity to make his program clear.

Other notable examples of budget messages among the states at the present time are those of the governors of California, Connecticut, Massachusetts, Missouri, North Carolina, New Mexico, New York, Rhode Island, and Virginia. Graphs, pie charts, and summary tables have been used in some of these messages. This

¹⁵ For example, see the budget documents of Colo., Idaho, Iowa, Minn., Mont., N. H., and Tenn.

¹⁶ See Colo., Ill., and Miss. documents.

would seem to be a worthwhile practice, for the budget message is usually the only part of the document that is widely publicized; such charts and tables give citizens a more concrete picture of the financial plan than words alone can present.

Budget summary

One of the most essential features of a good budget document, and one which is conspicuously lacking in Kentucky's, is the budget summary. This statement should be brief, but should comprehend the complete financial plan. It should be set up in a manner so as to exhibit a balanced relationship between estimates of income and outgo for the budget period. This does not mean, however, that it should take the form of a balance sheet. In fact, it is more nearly comparable to an operating statement. Simplicity and clarity of statement are the essence of all budget reports and especially of the budget summaries. The budget summary should be set up in such form and in such terminology that citizens can with reasonable effort understand it.

Figure 1 is a suggested form to be followed in a budget summary for Kentucky. The grouping into three funds was made in order to show the general fund plan, which in Kentucky is the budgeted plan, separate from the others, and the state road fund separate from the remaining funds, since its operations are of greater magnitude than any or all of the others. It should be emphasized that *all* funds other than the general and road funds should be included in the third section. Citizens are interested in the magnitude of government operations, and the one place where they should be able to find this information is in the budget document. It often happens that if a budget system is not fully comprehensive and some functions lie outside the scope of budgetary planning and management that the operations of these functions are not fully reported. Failure to include all receipts, earmarked or otherwise, and all disbursements results in a misconception of the government's finances.

Supporting schedules to the budget summary

Since only the broad outlines of the financial plan are presented in the budget summary, details of this outline must be exhibited on supporting schedules. Nearly all budget documents contain a number of such statements; in fact, if careful atten-

Figure 1
GENERAL BUDGET SUMMARY JULY 1, 1944 TO JUNE 30, 1946

Income	Support- ing sched- ule on p...	1944-45	1945-46	Expenditures	Support- ing Sched- ule on p....	1944-45	1945-46
1. General fund				1. General fund			
Surplus or deficit at beginning of year				Current operat- ing expenses			
Tax receipts				Capital outlay			
Non-tax receipts				Debt service			
				Unapprop. reserves			
2. State road fund				2. State road fund			
Surplus or deficit at beginning of year				Current operating expenses			
Tax receipts				Capital outlay			
Non-tax receipts				Debt service			
				Unapprop. reserves			
3. All other funds				3. All other funds			
Surplus or deficit at beginning of year				Current operat- ing expenses			
Tax receipts				Capital outlay			
Non-tax receipts				Debt service			
				Unapprop. reserves			
Total means of financing				Total expenditures			

tion is not given to their form and content, it is likely that the number and nature of these schedules will complicate rather than contribute to a clear understanding of the financial plan.

The legal requirements in Kentucky's budget law provide for certain of these statements of a summary character. Keeping in mind the requirements of the statutes the following supporting summary schedules are proposed for the Kentucky budget report. Different suggestions would be presented if requirements of the law were ignored.

1. A consolidated fund balance sheet as shown on page 11 of the 1942-44 document.
2. Balance sheets by funds as shown on pages 8 and 9 of the 1942-44 document.
3. Summary statements of general and road fund operations as shown on page 14 and 15 of the 1942-44 document, plus a similar statement for all funds other than these two.
4. Analysis of changes in deficit and surplus for the general and state road fund as shown on pages 29 and 30 of the 1942-44 document, plus a similar statement for all other funds.
5. A statement of debt following the statutory stipulations.
6. A one-page summary of all estimated tax receipts by source.
7. A one-page summary of all estimated non-tax receipts by source, preceded by a summary in the same form of data for the two last completed years.
8. A summary of estimated expenses as illustrated in Figure 2, preceded by a summary in the same form of data for the two last completed years.
9. A summary of expenditures in the same form as the statement on pages 39 and 40 of the 1942-44 document.

In compliance with the statutes the first three statements should give information for the last two fiscal years concluded, the current fiscal year, and for each of the two ensuing years. The information of the fourth statement should relate to the last two fiscal years concluded. The debt statement, prepared to reflect the constitutional debt to public education in the absence of other credit obligations will show the situation as of the close of the last completed fiscal year and the estimated status as of the close of the current fiscal year (inclusive of floating obligations). The coverage of statements 6-9 inclusive has been indicated already.

Figure 2

**SUMMARY OF ESTIMATED EXPENDITURES BY CHARACTER
AND OBJECT CLASSIFICATION JULY 1, 1944 TO JUNE 30, 1946**

	General fund	State road fund	All other funds
	1944-45	1945-46	1944-45
	1944-45	1945-46	1944-45
Current operating expenses:			
1. Personal services			
2. Services other than personal			
3. Materials and supplies			
4. Other current expenses			
Total			
Capital outlay:			
1. Land			
2. Buildings			
3. Machinery and equipment			
Total			
Combined Total			

Detail of estimates

Detailed statements of the estimates of income and expenditure complete the statement of the financial plan. Generally, the expenditure estimates are grouped according to organization unit and object and the revenue estimates by source and fund.

In some budget documents¹⁷ expenditures are itemized to a fine detail showing the number and class of positions, the postal, telephone, and other service charges, the materials to be purchased, and other breakdowns. This practice usually contributes more to the bulk of the budget report than to its value. Legislators have neither the time nor the will to examine expenditure estimates in such detail and are interested primarily

¹⁷ See, for example, the documents of Calif., Fla., and N. Y.

in causes for changes in certain classes of expenditure. The detail of this information they can obtain upon request from the budget officer. In other documents¹⁸ expenditures are grouped by funds. In many cases this arrangement cuts across organization units, and to examine the total expenditure requirements of a given department one must look under the several funds. The department or agency responsible for the expenditure is of primary significance and the fund, secondary.

Kentucky's budget law calls for:

"Detailed comparative statements of expenditures and requests for appropriations by funds, budget units and budget classes, showing the expenditures for each of the two fiscal years last concluded, the budget of the current year, and the requests of each budget unit and the Governor's recommendations for appropriations for each of the two ensuing years, all distributed according to budget classes of ordinary recurring expenses of operation and maintenance, and of extraordinary expenses and capital outlays. . . ."¹⁹

A summary statement of expenditures by organization unit and function for the three years preceding and for the ensuing two years is shown on the first page of the detailed estimates section in the Kentucky reports. Then the estimates are presented separately by departments of government as the main classification and are further detailed by fund, by budget unit under each department, and by budget class or object of expenditure under each budget unit. Five classes of expenditures are shown: personal services, services other than personal, materials and supplies, other current expenses, and capital outlay. A general statement of the organization and functions of each department precedes the estimate figures as an aid in interpreting the purpose of the expenditures.

The detailed estimates in the Kentucky budget documents are clear and well presented, but they are not complete. Disbursements from the general fund and the group of revolving, trust, and agency funds are the only ones that are shown. This does not, of course, reveal the total expenditures of the state. The most notable omission of funds is the state road fund, which means that the expenditures of the Department of Highways

¹⁸ See the Ill. and N. Y. reports.

¹⁹ Acts 1934, chap. 25, art. 3, sec. 4; KRS 45.050.

are not included.²⁰ Although the law clearly contemplates that the Department of Highways shall be as completely subject to budgetary control as the earmarking of its support will permit,²¹ the Department of Finance does not even show Highway Department estimates in the budget document. Certainly, in this report to the General Assembly the activities of this "budget unit" and its plan for the ensuing fiscal period should be fully shown.²²

The income estimates are usually presented by source and by fund. In many cases the income side of the budget plan is neglected even to the extent that some states fail to give any idea as to how expenditures are to be financed.²³ It is not unusual for states to report only general fund receipts or otherwise to omit receipts of some of its funds.

There is no one place in Kentucky financial reporting where a complete picture of the state's income is shown. The budget reports show receipts of the general fund, state road fund, and the group of revolving, trust, and agency funds only. This covers only approximately 80 per cent of the total.²⁴

The law requires:

"Statements of income and receipts for each of the two fiscal years last concluded, and the estimated income and receipts of the current fiscal year and of each of the two ensuing fiscal years. The statements of income and estimated income shall be itemized by sources, by organization units and sources, and by funds and sources. The statements of receipts and estimated receipts shall be itemized by organization units and sources, and funds and sources, and shall show separately, receipts from current income, receipts from refunds and reimbursements of expenditures, receipts from sale of assets, and receipts on account of the income of prior years, all detailed by source. . . ."

Income and receipts in Kentucky phraseology are differentiated on the basis that the former represents net addition to

²⁰ There are included among the miscellaneous appropriations recommendations for maximum amounts to be spent out of the state road fund for administration and highway patrol and a recommendation for the maintenance of certain rural highways.

²¹ See, e. g., KRS 45.010, 45.040, 45.050, and especially 45.150 and 45.170. Recent experience in Minnesota illustrates the fact that, although earmarking greatly cripples budgetary management, executive control over an agency supported by earmarked revenues can be largely effective.

²² In fact, of course, the law contemplates, and sound financial policy requires, that such a department should be as much as any other within the purview of the budget in every respect except as to method of support.

²³ See the Ind., Neb., N. D., and Utah documents.

²⁴ See Table 1.

²⁵ Acts 1934, chap. 25, art. 3, sec. 4; KRS 45.040.

assets and the latter may represent only a conversion of assets. In the budget documents both income and receipts are shown by source for the general, road, and revolving, trust, and agency funds. They are shown by organization unit and source for the revolving, trust, and agency group for one biennium only, 1940-42. It would seem to be especially worthwhile to continue showing this revenue by organization unit. If legislators are to make wise decisions as to the allocations of state money, they could utilize a statement of the receipts of the organization units through the revolving funds in determining general fund appropriations.

On the whole, the detail of expenditure and income estimates are well presented, but they are limited in their coverage. To present a complete picture of the state's financial plan, it should be emphasized that all receipts and all expenditures should be shown in both the various summary statements and in the detail of estimates.

Arrangement of the budget statements

Kentucky's budget document has three parts: (1) the budget message, (2) the financial statements, and (3) the detail of expenditure estimates, requests, and recommendations. The revenue estimates are lodged in the midst of the statements showing the financial condition of the state. A more logical arrangement would be to place the detail of revenue estimates with the detail of expenditure estimates. This would result in the following arrangement: part one, the budget message; part two, the budget summary, supporting summary schedules, and the legally required statements concerning the financial condition of the state; and part three, the detail of revenue and expenditure estimates. Drafts of appropriation and revenue bills are omitted from this arrangement on the ground that they would be repetitious of material elsewhere presented.²⁶

²⁶ This is not to suggest, of course, that these bills be neglected.

CHAPTER VI

AUTHORIZATION OF THE BUDGET

THE ROLE OF THE LEGISLATURE IN BUDGETING PROCEDURE

At first glimpse there appears to be a marked conflict in the relationship of the executive and legislative branches in the matter of planning a budget program for a government unit. Granting the postulate that the executive is in the strategic position to evaluate the expenditure requests of the spending agencies and to coordinate the financial program and accepting the principle that to hold him responsible for the administration of state activities demands giving him a voice in defining the activities, the question has been asked whether the executive budget system does not by concentrating authority in the executive diminish popular control over the purse and reduce legislative action to a perfunctory voting of the budget.¹ The answer to the question necessitates defining and delimiting the responsibility of each branch in formulating the state's financial policy. It should be emphasized, first, that the ultimate objective of both branches should be to prepare as sound and effective a financial program as circumstances permit. An executive budget system requires a governor, as chief administrator, to collect and assimilate the requests for appropriations of all the spending agencies and to present these requests, along with other required information, to the legislative body. If the governor has recognized and fulfilled his responsibility, he will have reviewed the details of the requests thoroughly and revised them to conform with his general financial policy and with the estimated revenue receipts, so that he submits to the legislature a carefully studied and comprehensive budget plan. The legislature is charged with the duty of reviewing the governor's financial plan. It has a definite responsibility to reject, to decrease, or to increase any

¹ See Robert Luce, *Legislative Problems*, 1935, pp. 344-348, 371 ff. for the nature of the arguments of those who question executive superiority in coordinating the financial plan. Lucius Wilmerding, Jr., *The Spending Power*, 1943, chap. 13 supports the belief that the Congress of the United States has sufficient power to control the purse, but that it has failed to develop machinery and methods of control to a satisfactory degree.

proposed revenues or expenditures not consistent with its interpretation of what the public desires.

However, practice in American government units indicates that the line of demarcation drawn in the preceding paragraph is more theory than fact. Legislative modification of the executive plan has sometimes extended to the point of substituting a legislative budget for the executive budget. And again, by exerting indirect party leadership powers legislative accomplishments of governors in propelling their budgets through the legislatures have earned for them the appellation of "chief legislator." Perhaps there can be no inviolate rule which would clearly limit the area of responsibility of each branch and which would apply in all circumstances. A complexity of executive-legislative relationships is involved in voting the budget.

Executive influence in authorizing the budget

The amount of authority given to the executive over the voting of the budget is a factor in determining the legislature's role and responsibility. While voting the budget is essentially a legislative function in democratic political systems, this is not the circumstance in all countries. In some governments there is a full authorization of the budget by the executive with only a formal legislative sanction. This does not usually happen under normal conditions and is characteristic of the dictator countries. Under the Japanese system the budget is largely determined by the executive, since certain expenditures amounting to about three-quarters of the total budget may not be altered by the Diet.² Sometimes the parliamentary and congressional governments provide for executive authorization in case the legislature fails to act in a specified time. For example, in Chile the executive budget becomes effective on the first day of the fiscal year if the Chilean Congress has not voted on it prior to that time.³ Second, there may be limited determination of the budget by the executive subject to legislative scrutiny and approval. This is the practice which has developed under the English budget system, now largely copied by the British Dominions.⁴ The House of Commons, by a self-denying rule of

² A. E. Buck, *The Budget in Governments Today*, 1934, p. 90.

³ *Ibid.*, p. 88.

⁴ *Loc. cit.*

long standing, has established a procedure under which budgetary initiative passes completely to the executive, no monetary proposals being considered by the House unless recommended by the Cabinet.⁵ The effect is to limit the action of the House to eliminations and reductions only, and the Cabinet may decline to accept these revisions if they are at all important. A few of the American states have adopted kindred restrictions on legislative action. For example, the Maryland, New York, and West Virginia constitutions provide that these states' legislatures may increase or decrease items relating to legislative and judiciary expenditures, but may only strike out or reduce the remaining budget proposals of the executives.⁶ The statutes of Nevada also limit the Legislature to eliminations and reductions.⁷ Third, the budget proposals of the executive may be preliminary or advisory subject to legislative initiative and action. When acting on the budget, most state legislatures are not bound, either by law or custom, to adhere to these proposals, or to accept them as a full measure of governmental requirements. They may disregard them entirely and devise their own financial program.

The federal government as well as most of the state governments in the United States fall in the third category, and the executives submit to the legislative bodies budget recommendations which are advisory proposals. However, if the law-making body fully realizes that the executive budget proposals supply information designed to assist the appropriating procedure, it will not disregard the executive plan. Instead, the appropriation acts will be such as to impose only the restrictions necessary to insure the proper application of public funds and to modify the budget only insofar as the executive proposals are inconsistent with legislative financial policies.

The Governors of Kentucky since 1936 have been singularly successful in promoting their financial programs without legislative alterations. The administration has prepared the appropriation bill to dovetail with the fiscal program incorporated in

⁵ Merlin Harold Hunter and Harry Kenneth Allen, *Principles of Public Finance*, 1940, pp. 554, 555.

⁶ *Maryland Constitution*, art. 3, sec. 52; *New York Constitution*, art. 7, sec. 4; *West Virginia Constitution*, art. 6, sec. 51. In Md. the legislature may add new items, which are subject to veto.

⁷ *Nevada Compiled Laws*, 1929, sec. 6995.

the budget, and the General Assembly, practically without dissent, has approved the bill as written.⁸ This does not mean that the legislature ought invariably to accept the Governor's budget, much less that full authorization by the executive without legislative sanction is the desired goal. It does mean that the Kentucky General Assemblies have not tried to mutilate the Governors' plans, nor have they tried to substitute their judgment in respect of details of expenditures for the judgment of those in charge of administration.

Executive-legislative cooperation

Another factor which strongly influences the voting of the budget is the degree to which the executive and the legislature cooperate in designing the financial program. Under ordinary circumstances party control affords practically the only unifying force between the two branches. The fundamental difficulty in obtaining cooperation is traceable to the theory of separation of powers. This principle precludes an easy solution, for it tends to discourage collaboration. Many treaties have been written on the subject of checks and balances. One eminent constitutional scholar indicated that there is little cause for the belief that our liberties are dependent upon separation of power when he wrote:

"Among all the modern fallacies that have obscured the true teachings of constitutional history, few are worse than the extreme doctrine of separation of powers and the indiscriminate use of the phrase 'checks and balances.' . . . The true safeguards of liberty against arbitrary government are the ancient legal limitation and modern political responsibility. But this responsibility which in modern times has become fully as important for our welfare as the ancient legal limits, is, I think, utterly incompatible with any extended system of checks and balances."⁹

Several recommendations, such as giving the executive the right to introduce financial measures on the floor and providing

⁸ Gov. Keen Johnson, *Kentucky Government, 1939-1943*, p. 54. The enactment of the last appropriation bill, however, evidenced some conflict between the Governor and the General Assembly; and the Governor's budget was substantially modified. The difficulty may be attributed partly to the fact that he Governor did not maximize his use of the Legislative Council (Cf. James W. Martin, "One Method of Limiting Taxation in the Blue Grass State," *Bulletin of the National Tax Association*, Jan., 1945, pp. 120 ff.) and partly due to the fact that the Governor was Republican and the legislature was largely Democratic. (See *Courier-Journal*, Jan. 2, 1944, sec. 3, p. 1.)

⁹ C. H. McIlwain, *Constitutionalism, Ancient and Modern*, 1940, pp. 144, 145.

that the executive and his cabinet be given an opportunity to join in the legislative debates, have appeared during the course of development of budgeting procedure with a view of promoting more collaboration between the two branches; but little action has resulted.¹⁰ Some states provide that the governor or his representative may appear before the legislature to defend his proposals, and a few, New York, Maryland, and Connecticut,¹¹ require that he appear to give explanations; but the provisions have become practically dead letters of law, owing to the failure of the legislatures to establish the necessary procedure to put them into effect.¹²

Although there is nothing in Kentucky law which requires collaboration between the two branches in the enactment of a budget program, the state has made progress toward effecting a compatible relationship between the Governor and the General Assembly through the medium of the Legislative Council. Essential facts are placed before the Legislative Council, the General Assembly's instrument for advance planning, in the hearings which the Governor convenes before submitting his proposals to the legislature. The Council, acting in an advisory capacity, makes suggestions toward improving the budget plan; and for the most part, the Governor embodies these suggestions in his recommendations.¹³ In this manner the legislature and the administration work jointly in formulating financial policy. The advantages of group thinking, contemplated in the old committee plan of defining the budget-making authority, is secured and pointed responsibility for the plan still remains vested in the Governor.

TRANSMITTING THE BUDGET PLAN TO THE LEGISLATURE

The budget document is usually transmitted to the legislative body as soon as it is printed. This is the duty of the budget-making authority, generally required by specific legal provisions naming the date of transmittal. In the several states the budget maker is required to transmit the budget to the legislature on

¹⁰ A. E. Buck, "Public Budgeting," in *Taxation and Public Policy* (edited by Paul Studenski), 1936, pp. 34, 35.

¹¹ *Maryland Constitution*, art. 3, sec. 52; *New York Constitution*, art. 7, sec. 3; *General Statutes of Connecticut*, 1939 supplement, sec. 52e(k).

¹² Buck, *The Budget in Governments of Today*, op. cit., p. 107.

¹³ Gov. Keen Johnson, loc. cit.

specified dates, generally within the first month of the session. Rarely is the state budget sent to the legislature on the first day of the session. The more common dates for transmitting are the fifth, fifteenth, twentieth, and thirtieth days of the legislative session.¹⁴ The problem connected with the submission date is one of providing the Governor time for formulating the plan and affording the legislators time enough to study the budget plan thoroughly before the session ends and before the beginning of the fiscal year. The Kentucky law provides:

"The State Budget Officer shall have the budget report, as approved by the Governor, printed in such number of copies as the Governor may order, and copies thereof shall be transmitted to the House of Representatives not later than the third Monday after the convening of the General Assembly in regular session."¹⁵

However, it has been reported that few members of the General Assembly see a budget document, aside from the draft of the general appropriation bill, before the budget bills are ready to be passed upon because it is not released from the printers in sufficient time.¹⁶ As a consequence, the legislators are not able to study the complete financial plan in advance of budget enactment. There seems to be little reason for failure on the part of the Governor and his staff to get the complete budget document assimilated, printed, and in the hands of the representatives in time for them to make use of the information it presents. The legislators should make the chief use of a budget document. It is of even more significance to them than to administrators, who, admittedly, need some digest of appropriations to the various departments. Apparently, in Kentucky the legislators utilize only the appropriation bills prepared by the budget staff and reported from the committees, which are neither so detailed in content nor so informative as the budget document.

The submission of the budget to the legislature may be a mere incident in a day's work, passing almost unnoticed, or it may be the most important occasion of the legislative session.

¹⁴ The Council of State Governments, *The Book of the States, 1941-1942*, p. 112.

¹⁵ *Acts 1934*, chap. 25, art. 3, sec. 10; KRS 45.100.

¹⁶ Conference with Mr. Charles Farnsley, former representative in the Kentucky General Assembly, Aug. 25, 1944 and conference with Mr. Frank D. Peterson, former Director of the Division of Accounts and Control, Kentucky Department of Finance, now Comptroller of the University of Kentucky, Aug. 26, 1944. Possibly the existing conditions may suggest deferring the date on which the budget is to be submitted.

American practice tends to make it a purely routine matter. It is possible to present the budget to the legislative body in such a way as to excite public interest in it and to stimulate the examination of its proposals by the members of that body and citizens generally. England has accomplished this to a remarkable degree through the "budget speech," which is delivered by the Chancellor of the Exchequer before the House of Commons, assembled in the committee of the whole on ways and means. It is carefully prepared by the Chancellor and usually takes him two or three hours to deliver, during which time any member of the House may interrogate him.

While our governmental system does not lend itself to the English practice, again owing to the independence of the executive and legislative branches, it is nevertheless possible for the executive to appear before the legislative body and deliver a budget speech in connection with the presentation of his financial plan. Kentucky Governors have followed this practice. In fact, the budget message is broadcast and published in a front-page spread in Kentucky papers. It is undeniable that public interest is heightened by the personal gubernatorial presentation of fiscal plans. Where a summation in the form of a budget message has not made its appearance, a number of difficulties have been noted;¹⁷ and it is probable that a lack of focus upon the governor's fiscal program enables him to shirk a part of his responsibility.

LEGISLATIVE ORGANIZATION

The bicameral legislature

The legislatures of state governments have the same double-chambered organization as their counterpart, the Congress of the United States; although the arguments for this arrangement do not seem to be as valid in one case as in the other. The chief problem of the bicameral arrangement in budgeting is the distribution of budget functions between the two chambers. Certain priority rights are evidenced in a few of the states. The initia-

¹⁷ "Because the budget document has not been presented to the Legislature by means of a formal message from the Governor . . . the legislators have paid scant attention to it. It receives no mention in the House or Senate journals and finds its place on the members' desks along with the reports of the various state officers and institutions." Brookings Institution, *Report on a Survey of State and Local Government in Mississippi, 1932*, p. 360.

tion of revenue measures in Kentucky, for example, is restricted to the lower house.¹⁸ However, the effect of these few priority rights has not been influential in bringing about the limitation of upper chamber power.¹⁹ Students of budget problems have not hesitated to add their blessings to the campaign for unicameral legislatures, not only because the plan would avoid costly duplications, but because the budget can best be considered as a unified plan if it is not acted on by two separate bodies.²⁰ In order to eliminate some of the disadvantages of the bicameral system without completely abandoning it, the procedure of combining the two houses in a joint committee of the whole has been suggested as a smoother means of reviewing the budget plan.

The committee system

The committee system is the core of state legislatures. The legislatures make up their collective minds largely vicariously through their committees.

The typical state legislature has a separate standing committee in each house for the study of the general appropriation bill. The committee in one house usually works independently of the committee in the other house. Before the appropriation bill is presented for open discussion by each house in Kentucky, it is considered by the appropriation committee of each house. During this discussion the Director of the Budget and his staff can be of great assistance to members of the committees in explaining and defending the budget as presented; and, in fact, they are required by statute to be at the disposal of the General Assembly and its appropriation committees while the budget is under consideration.²¹

What appears to be the greatest contribution made by the states is the recognition in some cases that joint committees should coordinate the activities of both chambers and thus avoid

¹⁸ The Senate may propose amendments to revenue bills provided no new matter is introduced. *Kentucky Constitution*, sec. 47.

¹⁹ A. E. Buck, *Modernizing Our State Legislature*, 1936, p. 1.

²⁰ *Loc. cit.* Buck, *The Budget in Governments of Today*, *op. cit.*, pp. 188, 189; *Public Budgeting*, 1929, p. 373; J. Wilner Sundelson, *Budgetary Methods in National and State Governments*, 1927, p. 447.

²¹ Acts 1934, chap. 25, art. 3, sec. 11; KRS 45.110.

duplication of work.²² Most of these states provide only for joint hearings by the committee, which does not as such vote on bills. Nevertheless, there is some indication that a unified legislative approach may be thus fostered.

Legislative councils

As noted before, Kentucky's use of the Legislative Council not only promotes cooperation between the administration and the general Assembly, but also serves as a means of joint discussion of the budget by the two houses, since its membership includes both senators and representatives. The Council when first created consisted of five senators, five representatives, and five administrative officials.²³ In 1938 a special session reorganized and provided for eight senators, appointed by the Lieutenant Governor, eight representatives, appointed by the Speaker of the House, and five administrative officers, appointed by the Governor; the Lieutenant Governor and the Speaker of the House are *ex officio* members and the Governor is an honorary member.²⁴ The 1944 General Assembly changed the provisions again to drop the administrative members, an amendment which was widely construed as a partisan measure.²⁵

The Kentucky Council was one of two similar bodies established in nine states which included administrative officers in its membership.²⁶ Although legislative councils are primarily agencies for harmonizing differences between parties and between houses, the inclusion of administrators aids in also promoting good feeling between the administration and the legislature. Some observers have expressed doubt as to whether good feeling among *all* legislators has been promoted, owing to the jealousy of Senate and House members who are not on the Council.

LEGISLATIVE ACTION ON THE BUDGET

Restrictions on revising the executive budget

As has been mentioned previously, among the American

²² The list of states that operate permanently with some joint committee actively on budgetary matters includes Conn., Ark., Del., Fla., Idaho, Me., Mass., Miss., Mo., N. C., Okla., S. C., Tenn., Va., Wis., and Wyo. Sundelson, *op. cit.*, p. 449.

²³ Acts 1936, 1st spec. sess., chap. 1, art. 21, sec. 2. Under the original law, the Council was officially a joint committee of the General Assembly.

²⁴ Acts 1938, 1st spec. sess., chap. 2, sec. 2.

²⁵ KRS 7.020; James W. Martin, "Kentucky Weakens Centralized State Administration," *National Municipal Review*, May, 1944, pp. 253, 254.

²⁶ The Council of State Governments, *op. cit.*, p. 109.

states there are only four, Maryland, Nevada, New York, and West Virginia, which have effective restrictions on changing executive budget proposals. These states provide that alterations of the budget plan shall take the form of eliminating or reducing items, but recommendations may not be increased. In three of these states, however, the law provides that items of appropriations may be added provided such additions are separate from the original item and refer to but one single object or purpose.²⁷

The most common limitations upon legislative action found in the states are of a general, cautionary nature, such as specifying that the budget shall be balanced or that no appropriation bills shall be considered before the budget bill as planned by the executive is passed upon. For the most part these admonitions are neither binding nor observed.

The Kentucky law stipulates:

"All expenditures of the state and of its budget units shall be made under the authority of an annual or biennial appropriation Act or appropriation Acts, which shall be based upon a budget prepared as provided in this chapter."²⁸

"The financial plan for each fiscal year as presented in the budget report shall be adopted, *with such modifications as are made by the General Assembly*, by the passage of an appropriation Act or Acts and such revenue and other Acts as are necessary for the purpose. . . ." (italics supplied).²⁹

Thus, the Governor in Kentucky, as in most states, prepares a financial program which could be only "wishful thinking" on his part. Whether it will become a legislative reality depends on the personality of the Governor, his party strength, and his relationships with legislative leaders.

The appropriation act

An appropriation act consists of individual appropriations that are defined by statute as:

"authorizations by the General Assembly to a budget unit to expend, from public funds, a sum of money not in excess of the sum specified, for the purposes specified in such authorization and under the procedure specified."³⁰

²⁷ *Ibid.*, p. 112.

²⁸ KRS 45.020

²⁹ KRS 45.050.

³⁰ KRS 45.010.

A budget unit is defined by statute as a department or other unit of organization for which appropriations are made separate from any other organization unit.³¹ This definition is flexible and leaves the preliminary determination of what shall constitute a budget unit to the Governor and final determination to the General Assembly. The Kentucky General Assembly makes appropriations to the various budget units in a lump sum and does not itemize to indicate the specific use of the money. This is a happier arrangement than the line item form of appropriation which specifies the amount to be spent for salaries, for supplies, for traveling expenses, etc., and which seriously impairs executive control over the execution of the budget. "A line item budget becomes a frozen budget, frozen for the ensuing year, practically incapable of adjustments, to the changing needs and changing conditions that may develop during the year."³²

However, a weakness in the Kentucky appropriation acts appears in connection with the revolving funds. Each biennium the various fees, rentals, admittances, sales, etc., collected by the professional boards, institutions, and other agencies of the state government are appropriated in full to these agencies. An appropriation which authorizes an agency to spend as much as it receives in revenue from fees and other sources makes the control over such expenditures more difficult. Similarly, the appropriations out of the state road fund, with minor exceptions, are not specific as to purpose, time, and amount and depend upon the receipts collected into the road fund.

Provisional budget voting

In Kentucky if the legislature should fail to make an appropriation for any fiscal year for any purpose or purposes required to be executed by provisions of existing laws, or if the Governor should veto an appropriation essential to the execution of such a purpose and an appropriation is not passed over the veto, then the existing appropriations, exclusive of appropriations for extraordinary expenditure and capital outlay, continue from year to year until they are altered by the legislature.³³

³¹ Acts 1934, chap. 25, art. 1, sec. 2(g); KRS 45.010.

³² John E. Burton, "Budget Administration in New York State," *State Government*, Oct., 1943, p. 205.

³³ Acts 1934, chap. 25, art. 3, sec. 12; KRS 45.120.

If the existing appropriations are applicable to ordinary recurring expenses and extraordinary or capital outlay expenses, the Department of Finance determines what proportion applies to ordinary recurring expenses; and the proportion so determined becomes the appropriation for the next fiscal year.³⁴ However, as yet a budget has been adopted each biennium prior to the opening of the fiscal year.

Few states provide in their statutes a measure which will cover contingencies of failing to get a budget plan adopted.³⁵ This is probably due to the fact that lengthy intervals between the adoption of the budget bills and the beginning of the period to which they refer are common and provisional budget procedures are seldom necessary.

THE EXECUTIVE VETO

In most jurisdictions in the United States before the voted program becomes effective it must be approved by the executive. Thus the veto power of the governors is a part of the process of budget authorization. In connection with the desire to advance and continue the philosophy of executive budgeting, attempts have been made to give governors exceptional power of review over budgetary items.

Section 88 of the Kentucky Constitution provides:

"Every bill which shall have passed the two Houses shall be presented to the Governor. If he approve, he shall sign it, but if not, he shall return it, with his objections, to the House in which it originated, which shall enter the objections in full upon its journal, and proceed to reconsider it. If, after such reconsideration, a majority of all members elected to that House shall agree to pass the bill, it shall be sent, with the objections, to the other House, by which it shall likewise be considered, and if approved by a majority of all the members elected to that House, it shall be a law; . . . The Governor shall have the power to disapprove any part or parts of appropriation bills embracing distinct items, and the part or parts disapproved shall not become a law unless reconsidered and passed, as in the case of a bill."

Most of the states allow the governor the privilege of the item veto.³⁶ In a few states the governor is given the power to

³⁴ Acts 1934, chap. 25, art. 3, sec. 12; KRS 45.120.

³⁵ Sundelson, *op. cit.*, pp. 507, 519.

³⁶ Council of State Governments, *op. cit.*, p. 78.

reduce as well as invalidate items in the budget bills.³⁷ In most of the states the vetoes are made more effective by virtue of the fact that the legislature may over-ride only with a higher vote than was necessary when the bill was originally passed; a two-thirds majority is customary.³⁸

However, it is now generally recognized that executive influence in the formulation of financial policy and his power in persuading the legislature to adopt his program are more helpful to the development and management of fiscal policies than is the veto power. The latter is, at best, a pruning device; the former can be constructive.

³⁷ Sundelson, *op. cit.*, p. 489.

³⁸ *Loc. cit.*

CHAPTER VII

EXECUTION OF THE BUDGET

Emphasis has been placed on the point that thoroughly satisfactory budgetary procedure cannot be established unless it rests upon an integrated administrative structure. An integrated administrative system is one in which the several services and institutions are grouped according to their functional character into departments, all of which are closely coordinated under the supervision and control of the governor. The system carries with it the requirement that the heads of these departments shall hold their offices by appointment by the governor and shall be subject to removal by him and that the line of administrative authority shall thus run through the governor to the legislature, instead of directly to that body. Under other conditions it is exceedingly difficult, if not impossible, for a governor, even though he may be directed by statute to formulate a budget, to prepare a document that would be more than a compilation and revision of programs prepared by other officers not responsible for the manner in which administrative affairs are conducted. By the same token, the task of executing and controlling the budget plan is made more arduous if administrative officials are independent of the governor. Mr. Buck, writing in 1929, said:

"However, as yet he (the governor) is little more than the nominal budget making authority in perhaps half of these states. This is due mainly to two things: in the first place, he does not have the proper staff assistance and the necessary information to formulate the budget; in the second place, he is not in a commanding position with respect to the administrative organization of the state government so that he can properly execute the budget when it has been adopted by the legislature."¹

In 1936, after a week's recess following the regular session, the Kentucky General Assembly was convened in extraordinary session to consider one subject only, the reorganization of the state government. The reorganization bill as passed provided for a systematic integration of administrative functions, so that

¹ *Public Budgeting*, 1929, p. 284.

like or similar functions would be performed in the same department.² Since 1936 other independent agencies have been created and added to the six designated by the reorganization act—the Board of Registration and Purgation, the County Debt Commission, the Soil Conservation Committee, and the Aeronautics Commission.³ The more the number of agencies independent of the Governor's supervision, the less integrated the system becomes. In 1944 the General Assembly again modified the administrative reorganization plan in such a way as to indicate a trend toward decentralization.

Twenty-seven other states have partially or nearly completely reorganized their state governments in the past quarter century for the declared purpose of obtaining "efficiency and economy."⁴ On the whole, the state governments which have reorganized their administrative structures have made possible more effective budgeting, especially from the standpoint of the execution of the budget.⁵ When the heads of the more important departments are placed on an equal footing with the governor as to the source of their authority, he has no power to manage administration, not even through the budget.

FINANCIAL ORGANIZATION FOR BUDGET EXECUTION

The financial machinery of any government, if it is to serve the purpose of budgetary administration and control, must be so constructed as to meet two requirements. In the first place, it must enable the executive to direct the fiscal affairs of the government; second, it must provide the means whereby the legislative body will have a check on the performances of the executive and the administration.

Many of the states have established budget bureaus or offices, which are, in most instances, headed by single officers appointed by and working under the direction of the governor, and which are connected with the executive office.⁶ This type of staff agency has the advantage of prestige gained as a result of being a direct representative of the governor, but in many cases

² See Chapter II for a description of the administrative structure as designed by the 1936 act.

³ KRS 66.300, 117.340, 183.020, 262.030.

⁴ The Council of State Governments, *The Book of the States*, 1941-42, p. 62.

⁵ Buck, *op. cit.*, p. 438.

⁶ *Loc. cit.*

these budget staffs fall short of performing all the functions necessary to give the governor adequate control, such as maintaining accounts through which budgetary control may be established.⁷ There is no reason why they could not be utilized to the maximum. Another popular type of staff agency makes use of departments of finance, which have powers covering important phases of fiscal management to a varying degree in the different states. The Kentucky Department of Finance holds a pre-eminent position in the state's organization, and few other states approach the degree of financial control in their finance departments as that achieved through the Kentucky scheme.⁸

The reorganization act of 1936 recognized the conception that budgeting is an administrative rather than a judicial or legislative function, and it set up machinery for administration of the budget plan by the executive, as well as for preparation and presentation of estimates to the General Assembly.⁹ The Department of Finance was organized to include a division to be responsible for the budgeting function as outlined in the 1934 Budget and Financial Administration Act, along with three other divisions—a Division of Accounts and Control, a Division of Purchases and Public Properties, and a Division of Personnel Efficiency.¹⁰ The fact that the Division of the Budget has not operated so as to take maximum advantage of the budget system¹¹ is not a defect in the organization scheme, but rather a failure on the part of both the governors and the legislatures to provide adequate personnel and to look upon the budget procedure as an important instrument of continuous financial planning.

One of the important contributions to sound budgeting made after 1936 was provision for adequate accounting facilities. The Public Administration Service was retained by the state to install records and to develop the best possible budgeting techniques.¹² The operation of the control system is described in the succeeding sections.

⁷ *Ibid.*, pp. 236, 297, 444.

⁸ James W. Martin, "Kentucky Weakens Centralized State Administration," *National Municipal Review*, May, 1944, pp. 253, 254.

⁹ See Chapter II.

¹⁰ *Acts 1936*, 1st spec. sess., chap. 1, art. 10, sec. 2; KRS 42.020, 42.040, 42.050, 42.060, 42.110.

¹¹ See Chapter IV.

¹² See Chapter II.

BUDGETARY CONTROL OVER EXPENDITURES

Control of the execution of the budget plan is a function of the Governor performed through machinery in the Division of Accounts and Control in the Department of Finance. The machinery consists essentially of a system of executive allotments, under which the spending agencies forecast the year's expenditures by periods and are required to observe these limitations as approved by the Department of Finance. In states in which this budgetary control is not exercised, but the departments of finance resort only to a pre-audit of claims and vouchers, the finances are likely to become maladjusted at the end of the fiscal year, because spending agencies often get over-ambitious in their spending at the beginning of the year and come up **without any** funds toward the last of the period. The Kentucky law stipulates:

"Except as deviations therefrom are made necessary by changes in conditions of operations, to meet unforeseen contingencies, to correct errors, or to avoid cash deficits, the heads of the budget units, the Department of Finance and the Governor, in allotting appropriations for expenditure, shall be governed by the work plans formulated by the heads of the budget units as shown in the detailed budget estimates as amended by the General Assembly, and shall make allotments semi-annually to permit the carrying out of such plans, and the heads of the budget units shall hold to the work plans and detailed expenditure estimates as authorized and approved on advices of allotments. In no case shall obligations be incurred or expenditures made in excess of the total amounts allotted. The decision of the Department of Finance as to the amount of any allotment for a specified period or as to the purposes for which money allotted may be expended shall be final and conclusive."¹²

The request for allotments

The budget calendar provides for the distribution of requests for allotments to the budget units by the Division of the Budget¹⁴ on May 1 of each year.¹⁵ Before the requests are distributed, the Division of the Budget inserts the name and amount of the appropriation against which the allotments are chargeable and the names of the respective departments, divi-

¹² Acts 1934, chap. 25, art. 3, sec. 17; KRS 45.160.

¹⁴ Since Kentucky has not established a division of the budget as a distinct entity (see Chapter IV), it is usually the Director of the Division of Accounts and Control who performs the duties connected with budget control.

¹⁵ Public Administration Service, *Handbook of Financial Administration*, Commonwealth of Kentucky, 1937, pp. 23, 37.

sions, and institutions on the forms. The provision of these data is necessary so that the department head may be informed by what units the Division of the Budget wishes to maintain control over expenditures. These forms are prepared in duplicate and the original copies must be returned to the Division of the Budget not later than May 31.¹⁶ As shown on the sample form on the following page, the estimated expenditures must be shown by budget class of expenditure and by quarterly periods.¹⁷ However, in practice allotments are made for only one quarter at a time. The space provided at the bottom of the form is for use by the Division of the Budget so that it can keep a summary record of allotments and the status of each allotment account.

Filling out the requests for allotment by the department heads usually amounts to a division of the total appropriation by four, since the spending agencies feel that all the money appropriated is theirs to spend.¹⁸ However, the appropriations made by the General Assembly designate the maximum amounts to be spent rather than the minimum and the Department of Finance has authority to cut appropriations in the case of unforeseen contingencies.¹⁹

Although the Department of Highways does not submit expenditure estimate forms and follow the regular budgetary procedure in the formulation stage,²⁰ it does comply with the regulations concerning the allotment procedure. The Highway Department prepares a work program, that is, the estimated number of miles of road construction contemplated, the amount of road repair and maintenance, etc., which is sent to the Division of the Budget with the request for an allotment; the budget division uses the work program and estimates of road fund receipts by the Commissioner of Revenue to make allotments to the Highway Department.²¹

¹⁶ Public Administration Service, *op. cit.*, p. 37.

¹⁷ Although the law refers to semi-annual allotments (*Acts 1934, chap. 25, art. 3, sec. 17; KRS 45.160*), the Department of Finance may require allotments based on shorter periods of time. (Conference with Mr. Warren Van Hoose, Assistant Budget Director, Kentucky Department of Finance, Sept. 6, 1944.)

¹⁸ Conference with Mr. Warren Van Hoose, Sept. 6, 1944.

¹⁹ *Acts 1934, chap. 25, art. 3, secs. 3 and 17; KRS 45.050 and 45.160.*

²⁰ See Chapter IV.

²¹ Conference with Mr. Frank D. Peterson, former Head of the Division of Accounts and Control, Kentucky Department of Finance, now Comptroller of the University of Kentucky, Oct. 13, 1944.

Advice of allotment

Requests for allotments are analyzed by the Division of the Budget, which determines allotments for the first quarter and tentatively decides upon allotments for the other three quarters. The spending agencies are informed of their quarterly allotments on the "Advice of Allotment" form on the twentieth of the month preceding the beginning of each quarter.²² The decisions of the budget office are final in determining allotments and in interpreting the meaning of items specified in any appropriation act.²³ However, the department heads often confer with the Director of the Budget on issues of controversy, and they may be able to convince him to allot according to their suggestions.

There have been occasions when the departmental administrators have made strong objections to the allotments made by the budget division. For example, when the second quarterly allotment was made to the Attorney General's office in 1938, it was reduced by approximately seven hundred dollars since there was an unspent balance of that amount left from the first quarter.²⁴ The Attorney General complained bitterly and filed a suit against the Department of Finance to get his allotment increased; but the Commissioner of Finance convinced him that if the need for additional money actually appeared, he could obtain it, and so the suit was dropped.²⁵

The Division of the Budget has sometimes made it a policy to reserve a percentage of the total appropriation from allotment in case the anticipated revenues are not fully realized. For the fiscal year 1936-37 a 10 per cent reserve was established; and, as a result when revenues were fully realized, several departments had at the beginning of the fourth quarter unspent balances in their total appropriations.²⁶ They tried to spend these balances by "stocking up," but the Commissioner of Finance prohibited these purchases. The result was that the budget for the year was underspent by about a million dollars, which amount was applied to payment of the state debt according to the Governor's established financial policy.²⁷

²² Public Administration Service, *loc. cit.*

²³ Acts 1934, chap. 25, art. 3, sec. 19; KRS 45.160.

²⁴ Conference with Mr. Frank D. Peterson, Oct. 18, 1944.

²⁵ *Loc. cit.*

²⁶ *Loc. cit.*

²⁷ *Loc. cit.*

Allotment transfers and supplements

Transfers from an allowance for one budget class (i.e., personal services; services other than personal; materials, supplies, and parts; replacements and other current expenses; capital outlay; and debt and interest) to an allowance for another budget class within the same budget unit may be authorized by the administrative head of the budget unit if approved by the Division of the Budget.²⁸ It is the policy of the Division of the Budget to sanction these transfer requests, except that the allotment for personal services is more rigidly scrutinized since considerable difficulty would result from lack of funds for salaries.²⁹

Supplementary allotments are left to the judgment of the Budget Director; however, in no case are total allotments made in excess of the appropriation.³⁰

Control over commitments

The task of the Division of the Budget does not end with fixing the allotments. Execution and control of the budget plan is a continuous process, and keeping expenditures within allotments by machinery set up in the Division of Accounts and Control is a function of the Division of the Budget to insure the execution of the budget plan as it was adopted by the General Assembly.

Budgetary control over incurring state expenditures is effected by routing all vouchers authorizing encumbrances to the Department of Finance, which determines whether or not the proposed expenditures are authorized by the appropriations and allotments against which it is proposed to charge them, and that the amounts involved do not exceed the unencumbered balances of such allotments.³¹ After approval as to propriety and the sufficiency of funds, the amounts are posted to the expenditure and encumbrance ledger, which is a subsidiary ledger maintained to reflect the status of each allotment account. This procedure is known as a pre-audit of proposed expenditures. There is still another pre-audit before cash is disbursed. After the goods are delivered and the invoices rendered, the invoices are checked

²⁸ Acts 1934, chap. 25, art. 3, sec. 18; KRS 45.130.

²⁹ Conference with Mr. Warren Van Hoose, Sept. 6, 1944.

³⁰ *Loc. cit.*

³¹ Acts 1934, chap. 25, art. 4; KRS 45.190.

with the purchase order and the receiving report against the goods delivered. It is only after this final check that the Department of Finance writes out a treasury warrant on which the checks are drawn.

Appropriation transfers and emergency funds

The allotment and pre-audit procedures are valuable adjuncts of budget control; but they are, generally speaking, techniques of a preventative character. The Governor has also been granted power to manage the state finances in a positive way, even after allotments have been made against appropriations. In the first place, the Governor's budget staff agency is authorized to make transfers between appropriations to the budget units within one state department.³² For example, a transfer of a part of the appropriation to the Division of Personnel Efficiency to the Division of the Budget could be made since both these budget units are in the same department. This authority permits some flexibility in the budget plan; it also could be used to pointed advantage if the legislature should make detailed appropriations.

A second tool of budget management, which is responsive to changing conditions, is provided by the Governor's general emergency fund. The General Assembly has followed a policy of appropriating a specified amount "for meeting ordinary recurring and extraordinary expenses deemed emergencies by the Governor of the Commonwealth and to be expended by the Governor to meet any emergency that may arise. . . ."³³ The general emergency fund has ranged in amount from \$200,000 to \$250,000;³⁴ and has been used for such large emergencies as meeting the expenses incurred because of the flood in the capital city in 1937.³⁵ The Governor has also used the emergency fund effectively in supplementing regular departmental appropriations when they have been found to be insufficient. For example, in one year when the office of the Clerk of the Court of Appeals had extra maintenance and operation expense because of a heavy docket and was about to incur an overdraft of \$1,100

³² *Acts* 1934, chap 25, art. III, sec. 18; KRS 45.130.

³³ This is the language of the appropriation acts.

³⁴ *Acts* 1938, chap. 1, sec. 4; *Acts* 1940, chap. 16, sec 4; *Acts* 1942, chap. 1, sec. 4; *Acts* 1944, 2nd spec. sess., chap. 1, sec. 4.

³⁵ Conference with Mr. Frank D. Peterson, Oct. 18, 1944.

the Governor by an executive order transferred this amount from his emergency fund to the account of the clerk of the Court of Appeals.³⁶ Any department head may appeal to the Governor for assistance and will get it if he convinces the Governor that he has just cause and that his request does not reflect wasteful or imprudent expenditure.

Both the provision for transferring appropriations and the grant of an emergency fund to the Governor allow adjustments in expenditures which were not contemplated when the budget was formulated. They make it possible for the Governor to execute the budget plan without undue rigidity and without having to call the legislature in special session to make additional emergency appropriations. The policy of the General Assembly of granting to the Governor unrestricted authority over the expenditure of the emergency fund also reflects the placing of full responsibility upon him for the successful management of the state's finances.

ACCOUNTING RECORDS

The accounting system maintained by the Division of Accounts and Control plays an important part in the preparation and the execution of the budget. It serves the budgetary process by: (1) providing information concerning expenditures and revenues of prior years, which is employed in building the budget for the new fiscal period. (2) keeping records which furnish information for current control over expenditures; and (3) making reports to the public, the Governor, the Commissioner of Finance, and the heads of the budget units to assure that appropriate action will be taken if actual revenues prove to be less than the estimates, or any irregularities or "tight" conditions exist in the funds available to any department.

The Division of Accounts and Control is required to maintain:

1. A set of budgetary control accounts for each fund which will show at all times the status of the fund.
2. A subsidiary appropriation ledger for each fund showing the appropriation to each budget unit, additions to the appropriations, allotments from the appropriation, the unallotted balance of the appropriation, commit-

³⁶ *Loc. cit.*

ments charged to allotments, and the free or unencumbered balance of allotments.

3. A set of general controlling proprietary and operating accounts for each fund so as to record transactions in summary form and show the actual current assets, pre-paid expenses, current liabilities, deferred credits to income, reserves, current liabilities, actual income, actual expenditures, and the current surplus or deficit.
4. A uniform classification of revenue and non-revenue receipts by sources, which is to be observed by all budget units in transmitting monies and reporting on revenue receipts.
5. A standard classification of expenditures by activities of the budget units.
6. A standard classification of budget units by major functions.
7. Such other accounts and records as the Commissioner of Finance may consider necessary to obtain needed information relative to financial condition, financial operations, and costs.
8. Controlling accounts for receipts, payments, and state depositories entirely independent of those maintained by the Treasury.³⁷

As documents evidencing financial transactions pass through the Division of Accounts and Control, they are subject to the review described above and are entered upon the appropriate records. The establishment of effective record-keeping in this Division makes it possible for the Governor to maintain control over the execution of the budget plan.

FISCAL REPORTING

The current information concerning the status and changes in all phases of the state's financial picture is employed by the Governor, the budget and finance officers, and departmental officials in the management of the commonwealth's activities. Under the provisions of the Budget and Financial Administration Act dealing with fiscal reporting, the Division of Accounts and Control is required:

1. To furnish each budget unit, within ten days after the close of each month, a statement of its appropriations and allotments showing all transactions recorded during the previous month and the balances as of the beginning and end of each month.
2. To furnish the Governor and the Commissioner of Fi-

³⁷ Acts 1934, chap. 25, art. 7, secs. 1 and 3; KRS 45.300.

nance, within ten days after the close of each month, a report containing:

- (a) a summary statement of the actual financial condition of each fund as of the close of the previous month;
 - (b) a summary statement of the receipts and payments of each fund for the previous month and for the current fiscal year to the close of the previous month;
 - (c) a summary budget statement for each fund showing the available cash balance as of the end of the previous month, the amount of cash estimated to be received from each source during the remaining months of the fiscal year, the total means of financing the amount of unallotted balances of appropriations, the estimated amount of unliquidated commitments, and the estimated cash surplus or deficit.
3. To file with the Governor, on or before the first day of October of each fiscal year, a complete report of the financial transactions of the preceding fiscal year and of the financial condition as of the end of that fiscal year, with such supplementary data and comments as may be necessary to make the report complete and easy to understand.³

REVISED ESTIMATES OF RECEIPTS

Important to budgetary administration is the analysis of revenue collections as compared with the estimates in the budget plan and the interpretation of such data from the viewpoint of the plan's execution. If the state's expenditure program is to be properly coordinated with revenue collections, it is necessary that the original receipts estimates be revised whenever the need for such revision is indicated by actual collections or by significant changes in the factors upon which the estimates were based. The revenue collection estimates are a decisive element in guiding the allotment process. Effective utilization of the revenue estimates requires sustained revision of the estimates and also requires making the appropriate entries to the general and subsidiary accounting records.

The Department of Finance asks for quarterly revisions of revenue estimates from the Department of Revenue when the revisions appear to be necessary; and it has been a general practice for the Revenue Department to submit revisions at the beginning of each fiscal year whether called for by the Finance Department or not.

³ Acts 1934, chap. 25, art. 7, sec. 2; KRS 45.320.

CHAPTER VIII

KENTUCKY BUDGETING, 1918-1944: RESUMÉ

Although Kentucky endorsed the budget idea as early as 1918, it was not until after 1936 that the state installed a budget system which would aid financial administration in any substantial degree.

A thoroughgoing budget procedure demands that a comprehensive financial plan, encompassing all anticipated activities of the state for the future fiscal period, be carefully formulated and executed. Budgeting practices in Kentucky from 1918 to 1934 failed to conform to this criterion for several reasons. (1) The revenues of the state were largely restricted by law for specific expenditure. Because of the earmarking of taxes and other receipts, the budget authorities and the legislators could plan, or budget, only a small portion of the state's financial transactions. (2) No public official during this period was pointedly responsible for either preparing or administering a budget plan. A Budget Commission of three administrators was charged with the task of submitting a budget to the General Assembly for its consideration, but preparation of a budget was secondary to other official duties for which each member of the Commission was primarily responsible. Moreover, the framers of the budget laws did not envision the scope of the work involved in formulating a real budget plan, for they failed to provide the Commission with adequate staff assistance. (3) The state's financial structure was disintegrated; and no office had specific authority or the means to coordinate and control the finances according to a pre-designed plan, even if a comprehensive budget had been prepared. (4) Finally, the accounting records did not produce adequate financial information necessary as a basis on which to build a budget plan and essential for current budget control.

The 1934 General Assembly paved the way for establishing a serviceable budget system by abandoning to a large extent the old scheme of blanket authorization to spend money, and thus

making it possible for the budget system to comprehend a greater portion of the state's financial transactions; by adopting the executive budget philosophy, which made the Governor the responsible general manager of financial policy; and by installing budgetary control procedure. However, because the Governor was not in a controlling position with respect to state governmental machinery and because the financial organization did not provide him with adequate technical assistance, the budget system "limped" between 1934 and 1936. The Governmental Reorganization Act of 1936 integrated the major functions of government into departments under the Governor's supervision and management and coordinated the staff services of administration into a single Department of Finance, which provided the Governor the technical assistance necessary to prepare, present, and administer his budget.

Budgeting in Kentucky practice now means planning programs for welfare activities, for conservation, for education, and for all other functions which the budget system covers; ascertaining the cost of these programs; submitting to the legislature a proposed plan of financing the work; authorization of the plan by the legislature; and carrying out the plan thus made and approved. The state also provides for checking the execution of the plan after it has been consummated.

Aside from the outstanding fact that the Division of the Budget in the Department of Finance has not been elevated to a position in which it can effectively and continuously study the needs of the spending agencies and contribute maximum service to the Governor in planning expenditures, the *authorized* budgetary resources have been exploited with considerable success since 1936. The word "authorized" is emphasized because the General Assembly has not designed a completely comprehensive budget system. The statutes permit approximately three-fifths of all expenditures to be made by virtue of the fund which finances them, rather than by virtue of appropriations based on a budget. The chief examples of these extra-budgetary funds are the state road and the revolving, trust, and agency group. To the extent that receipts are earmarked by law for specific expenditure, the effectiveness of the budget plan is decreased.

Beginning with the 1938 legislative session and continuing through each successive biennial session, the Governor has placed before the General Assembly a reasonably clear-cut fiscal plan. By developing the extra-legal procedure of inviting the Legislative Council to attend budget hearings and give advice with respect to estimates and policies which ought to be reflected in the executive budget, the Governors up to, but not including, 1944 have been singularly successful in getting their financial programs adopted in the General Assembly, and have thereby improved budgeting practice. The commonwealth also has much cause for gratification regarding the control of finances exercised after legislative appropriations have been made. This control is made possible by authorizing the Governor through the Department of Finance to confine the expenditures of individual agencies to quarterly allotments based on approved work programs and by an effective pre-audit of commitments to insure legality and the sufficiency of allotments before cash is disbursed by the Treasurer. Another technique which the Governors have employed in connection with executing the budget plan is made possible by the appropriation of a fairly substantial amount to an emergency fund, which the Governor may spend to meet exceptional demands. The 1936 act also separated the comptroller functions from the Office of the Auditor of Public Accounts and provided for an effective post-audit of administrative activities. A post-audit is an indispensable counterpart of successful budgeting since it affords a means of checking the stewardship and efficiency of the administrators who were charged with the execution of the financial plan adopted by the legislature.

Whatever has been achieved in budget administration since 1936 has been facilitated by the fact that since that date the state has had a real accounting system. The beginnings of the system date to 1934, when provisions for its establishment were enacted. These provisions became a reality after the Governor in 1936 had modern accounting techniques installed.