

THE FISCAL HIGHROAD

A Responsible and Sustainable Path for America's Economic Future

A Joint Project of The Century Foundation and Dēmos

With the enactment of a \$787 billion economic recovery plan, combined with additional federal commitments in excess of \$1 trillion to help repair the broken financial services industry, many Americans are understandably fearful about the nation's long-term fiscal health. On top of familiar concerns about the challenges connected to the pending retirement of the large Baby Boom generation, the large new investments intended to stave off a second Great Depression sound potentially overwhelming for the government. The numbers are big, the issues are complicated, and media reports related to federal deficits and debt are often enormously confusing.

Further stoking that public fear and confusion is, unfortunately, part of the strategy pursued by well-funded institutions and foundations. These institutions are pursuing a low-road approach to fiscal responsibility—one focused on curtailing social investment and dismantling social insurance while maintaining current tax policy. All too often, the case is made based on misleading analyses and deceptive statistics. This document debunks some of the most commonly repeated claims intended to advance the country down that low-road path.

OUR NATION'S FISCAL FUTURE: TODAY'S REALITY AND FUTURE CHALLENGES

CLAIM: The United States faces \$56 trillion in liabilities and unfunded retirement and health care obligations—a burden of \$184,000 for every American.

REALITY: It's deceptive and misleading to use these figures—which are based on projections of health care costs over 75 years, and assumes no changes in tax revenues or reductions in health care costs.

More than four-fifths of the \$56 trillion figure is attributable to forecasts of relentlessly rising health care costs compounding unchecked over three-quarters of a century. It assumes no changes in existing tax and spending policies, including reforms that would curtail rising health care costs. Because health care costs have consistently climbed much faster than income in the United States, assuming the same rapid increases over many decades into the future produces such a big number due to the mathematics of compounding. Social Security's obligations, in contrast, are projected to rise much more slowly—from about 4.5 percent of GDP today to 6.5 percent in 2030. Because Social Security is in much stronger shape than health insurance programs, it's misleading to say there's a general "entitlements crisis" when the genuine cause for concern is confined to medical care.

Reforming the nation's health care system to reduce medical costs and improve the quality of health care is the central, genuine challenge facing the United States. Conflating this fundamental problem with estimates of the national debt in the future misdirects the public into believing austerity in the form of benefit cuts is the only solution, when in fact benefit cuts alone would only shift more and more health care costs onto individual Americans.

Relatively minor public policy adjustments, or modest shifts in the economic outlook, can cause this estimate to dramatically change. For example, estimates of the long-term fiscal gap would be sliced nearly in half if Congress simply allowed the 2001 and 2003 tax cuts to expire as scheduled at the end of 2010. In the 1990s, the long-term budget outlook greatly improved due to the strong economic performance that followed

the modest tax increases enacted in 1993. Unfortunately, this decade's tax cuts, military commitments, and troubled economy squandered those previous improvements in the country's fiscal health.

Finally, targeted tax increases almost certainly will be necessary in the future, particularly to help finance a more efficient health insurance system and ensure an adequate safety net for an aging population. But those hikes can be

targeted disproportionately on high-earners. For example, allowing the Bush tax cuts to expire after 2010 will significantly boost the obligations of wealthy taxpayers while greatly reducing the long-term fiscal gap without noticeably affecting the personal finances of the vast majority of Americans. So the claim that "every American" carries the same "burden" neglects the reality that policy responses can be designed to protect average citizens.

CLAIM: Tax rates will have to more than double in our lifetimes in order for our country to get by.

REALITY: The future prosperity of our nation depends on reversing decades of neglect in our social and physical infrastructure and reversing the regressive tax cuts of the last 8 years.

Our nation's long-term economic health depends primarily on improvements to its productive capacity, which will require effective public and private investments in human and physical capital, infrastructure, and innovations. If such investments succeed in producing broadly shared prosperity, tax revenues will increase as incomes rise, even if tax rates increase only modestly and in a progressive fashion. For example, in the aftermath of relatively minor tax increases in 1993, including small increases in the tax rates on upper-income Americans, the economy grew so vigorously that large and rising deficits transformed into budgetary surpluses. So there's little justification for asserting that tax rates will have to double in order "for our country to get by."

That said, it has become painfully obvious that the United States will need to adopt a system of universal health insur-

ance to enable our overall living standards to begin rising again while restoring our ability to compete with other developed countries—which almost without exception have universal medical coverage. Adopting universal health insurance will require tax increases, although ideally a number of other reforms would be included that would help to constrain the rapid growth in medical spending on technology and procedures that do little to improve health outcomes. The central challenge is finding ways to constrain medical costs while improving the quality of health care. There is no reason to believe that tax increases for universal coverage would have to amount to anywhere near double today's levies if reforms are implemented to reduce the rate of increase in health spending to the past levels in other countries.

CLAIM: With increasing government and personal debt, young people today are set to be the first generation that won't enjoy the same growth in standard of living as their parents.

REALITY: This generation of young people is falling behind their parents' generation due to a decline in job quality and disinvestment in higher education, and a failure to adopt policies that help young families balance their roles as workers and parents.

Major shifts in the economy combined with changes in public policy over the last 30 years, have diminished the economic opportunities available to a new generation. Across almost all indicators—income, education level, health insurance coverage—this generation of young people are falling behind that of their parents. The median earnings of young male workers are 19 percent lower than they were in 1975, while the typical earnings for young female workers have risen only a modest 4 percent. College educated young people have seen their earnings stagnate, while their student loan debt burdens now average nearly \$20,000. Half of young adults under 30 reported not having healthcare at some point during the last year.

But the cause of this generational decline is not the national debt, nor is it our obligations to senior citizens through Social Security and Medicare. Rather, today's young people are experiencing the full effect of nearly 30 years of seismic changes in the economy and a systemic retrenchment in all forms of social investment. From a higher education system that leaves many bright students behind and leaves those who graduate with too much debt to our failure to provide affordable and high quality child care for the working parents of young children, today's generation suffers from the 30-year long shift toward privatization, deregulation and disinvestment of anything related to the public purpose.

There is legitimate concern about the growing amount of debt accrued by college students—but a failure among low-road fiscal reformers that this rising debt burden is the result of declining investment in higher education at the state level and a shift away from grant-based federal financial aid to loan-based aid. The public policy responses proposed by the low-roaders would likely intensify this problem.

The worst outcome for today's young people would be taking the path prescribed by the low-road—balancing the federal budget for the sheer purpose of balancing the budget. This is a bargain in which young people will certainly lose as existing expenditures are cut or new investments rejected under the tired refrain of “we can't afford it.” For too long, our nation has skimmed on investments that young people in almost every other advanced nation take for granted: universal health care, universal child care and paid family leave, low or no-cost college tuition, and a sophisticated workforce development strategy to train and retrain the workforce.

Our nation can and must invest more in our nation's youngest members and continue to meet its promises to older Americans. Pitting the generations needs against each other is a cynical attempt to incite generational warfare, when the reality is young people want their grandparents and parents to live out their old age in dignity, and rightfully expect that a nation as rich as ours has enough resources to meet the needs of all of its people.

CLAIM: Future Social Security benefits are likely to be smaller than today's. In the year 2056, when today's 20-year-olds become eligible for full Social Security benefits, those benefits will be just 78% of what's been promised.

REALITY: Full Social Security benefits can be available for today's 20-somethings with modest adjustments.

Social Security benefits will be smaller in the future only if the low-roaders are successful in their efforts to scare Americans into thinking that the current system is wholly unsustainable. The most recent projects from the Congressional Budget Office show that even if no changes at all are implemented, Social Security should be able to continue paying promised benefits in full until the year 2049. After that point, payroll taxes from future workers would be able

to sustain 84 percent of scheduled benefits. Preventing that shortfall from occurring 40 years from now and thereafter could be accomplished by an increase in the payroll tax of 1.06 percent, or any other combination of tax increases and benefit reductions of that magnitude. Notwithstanding the rhetoric of budget alarmists, that's a relatively minor adjustment compared to the more significant reforms implemented in the past.

CLAIM: The government already spends a relatively small portion on education. In 2008, 3.3% of all government spending went to education, compared to 43% spent on Social Security, Medicare and Medicaid. In 2018, the government is expected to devote 2.5% of its spending to education, compared to 53% spent on Social Security, Medicare and Medicaid.

REALITY: By leaving out state and local spending on education, this claim conveys the misleading impression that spending on older Americans crowds out investment in younger ones.

That claim is terribly misleading because it refers only to federal spending, even though public education in the United States is predominantly financed by localities and states. For example, in the 2004-5 school year, total government spending on elementary and secondary education amounted to \$536 billion—slightly higher than Social Security outlays for that same period. But the federal govern-

ment contributed only 8.3 percent of that amount because our educational system is so decentralized. The federal government has always been only a relatively small contributor to public education, for reasons having nothing to do with social insurance programs and everything to do with the nation's historical reliance on states and localities for schooling.