Deviations from the long-run equilibrium regression line have typically been within ±¼ percent of GDP, and this continues to hold in recent years.

5. ***In any case, the error-correction model indicates that true surprises are reversed quickly***. The coefficient on the error-correction term in the short-run equation is negative one or slightly larger, implying that deviations from long-run equilibrium are soon erased and that tax revenue is mostly driven by contemporaneous variables. Indeed, for overall revenue and individual income taxes, errors in one direction have tended to be followed by errors in the opposite direction.

Conclusions and Policy Implications

6. ***Our results suggest some caution in projecting that recent revenue buoyancy will persist***. Not only are deviations quickly reversed, but many of the explanatory variables are volatile over the business cycle. Corporate profits, capital gains, and the income share of the wealthiest may not remain at today's elevated levels, and if these factors revert to historical levels, our out-of-sample forecasts show that revenue could be substantially affected (Figure 2).

Figure 1. Contribution to Revenue Increase, 2004–2006

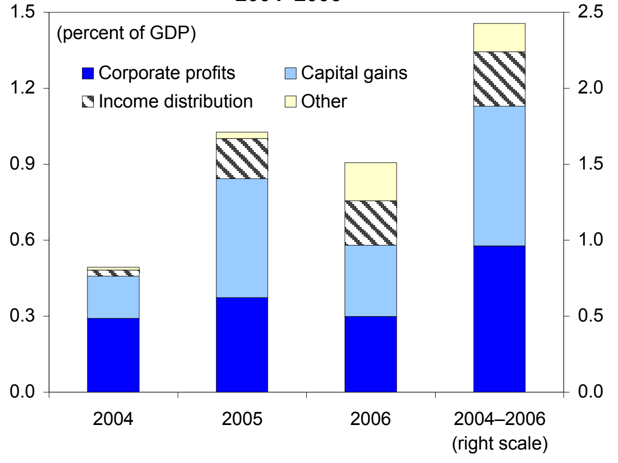
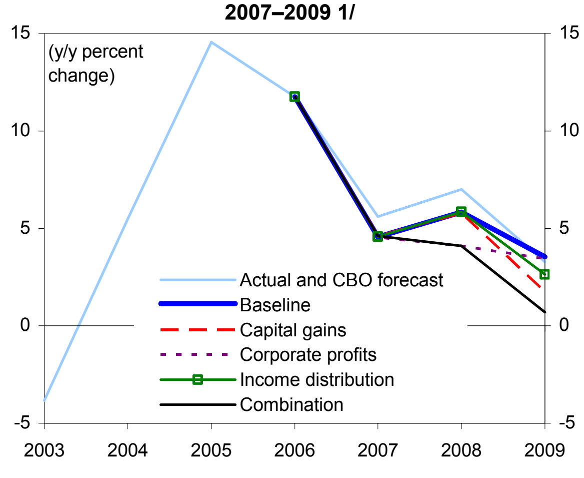


Figure 2. Out-of-Sample Revenue Forecast, 2007–2009 1/



1/ Each of the capital gains, corporate profits, and income distribution scenarios assumes a one standard deviation shock to that variable in 2008. The combination scenario assumes a one standard deviation shock to all three variables.

VII. Summary of Applying the *GFSM 2001* Framework to U.S. Fiscal Data

Information Note
by Isabel Rial and Cornelis Gorter

1. ***The Note reports on a study to present the U.S. fiscal data in a manner consistent with the Government Finance Statistics Manual (GFSM 2001)***. At an Executive Board seminar in 2005, Directors agreed that the use of the *GFSM 2001* framework would lead to greater transparency and consistency in the presentation of country fiscal data in staff reports. The Note summarizes how the *GFSM 2001* operating statement, integrated balance sheet, and cash statement could be integrated into staff monitoring of the U.S. fiscal sector.

2. ***The study incorporates cash and accrual data, as well as flows and stocks in a consistent framework, thus enhancing the accuracy and transparency of fiscal data***. The sources used are the *Budget of the United States Government*—mainly on a cash basis—as well as the *Financial Report of the United States Government*, the *National Income Product Accounts (NIPAs)*, and *the Flow of Funds Accounts (FFAs)*—all on an accrual basis.

3. ***The pilot demonstrates that presentation of fiscal data in accordance with GFSM 2001 recommendations is feasible for the U.S. in the short-term***. However, the numerical results of the pilot study should still be considered illustrative due to some unresolved data issues.

4. ***The U.S. pilot study draws attention to:***

From an analytical point of view,

- the less favorable fiscal position of the federal government if, in accordance with international recommendations, the obligations of unfunded government employee pension funds are recognized;
- the deterioration of federal net worth over the four-year period under analysis.

From a statistical point of view,

- the existence of data gaps for measuring of federal government net worth, as well as a full integration of stock and flow data; and
- the need to reconcile cash-based and accrual-based fiscal data in order to foster fiscal transparency.

5. ***The fiscal outturn of the federal government as measured under GFSM 2001 is less favorable than that derived from accrual-based NIPAs***. The discrepancies relate mainly to the treatment of employee pension funds covering federal employees and military personnel. Following the *GFSM 2001* methodology, the costs of the unfunded part of pension promises made to staff should be recognized. In 2006, these adjustments increase the deficit by

0.8 percent of GDP on an accrual basis and increase the federal government's debt by 10 percent of GDP.

6. ***Unlike the government employee pension funds, social security schemes do not give rise to liabilities in the GFSM 2001 framework***. Nevertheless, for long-term fiscal policy and fiscal sustainability analysis the *GFSM 2001* recommends including these obligations as a memorandum item to the balance sheet. For the federal government, this memorandum item represented 320 percent of GDP in 2006.

7. ***Federal government net worth deteriorated by 14.1 percent of GDP over the four-year period under analysis, although at a diminishing rate***. While the deterioration has been significant, as shown by the net operating budget (NOB) in Table 1, the authorities achieved equilibrium in the primary net operating balance in 2006. This indicates an improvement in the sustainability of government operations. As the net acquisition of nonfinancial assets was maintained at low levels, the net lending/borrowing (NLB) closely mirrors the evolution of the NOB in terms of magnitude and trend. The net borrowing requirement was financed by an increase in liabilities, primarily securities.

8. ***The Statement of Operations (Table 1) indicates a high degree of vertical integration—that is, consistency between data on operating transactions and financing***. Statistical discrepancies may arise between the NLB and its financing (net acquisition of financial assets minus net incurrence of liabilities) due to data deficiencies. The authorities periodically reconcile both datasets and, in the case of the federal government, the statistical discrepancy accounts for only 0.2 percent of GDP, on average.

9. ***However, the Integrated Balance Sheet (Table 2) shows horizontal integration to be less robust on account of specific data gaps***. These gaps are particularly apparent in the lack of data on nonproduced assets, while the valuation of the stock of assets and liabilities precludes a complete explanation of differences between opening and closing balance sheet. Despite existing data gaps, Table 2 provides an important insight into the composition of government liabilities. In this regard *GFSM 2001*, by presenting stock and flow data in an integrated framework, fosters data consistency and analysis of changes in net worth.

10. ***The Statement of Sources and Uses of Cash (reported in the Information Notice) suggests a greater margin of comfort in cash-based fiscal operations than the comparable accrual aggregate.*** The accrual balancing item, the NLB, is higher than the cash deficit in every year under analysis, the difference being (i) expense items that do not have a cash equivalent, and (ii) timing differences in the recording of revenue and expense.

Table 1. United States: Statement of Federal Government Operations

		2003	2004	2005	2006 Preliminar
	(Calendar year, in billions of dollars)				
Transactions affecting net worth:					
1	**Revenue**	**1,909**	**2,037**	**2,289**	**2,527**
11	**Taxes**	**1,093**	**1,175**	**1,391**	**1,562**
111	Taxes on income, profits and capital gains	981	1,056	1,265	1,449
114	Taxes on goods and services	68	71	76	74
115	Taxes on international trade and transactions	21	23	25	27
116	Other taxes	0	0	0	0
12	**Social contributions**	**759**	**802**	**855**	**920**
13	**Grants**	**0**	**0**	**0**	**0**
14	**Other revenue**	**57**	**60**	**43**	**45**
2	**Expense**	**2,391**	**2,526**	**2,703**	**2,825**
21	Compensation of employees	374	395	412	428
22	Use of goods and services	333	374	401	339
23	Consumption of fixed capital	28	29	31	104
24	Interest	212	220	253	280
25	Subsidies	48	44	57	52
26	Grants	410	422	446	451
27	Social benefits	967	1,018	1,082	1,171
28	Other expense	21	22	22	0
GOB	***Gross operating balance 1/***	***-454***	***-460***	***-383***	***-194***
NOB	***Net operating balance***	***-482***	***-489***	***-414***	***-298***
Transactions in nonfinancial assets					
31	**Net acquisition of nonfinancial assets 2/**	**10**	**11**	**12**	**1**
311	Fixed assets	10	11	12	14
312	Change in inventories	1	0	0	0
313	Valuables	0	0	0	0
314	Nonproduced assets	0	0	-1	-13
NLB	***Net lending/borrowing 3/***	***-493***	***-500***	***-426***	***-299***
Transactions in financial assets and liabilities (financing):		**-510**	**-456**	**-381**	**-262**
32	**Net acquisition of financial assets**	**34**	**-3**	**15**	**6**
3202	Currency and deposits	-17	-35	-1	-2
3203	Securities other than shares	0	0	0	0
3204	Loans	-3	3	-3	5
3205	Shares and other equity	1	2	1	0
3206	Insurance technical reserves	0	0	0	0
3207	Financial derivatives	0	0	0	0
3208	Other accounts receivable	53	26	22	3
323	Monetary gold and SDRs	-1	0	-5	0
33	**Net incurrence of liabilities**	**544**	**453**	**396**	**267**
3302	Currency and deposits	1	1	1	1
3303	Securities other than shares	396	362	307	183
3304	Loans	0	0	0	0
3305	Shares and other equity	0	0	0	0
3306	Insurance technical reserves	77	75	71	75
3307	Financial derivatives	0	0	0	0
3308	Other accounts payable	70	16	18	9
Discrepancy Net lending/borrowing and financing		***-17***	***44***	***45***	***38***
	(Calendar year, in percent of GDP)				
1	Revenue	17.7	17.7	18.7	19.3
2	Expense	22.1	21.9	22.0	21.6
NOB	***Net operating balance 1/***	***-4.5***	***-4.2***	***-3.4***	***-2.3***
	Primary net operating balance 1/	***-2.5***	***-2.3***	***-1.3***	***-0.1***
31	Net acquisition of nonfinancial assets 2/	0.1	0.1	0.1	0.0
NLB	***Net lending/borrowing 3/***	***-4.6***	***-4.3***	***-3.5***	***-2.3***
32	Net acquisition of financial assets	0.3	0.0	0.1	0.0
33	Net incurrence of liabilities	5.0	3.9	3.2	2.0
Memorandum items:					
GDP at market prices (billions of dollars)		10,809	11,518	12,266	13,061

Sources: BEA data submission, and STA staff estimates.

1/ The net operating balance equals revenue minus expense, when expense includes the consumption of fixed capital.
The gross operating balance equals revenue minus expense other than consumption of fixed capital.
2/ Acquisitions minus disposals and consumption of fixed capital.
3/ Net lending/borrowing equals the net operating balance minus the net acquisition of nonfinancial assets.
It is also equal to the net acquisition of financial assets minus the net incurrence of liabilities.