

United States Government Accountability Office

Saving  
Our Future  
requires  
Tough Choices Today

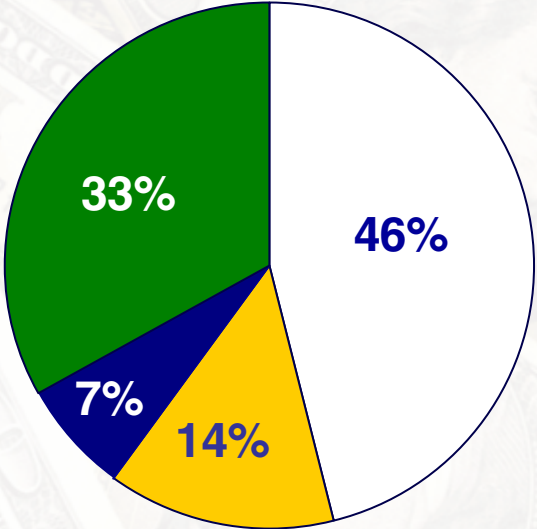
Richmond Town Hall Forum

September 26, 2005

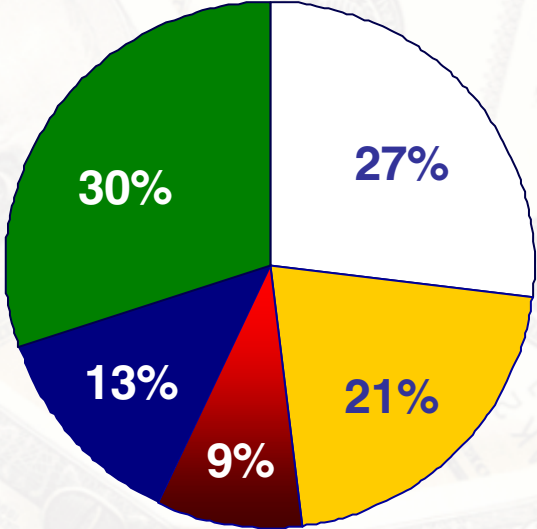


# Composition of Federal Spending

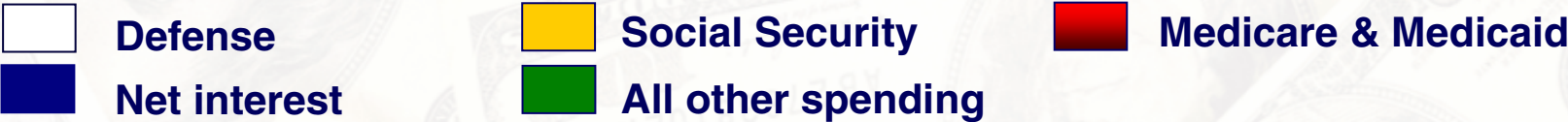
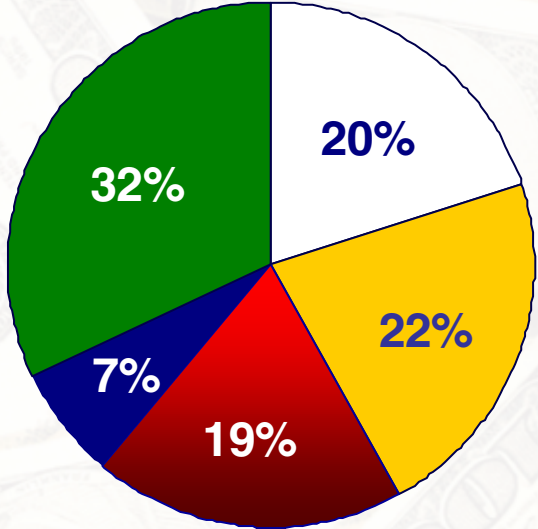
1964



1984



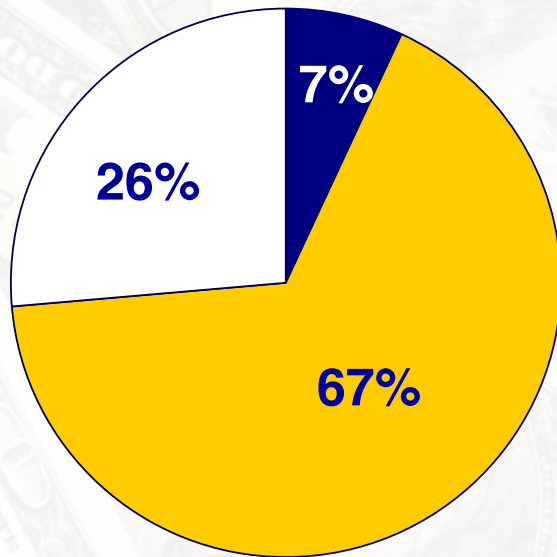
2004



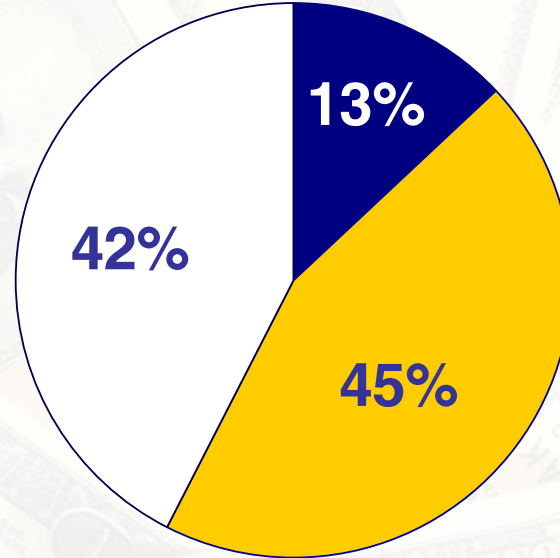
Source: Office of Management and Budget.

# Federal Spending for Mandatory and Discretionary Programs

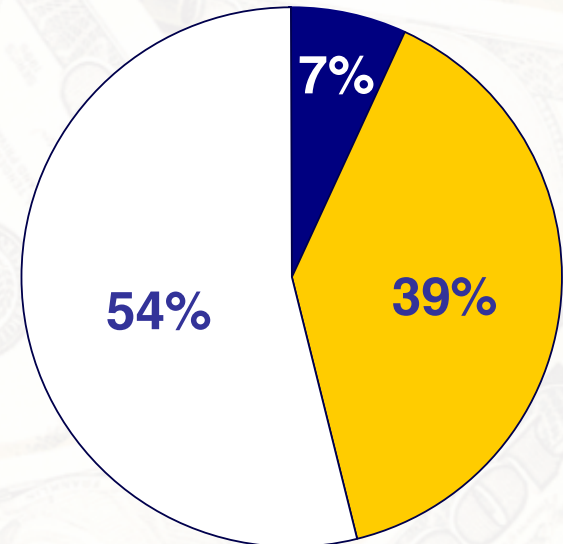
1964



1984



2004



Net Interest

Discretionary

Mandatory

Source: Office of Management and Budget.

# Fiscal Year 2004 Deficit Numbers

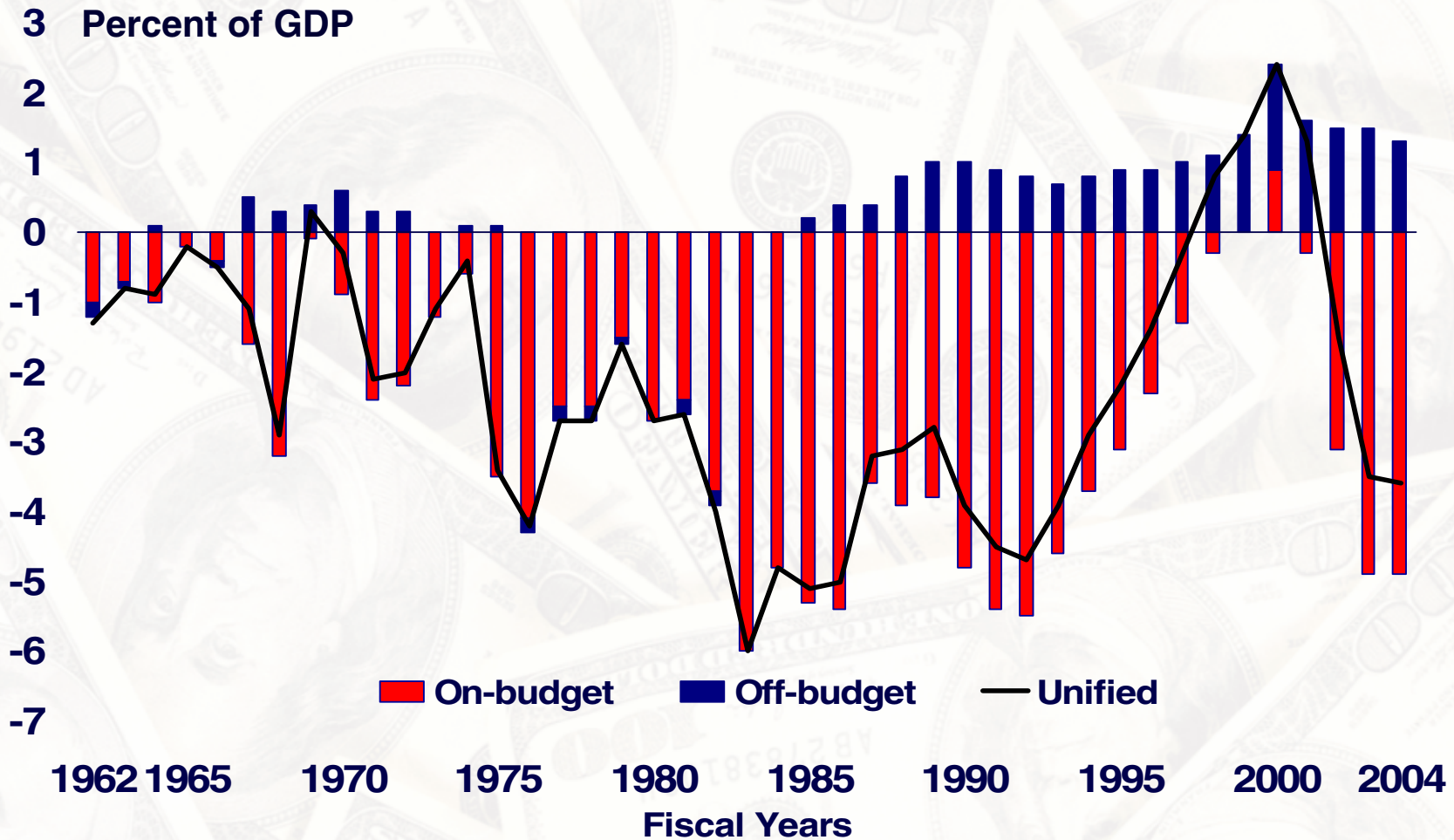
	\$ Billion	% of GDP
On-Budget Deficit	(567)	(4.9)
Off-Budget Surplus	155*	1.3
Unified Deficit	(412)	(3.6)

\*Includes the \$151 billion Social Security surplus and a \$4 billion surplus for the Postal Service  
March 2005



# Surplus or Deficit as a Share of GDP

Fiscal Years 1962-2004



Source: Office of Management and Budget and Congressional Budget Office.

# The Importance of Looking Beyond the 1<sup>st</sup> Year

- **Terrorism Risk Insurance expansion to aircraft and aircraft engine manufacturers enacted in 2003**
  - Estimate for FY 2004: \$3 million income
  - Estimate for 10 years (2004-2013): \$47 million cost
- **Health Care Benefit extension to older uniformed services retirees enacted in 2000**
  - Estimate for FY 2001: \$223 million cost
  - Estimate for 10 years (2001-2010): \$40.4 billion cost
  - Financial statement liability: \$293 billion
- **Medicare Drug Benefit enacted 2003**
  - Estimate for CY 2006: \$64.4 billion
  - Estimate for 2006-14: \$851 billion
  - Estimate from program inception through 2079: \$8.7 trillion in present value terms

Sources: Medicare estimates for net federal spending are drawn from the 2005 Medicare Trustees' intermediate estimates. All others are CBO cost estimates in year of enactment and 2001 Consolidated Financial Statement.

# Estimated Fiscal Exposures

(in \$ trillions)

	2000	2002	2004
<b>• Explicit liabilities</b>	<b>\$6.9</b>	<b>\$7.8</b>	<b>\$9.1</b>
<ul style="list-style-type: none"> <li>• Publicly held debt</li> <li>• Military &amp; civilian pensions &amp; retiree health</li> <li>• Other</li> </ul>			
<b>• Commitments &amp; Contingencies</b>	<b>0.5</b>	<b>0.8</b>	<b>0.9</b>
<ul style="list-style-type: none"> <li>• E.g., PBGC, undelivered orders</li> </ul>			
<b>• Implicit exposures</b>	<b>13.0</b>	<b>17.8</b>	<b>33.3</b>
<ul style="list-style-type: none"> <li>• Future Social Security benefits</li> </ul>	3.8	4.6	5.2
<ul style="list-style-type: none"> <li>• Future Medicare Part A benefits</li> </ul>	2.7	5.1	8.5
<ul style="list-style-type: none"> <li>• Medicare Part B benefits</li> </ul>	6.5	8.1	11.4
<ul style="list-style-type: none"> <li>• Medicare Part D benefits</li> </ul>	--	--	8.1
<b>Total</b>	<b>\$20.4</b>	<b>\$26.4</b>	<b>\$43.3</b>

Sources: Consolidated Financial Statements.

Note: Estimates for Social Security and Medicare are PV as of January 1 of each year as reported in the Consolidated Financial Statements and all other data are as of September 30. The 2005 Trustees Reports issued in March of this year show that the Social Security and Medicare exposures have increased as follows: Social Security increased to \$5.7 trillion, Medicare Part A increased to \$8.8 trillion, Medicare Part B increased to \$12.4 trillion and Part D increased to \$8.7 trillion. Totals may not add due to rounding.



# Growing Fiscal Burden

**Another way to think about these fiscal exposures is:**

	2000	2002	2004
<b>Fiscal exposures [from previous page]</b>	<b>\$20.4</b>	<b>\$26.4</b>	<b>\$43.3</b>
<b>Per person</b>	<b>72,000</b>	<b>92,000</b>	<b>147,000</b>
<b>Per full-time worker</b>	<b>165,000</b>	<b>214,000</b>	<b>350,000</b>



# How Big is Our Growing Fiscal Burden?

**Our total fiscal burden can be translated and compared as follows:**

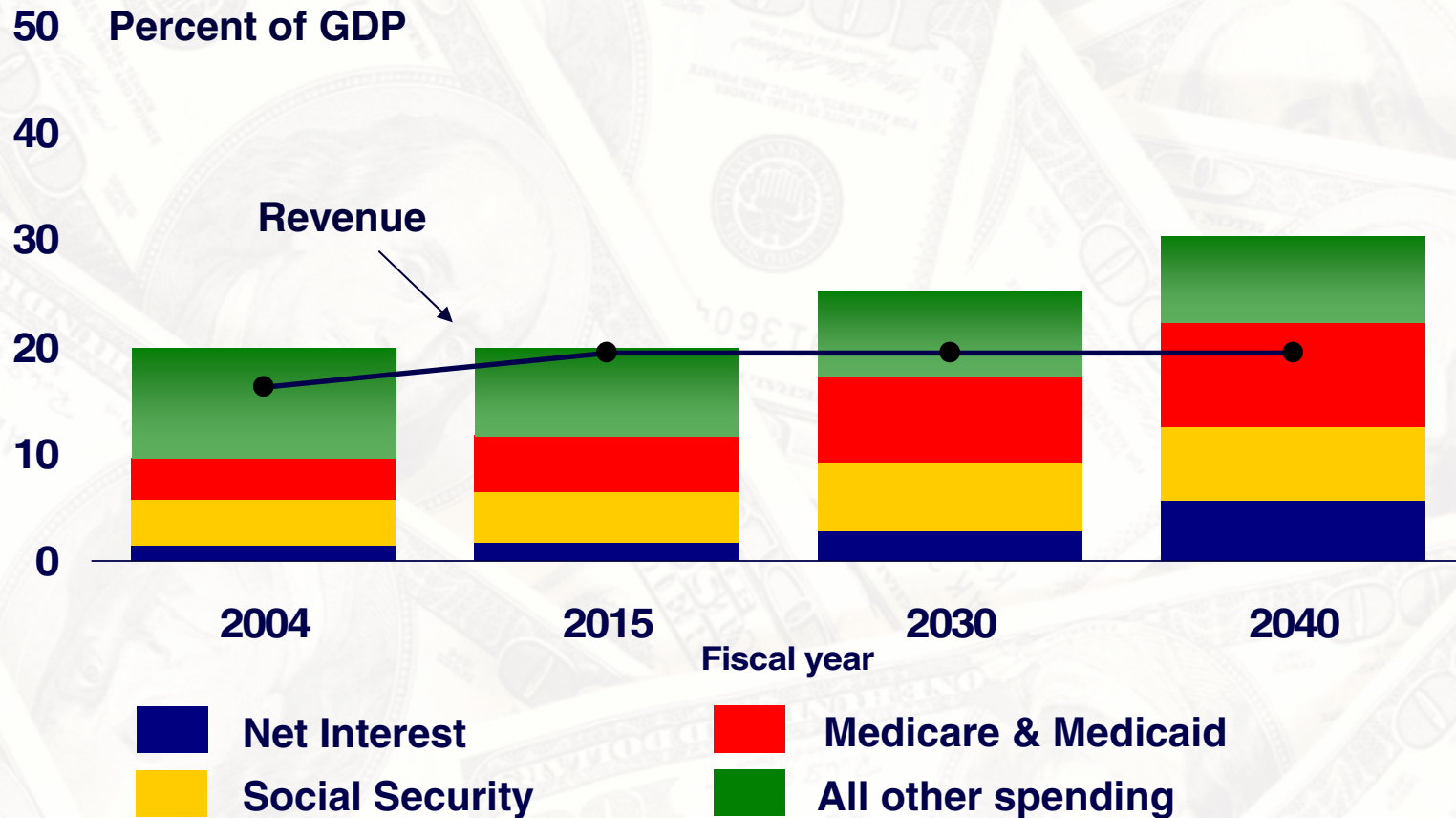
<b>Total fiscal exposures</b>	<b>\$43.3 trillion</b>
<b>Total household net worth</b>	<b>\$48.5 trillion</b>
<b>Burden/Net worth ratio</b>	<b>89 percent</b>
<b>Burden</b>	
<b>Per person</b>	<b>\$147,000</b>
<b>Per full-time worker</b>	<b>\$350,000</b>
<b>Per household</b>	<b>\$383,000</b>
<b>Income</b>	
<b>Median household income</b>	<b>\$44,389</b>
<b>Disposable personal income per capita</b>	<b>\$29,475</b>

Note: Net worth and income data are calendar year 2004 levels.

Sources: Federal Reserve Board for household net worth; Census Bureau for median household income; and the Bureau of Economic Analysis for disposable personal income per capita.

# Composition of Spending as a Share of GDP

## Under Baseline Extended

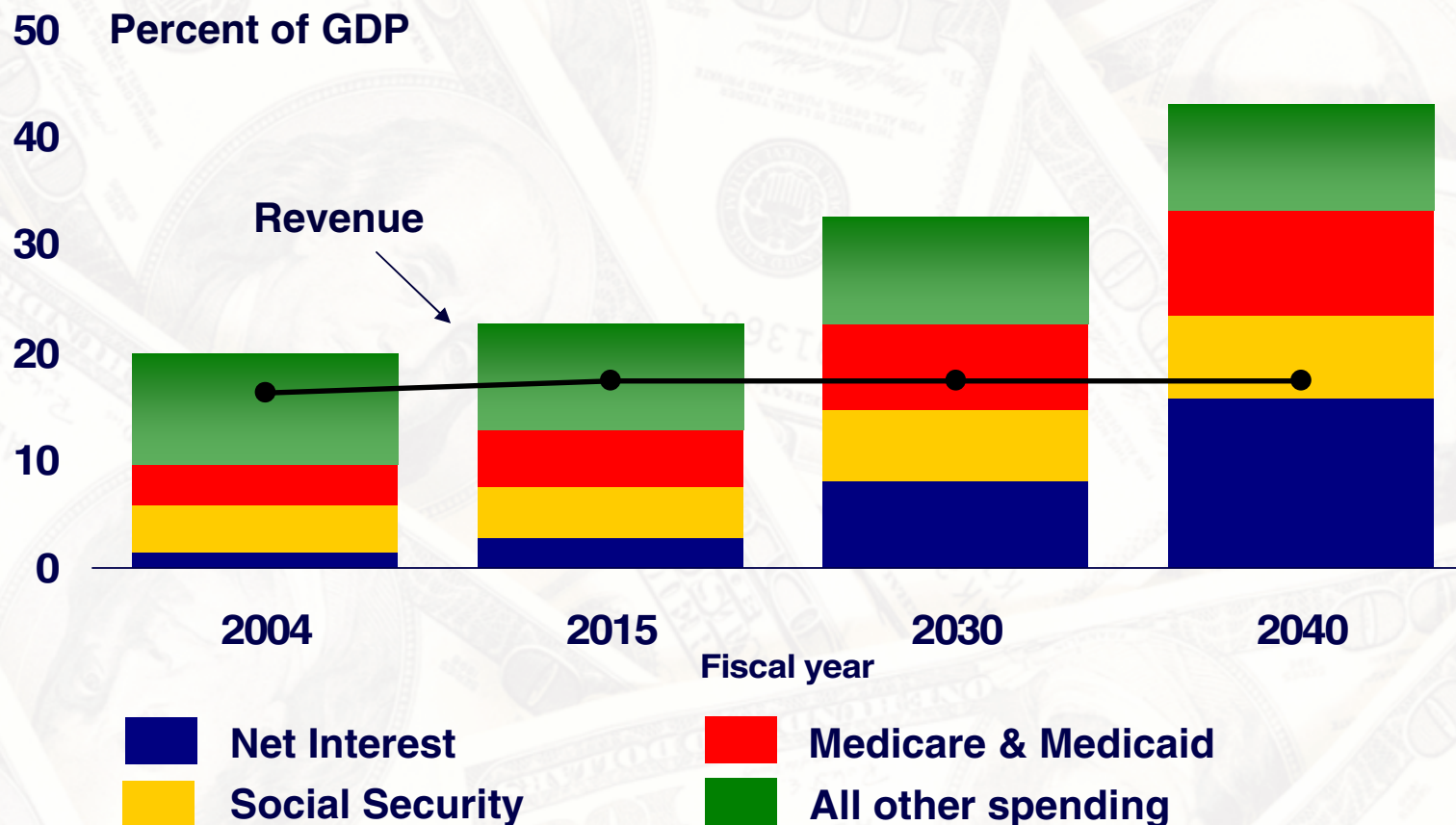


Notes: In addition to the expiration of tax cuts, revenue as a share of GDP increases through 2015 due to (1) real bracket creep, (2) more taxpayers becoming subject to the AMT, and (3) increased revenue from tax-deferred retirement accounts. After 2015, revenue as a share of GDP is held constant.

Source: GAO's August 2005 analysis.

# Composition of Spending as a Share of GDP

Assuming Discretionary Spending Grows with GDP after 2005  
and All Expiring Tax Provisions are Extended



Notes: Although expiring tax provisions are extended, revenue as a share of GDP increases through 2015 due to (1) real bracket creep, (2) more taxpayers becoming subject to the AMT, and (3) increased revenue from tax-deferred retirement accounts. After 2015, revenue as a share of GDP is held constant.

Source: GAO's August 2005 analysis.

# Debt per Capita Could Exceed GDP per Capita by 2030

Assuming Discretionary Spending Grows with GDP after 2005  
and All Expiring Tax Provisions are Extended

Per capita 2005 dollars

200,000

175,000

150,000

125,000

100,000

75,000

50,000

25,000

0

2005

2030

2040

■ Debt per Capita

■ GDP per Capita

Source: GAO's August 2005 analysis.



# Current Fiscal Policy Is Unsustainable

- **The “Status Quo” is Not an Option**

- We face large and growing structural deficits largely due to known demographic trends and rising health care costs.
- GAO’s simulations show that balancing the budget in 2040 could require actions as large as
  - Cutting total federal spending by 60 percent or
  - Raising federal taxes to 2.5 times today's level

- **Faster Economic Growth Can Help, but It Cannot Solve the Problem**

- Closing the current long-term fiscal gap based on reasonable assumptions would require real average annual economic growth in the double digit range every year for the next 75 years.
- During the 1990s, the economy grew at an average 3.2 percent per year.
- As a result, we cannot simply grow our way out of this problem. Tough choices will be required.

# The Way Forward: Three Pronged Approach

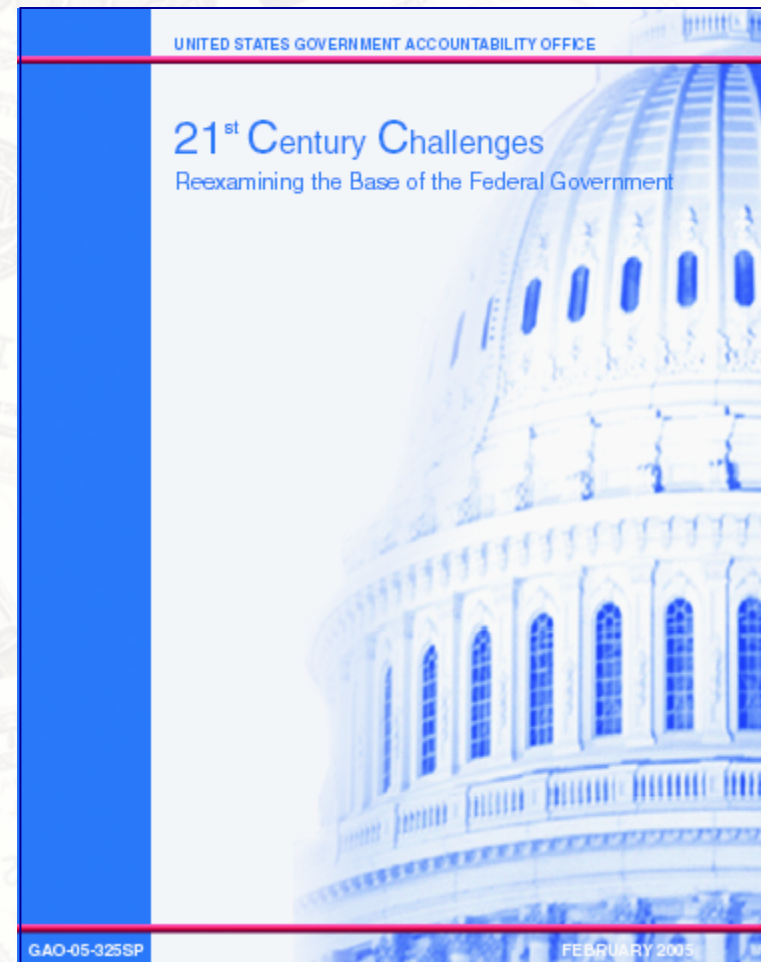
## **Re-examine Policies and Programs:**

- Restructure existing entitlement programs
- Reexamine the base of discretionary and other spending
- Review and revise our tax policy and enforcement programs

**Develop new metrics, measures, and control mechanisms for recognizing and considering long-term implications of spending and tax policies.**

# 21<sup>st</sup> Century Challenges Report

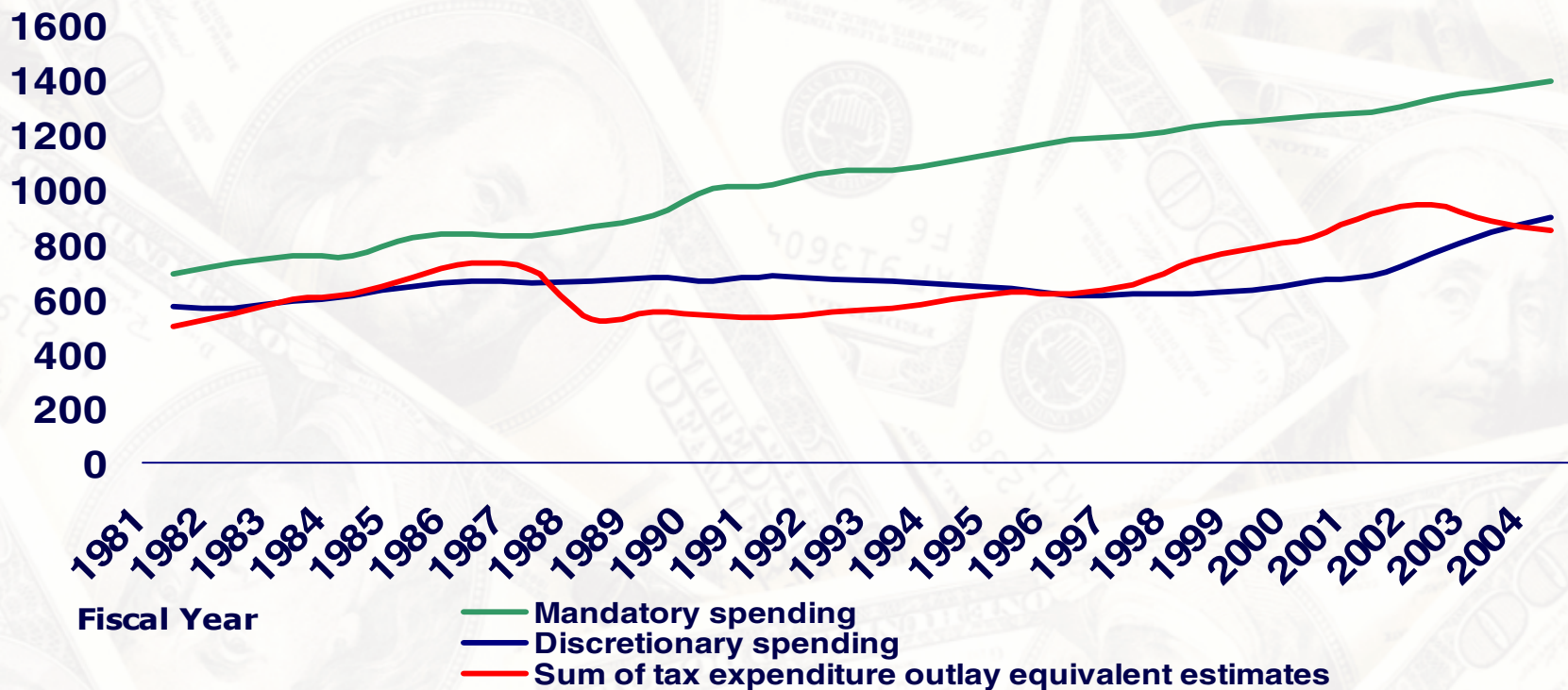
- Provides background, framework, and questions to assist in reexamining the base
- Covers entitlements & other mandatory spending, discretionary spending, and tax policies and programs
- Based on GAO's work for the Congress





# Measured on an Outlay Equivalent Basis, Tax Expenditures Exceeded Discretionary Spending for Most Years in the Last Decade

Dollars in billions (in constant 2004 dollars)



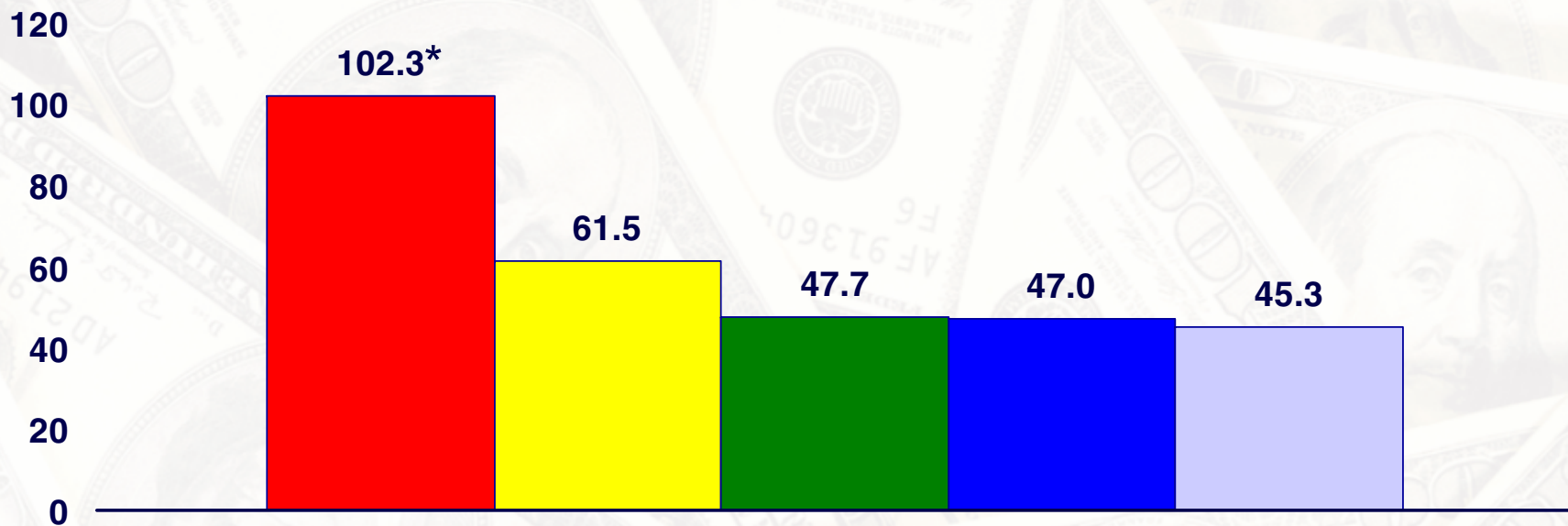
Note: Outlay-equivalent estimates represent the amount of budget outlays that would be required if the government were to provide taxpayers with the same after-tax income they receive through the tax expenditure. Outlay-equivalent estimates are useful to compare tax expenditures and other parts of the federal budget. Summing tax expenditure estimates does not take into account interactions between individual provisions.

Source: GAO Analysis of OMB's Budget Reports on Tax Expenditures, Fiscal Years 1976-2006.



# Health Care Is the Nation's Top Tax Expenditure in Fiscal Year 2004

Estimated dollars in billions



- Exclusion of employer contributions for insurance premiums and medical care
- Deductibility of mortgage interest on owner-occupied dwellings
- Exclusion of pension contributions and earnings: employer-sponsored 401(K) plans
- Exclusion of pension contributions and earnings: employer-sponsored defined benefit plans
- Deductibility of nonbusiness state and local taxes (other than on owner-occupied dwellings)

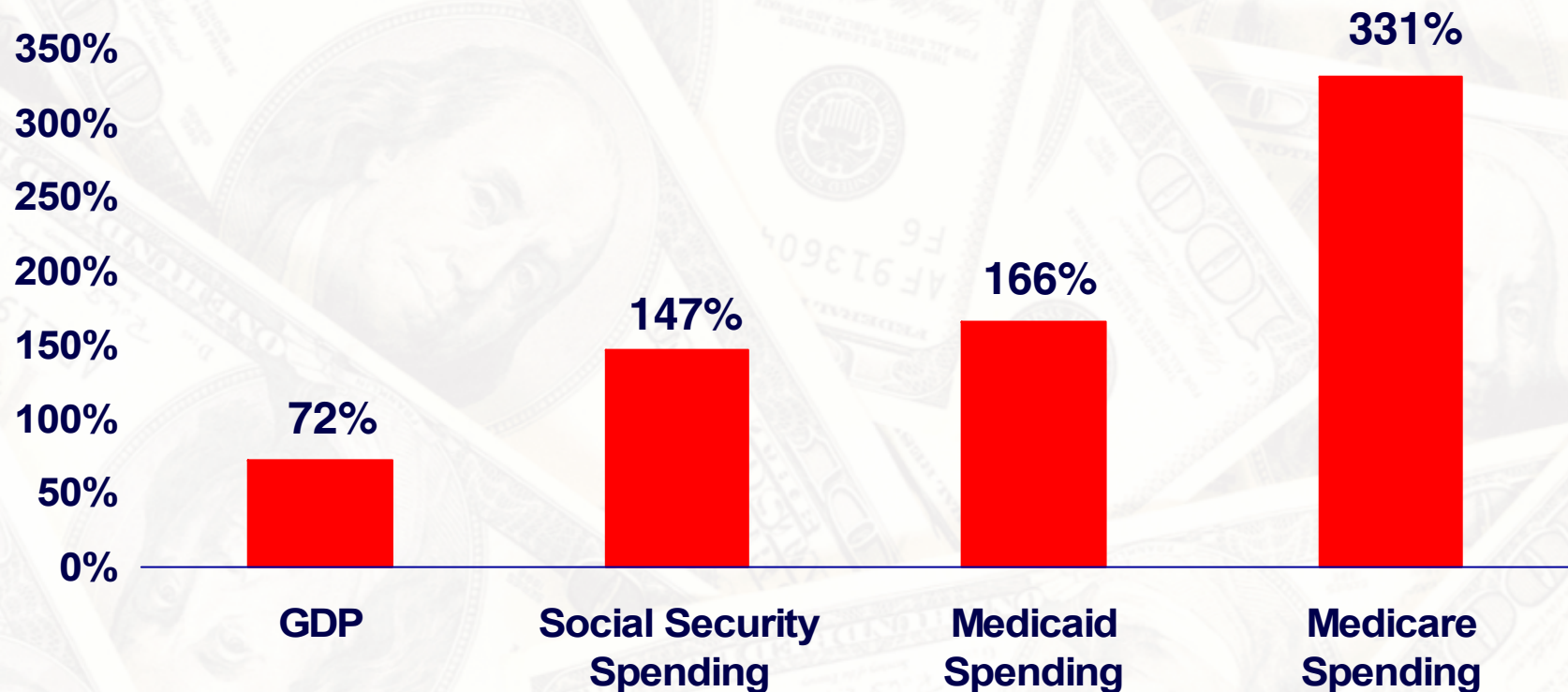
Note: "Tax expenditures" refers to the special tax provisions that are contained in the federal income taxes on individuals and corporations. OMB does not include forgone revenue from other federal taxes such as Social Security and Medicare payroll taxes.

\* If the payroll tax exclusion were also counted here, the total tax expenditure for employer contributions for health insurance premiums would be about 50 percent higher or \$153.5 billion.

Source: Office of Management and Budget (OMB), *Analytical Perspectives, Budget of the United States Government, Fiscal Year 2006*.

# Growth in Spending for Social Security, Medicare, and Medicaid Expected to Outpace Economic Growth

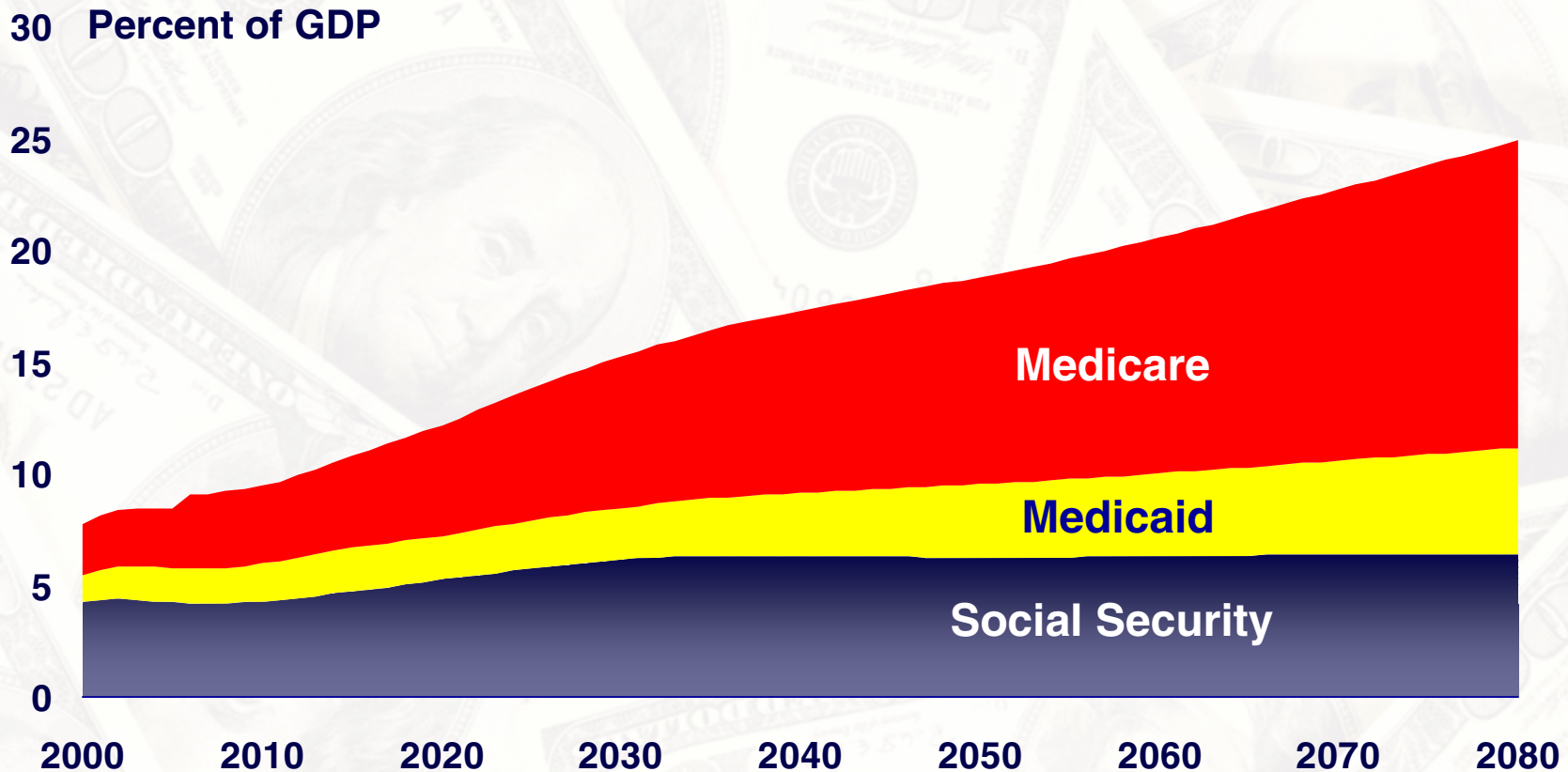
Growth in constant dollars 2005-2030



Note: Social Security and Medicare projections based on the intermediate assumptions of the 2005 Trustees' Reports. Medicaid projections based on CBO's December 2003 long-term projections for federal spending on Medicaid under mid-range assumptions.

Source: GAO analysis based on data from the Office of the Chief Actuary, Social Security Administration, Office of the Actuary, Centers for Medicare and Medicaid Services, and the Congressional Budget Office.

# Social Security, Medicare, and Medicaid Spending as a Percent of GDP



Note: Social Security and Medicare projections based on the intermediate assumptions of the 2005 Trustees' Reports. Medicaid projections based on CBO's January 2004 short-term Medicaid estimates and CBO's December 2003 long-term Medicaid projections under mid-range assumptions.

Source: GAO analysis based on data from the Office of the Chief Actuary, Social Security Administration, Office of the Actuary, Centers for Medicare and Medicaid Services, and the Congressional Budget Office.



# Moving the Debate Forward

- **The Sooner We Get Started, the Better**
  - The miracle of compounding is currently working against us
  - Less change would be needed, and there would be more time to make adjustments
  - Our demographic changes will serve to make reform more difficult over time
- **Need Public Education, Discussion, and Debate**
  - The role of government in the 21<sup>st</sup> Century
  - Which programs and policies should be changed and how
  - How government should be financed





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