

The Structure and Political Economy of the U.S. Federal Budget

A basic explanatory guide to national power, congressional budget procedure, revenues and outlays, deficits, Treasury debt, financial markets, and the welfare-state debate

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This document explains the U.S. federal budget not merely as a spending plan, but as a vast fiscal system in which the executive branch and Congress, taxation and welfare, defense and financial markets, public debt, and electoral politics are deeply connected.

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Summary

The U.S. federal budget is not simply an accounting ledger for government spending. It is a mechanism for allocating power: deciding which functions the state will prioritize and who will bear the cost. The President presents the executive branch’s policy priorities through the budget proposal, but actual spending authority belongs to Congress. Congress determines the fiscal direction of the federal government through budget resolutions, appropriations bills, tax legislation, reconciliation, and debt-ceiling negotiations.

The core of the federal budget can be understood in three categories. First, mandatory spending flows automatically under statutory eligibility rules, as with Social Security, Medicare, and Medicaid. Second, discretionary spending is determined each year through congressional appropriations and includes defense, education, diplomacy, transportation, and agency operations. Third, interest on the debt is the financial cost created by past accumulated deficits and current interest rates.

In fiscal year 2025, the federal government collected about \$5.2 trillion and spent about \$7.0 trillion, producing a deficit of about \$1.8 trillion. Over the long run, aging, health-care costs, interest on Treasury debt, inadequate revenues, and political competition over tax cuts are the central sources of fiscal pressure.

1. Basic Structure of the U.S. Federal Budget

The federal budget moves through three broad stages. First, the President and the Office of Management and Budget prepare the executive budget proposal. Second, Congress debates budget resolutions and aggregate fiscal targets. Third, appropriations and tax-writing committees turn spending and revenue decisions into law. Throughout this process, the Congressional Budget Office provides nonpartisan cost estimates and fiscal projections to Congress.

Stage	Core Question	Lead Institutions	Political Meaning
Presidential budget proposal	What does the executive branch want?	President, OMB	Policy priorities and the opening position for negotiation
Congressional budget process	How does Congress set aggregate totals and priorities?	House/Senate Budget Committees, CBO	Political adjustment of deficits, revenues, and spending limits
Spending and revenue legislation	How are actual money and tax law changed?	Appropriations, Ways and Means, Senate Finance	Determination of winners and losers by program

The Presidential Budget and OMB

The President’s budget is not law. It is a policy statement and the starting point for budget negotiations with Congress. OMB coordinates agency requests and integrates revenue, spending, regulatory, and management strategies with the President’s policy goals. OMB is therefore not merely an accounting office; it is the fiscal execution arm of presidential power.

The Role of CBO

CBO functions as Congress’s numerical referee. Separate from OMB’s executive-branch projections, CBO provides cost estimates for legislation, baseline projections, and long-term fiscal outlooks. CBO does not recommend policy. It supplies nonpartisan analysis so Congress can judge tax and spending legislation on a common analytical basis.

2. Powers of the Key Congressional Committees

To understand the federal budget, one must understand the committee structure. Budget power in Congress is not concentrated in a single body. It is distributed among several committees, and this distribution is what makes American budget politics complex and negotiation-driven.

Institution / Committee	Core Authority	Meaning in Budget Politics
House Budget Committee	Drafts the budget resolution; sets aggregate spending, revenue, and deficit targets; may include reconciliation instructions	Architect of aggregate budget politics in the House

Institution / Committee	Core Authority	Meaning in Budget Politics
Senate Budget Committee	Manages the Senate budget resolution and reconciliation process	Gateway to simple-majority budget legislation in the Senate
Appropriations Committees	Allocate funding to federal agencies through the 12 regular appropriations bills	Practical distributors of agency operating funds and defense/nondefense discretionary spending
House Ways and Means Committee	Handles individual income taxes, corporate taxes, tariffs, and Social Security-related revenue legislation	Center of tax power in the House
Senate Finance Committee	Has jurisdiction over taxes, tariffs, Medicare, Medicaid, Social Security, and related matters	Core Senate committee for taxation and welfare-state finance

3. Spending Structure: Mandatory, Discretionary, and Interest

Mandatory Spending

Mandatory spending is outlay that flows automatically according to eligibility rules and benefit formulas established in existing law. Major examples include Social Security, Medicare, Medicaid, CHIP, SNAP, federal employee retirement benefits, and some veterans’ benefits. Congress does not set a new amount for these programs each year; spending changes according to the number of eligible beneficiaries and statutory payment formulas.

This area is politically the hardest to cut. Social Security and Medicare are directly linked to the income security and health care of older voters, while Medicaid connects state governments, hospitals, insurers, and low-income health systems. Therefore, the mandatory-spending debate is not merely about budget cuts. It is a debate over the size of the American welfare state and the intergenerational contract.

Discretionary Spending

Discretionary spending is determined each year through appropriations bills. It includes defense, homeland security, diplomacy, education, transportation, housing, the Department of Justice, the National Institutes of Health, NASA, and the operating budgets of most federal agencies. Politically, this category often produces the loudest annual fights, but it is smaller than mandatory spending as a share of the total federal budget.

Interest on the Debt

Interest on the debt is not a policy program. It is the financial cost created by accumulated past deficits and current interest rates. It is difficult to cut because it reflects payment obligations on Treasury securities that the federal government has already issued. The larger the debt and the higher the interest rate, the more interest costs crowd out fiscal space for welfare, defense, education, and other programs.

Category	Character	Representative Items	Political Meaning
Mandatory spending	Automatic spending under law	Social Security, Medicare, Medicaid, SNAP	Welfare state, aging, and health-care-cost debate
Discretionary spending	Allocated annually through appropriations laws	Defense, education, transportation, diplomacy, agency operations	Partisan negotiation and shutdown risk
Net interest	Financial cost of debt	Interest on Treasury debt	Interest rates, Treasury market, and long-term fiscal sustainability

4. Revenue Structure

The federal government’s revenue base is centered on individual income taxes and payroll taxes. Corporate taxes, customs duties, excise taxes, and other receipts exist, but they are not large enough to replace individual income taxes and social insurance receipts. This point reveals the essence of American tax politics: the federal government is funded primarily by personal income, labor income, and payroll taxation.

Revenue Source	Approximate FY2025 Amount	Approximate Share	Political-Economic Meaning
Individual income taxes	About \$2.656 trillion	About 51%	Largest federal revenue source

Revenue Source	Approximate FY2025 Amount	Approximate Share	Political-Economic Meaning
Payroll taxes / social insurance receipts	About \$1.748 trillion	About 33%	Core funding source for Social Security and Medicare
Corporate income taxes	About \$452.1 billion	About 9%	Sensitive to corporate profits, tax rates, and depreciation rules
Customs duties	About \$194.9 billion	About 4%	Tool of trade policy and industrial policy
Excise, estate and gift taxes, and other receipts	Relatively small	Minor share	Fuel taxes, alcohol and tobacco taxes, fees, and miscellaneous receipts

For that reason, proposals to replace the individual income tax or payroll tax with tariffs alone are highly unrealistic under the current scale of federal finance. Tariffs may be important as a political message and an industrial-policy tool, but they are not the main revenue source for the overall federal government.

5. Major Spending Areas

The federal budget covers the full range of government functions. Structurally, however, the largest areas are Social Security, Medicare, Medicaid, defense, and interest on the debt. Education, transportation, diplomacy, agriculture, and veterans' programs are politically important, but they are generally smaller than the largest entitlement, defense, and interest categories.

Area	Budget Character	Core Content
Social Security	Mostly mandatory	Old-age, survivors, and disability insurance; aging and trust-fund finances are central issues
Medicare	Mandatory	Health insurance for older Americans; tied to health-cost growth and hospital, pharmaceutical, and insurance interests
Medicaid	Mandatory; federal-state joint program	Health coverage for low-income people; connected to state finances, hospital systems, and welfare policy
Defense	Mostly discretionary	Department of Defense, weapons systems, personnel costs, overseas operations, and defense-industry contracts
Interest on the debt	Mandatory financial cost	Result of accumulated debt and interest rates; a central source of long-term fiscal pressure
Education	Mostly discretionary plus some mandatory components	Grants, student aid, support for low-income students, research, and training programs
Transportation	Discretionary plus trust-fund finance	Highways, aviation, rail, public transit, and infrastructure investment
Veterans affairs	Mandatory plus discretionary	Veterans' health care, compensation, education, and housing support
Agriculture	Mandatory plus discretionary	Farm subsidies, crop insurance, food assistance, and rural development
Diplomacy	Mostly discretionary	State Department, foreign assistance, international organizations, and diplomatic missions

6. Core Budget Concepts

Budget resolution: An internal congressional budget blueprint. It is not a law, but it sets aggregate targets for spending, revenues, deficits, and debt, and may include reconciliation instructions.

Appropriations bills: Spending bills that give federal agencies actual budget authority. They are usually divided into 12 regular appropriations bills.

Continuing resolution: A temporary spending law that keeps the government operating when regular appropriations bills have not been enacted before the start of the fiscal year.

Omnibus bill: A legislative vehicle that combines multiple appropriations bills or policy provisions into one large bill.

Reconciliation: A procedure for moving budget-related legislation on revenues, direct spending, and the debt limit more quickly. In the Senate, it can bypass the filibuster and allow passage by a simple majority.

Debt ceiling: Not a device that authorizes new spending, but a limit that allows the Treasury to borrow to meet obligations already created by enacted spending and tax laws.

Government shutdown: A condition in which some federal agencies lose budget authority because no appropriations law or continuing resolution is in place.

Sequestration: An automatic spending-cut mechanism triggered when statutory limits or PAYGO rules are violated.

Deficit: The amount by which spending exceeds revenue in a single year.

National debt: The accumulated result of past deficits.

Trust fund: An accounting structure that links certain revenues and outlays, as in Social Security and Medicare.

Baseline budgeting: A projection of future revenues, spending, deficits, and debt under the assumption that current law continues.

7. How the Budget Connects to Political Economy

Partisan Conflict and Electoral Strategy

The budget is a central language of electoral politics. Tax cuts, welfare expansion, defense increases, fiscal responsibility, and debt reduction are all political promises offered to voters. The difficulty is that most political promises carry costs. If tax cuts and spending increases are pursued at the same time, deficits rise. If deficits are to be reduced, taxes must rise, spending must fall, or both.

Interest Groups and Lobbying

The federal budget is one of Washington's largest arenas of lobbying. Defense contracts, hospital and pharmaceutical reimbursement systems, farm subsidies, university research funding, transportation infrastructure, energy tax credits, and regional development grants all attract organized pressure from interested groups. A small phrase in the tax code can create billions of dollars in value for a specific industry.

Financial Markets, Inflation, and Interest Rates

Larger fiscal deficits increase Treasury issuance, which can affect interest rates, confidence in the dollar, Treasury-market liquidity, and inflation expectations. In a high-rate environment, past debt becomes a present budgetary constraint. As interest costs grow, the government has less policy space for the same level of revenue.

The Welfare-State Debate

Social Security, Medicare, and Medicaid are the core of the American welfare state. Beneficiaries often view these programs as earned rights, while the programs face fiscal pressure from aging and rising health-care costs. The American welfare-state debate is therefore not simply a debate between big government and small government. It combines intergenerational burden-sharing, the structure of the health-care industry, tax fairness, labor markets, and family structure.

8. How to Read and Analyze the U.S. Federal Budget

No single document is enough to analyze the federal budget. One must read the executive branch's intentions, Congress's cost estimates, actual cash flows, and audit or performance evaluations together.

Source	What to Look For	How to Use It
White House Budget	The President's policy priorities and agency budget requests	Read what model of government the executive branch is proposing
OMB Historical Tables	Long-run trends in revenues, outlays, deficits, and debt	Compare whether current figures are historically large or small

Source	What to Look For	How to Use It
CBO Budget and Economic Outlook	Ten-year fiscal outlook under current law	Identify the baseline for policy debates and long-term risks
Treasury Monthly Statement	Monthly receipts, outlays, and deficits	Track cash-flow patterns close to actual budget execution
GAO Reports	Audits, government operations, program performance, and long-term fiscal risks	Analyze whether money is being spent effectively and where institutional risks lie

9. Step-by-Step Learning Guide

Step 1: Start with the big numbers

First identify total revenues, total outlays, the deficit, total debt, and their ratios to GDP. Fiscal numbers become clearer when viewed relative to the size of the economy rather than only in absolute dollars.

Step 2: Divide spending into three categories

Distinguish mandatory spending, discretionary spending, and net interest. Many misunderstandings about U.S. budget politics arise because these categories are confused.

Step 3: Identify the main revenue sources

Understand that individual income taxes and payroll taxes are the core of federal revenue. Corporate taxes and tariffs matter, but they are not the primary fiscal base of the federal government.

Step 4: Learn the committee structure

Understand the differences among the Budget Committees, Appropriations Committees, House Ways and Means Committee, and Senate Finance Committee.

Step 5: Separate the baseline from policy changes

Current-law projections are different from the effects of new legislation. The CBO baseline is the starting point for most budget debates.

Step 6: Read the budget as political economy

Look beyond the numbers and identify where generational, class, regional, industrial, financial-market, and electoral interests are located.

Conclusion

The U.S. federal budget is not merely a ledger of money. It is a blueprint for the American state model. It decides who pays taxes, who receives benefits, what the country will address through military power, what forms of social protection it will promise, and whether the cost will be borne by the current generation through taxes or shifted to future generations through debt.

Reading the federal budget therefore means reading power, institutions, interests, markets, and intergenerational contracts together. Beginners should first learn to distinguish mandatory spending, discretionary spending, interest, deficits, debt, baselines, appropriations, reconciliation, and the debt ceiling. Once those concepts are connected to official data sources, the structure of American budget politics begins to become visible.

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