

THE PUBLIC STRATEGIES GROUP 2005

# Reinventing Government Symposium

A Discussion of

THE **NATION'S GROWING**  
Fiscal Imbalance

The Honorable David M. Walker  
**Comptroller General of the United States**  
Las Vegas, Nevada  
January 31, 2005

# What Kind of Work Does GAO Do?

**Oversight**—designed to determine that government entities are doing what they are supposed to, that funds are being spent for the intended purpose, and that applicable laws and regulations are being complied with.

**Insight**—designed to determine what programs and policies work and those that don't. This involves sharing various best practices and benchmarking information and looking horizontally across the silos of government and vertically between the levels of government.

**Foresight**—designed to identify key trends and emerging challenges before they reach crisis proportions, e.g., challenges of an aging population and the demands of the information age, to changing security threats and fiscal challenges.

# GAO's Strategic Plan



## SERVING THE CONGRESS AND THE NATION GAO'S STRATEGIC PLAN FRAMEWORK

### MISSION

GAO exists to support the Congress in meeting its constitutional responsibilities and to help improve the performance and ensure the accountability of the federal government for the benefit of the American people.

### THEMES

Long-Term Fiscal Imbalance

National Security

Global Interdependence

Changing Economy

Demographics

Science and Technology

Quality of Life

Governance

### GOALS & OBJECTIVES

Provide Timely, Quality Service to the Congress and the Federal Government to ...

Address Current and Emerging Challenges to the Well-Being and Financial Security of the American People *related to ...*

- Health care needs and financing
- Education and protection of children
- Work opportunities and worker protection
- Retirement income security
- Effective system of justice
- Viable communities
- Natural resources use and environmental protection
- Physical infrastructure

Respond to Changing Security Threats and the Challenges of Global Interdependence *involving ...*

- Emerging threats
- Military capabilities and readiness
- Advancement of U.S. interests
- Global market forces

Help Transform the Federal Government's Role and How It Does Business to Meet 21st Century Challenges *by assessing ...*

- Roles in achieving federal objectives
- Government transformation
- Key management challenges and program risks
- Fiscal position and financing of the government

Maximize the Value of GAO by Being a Model Federal Agency and a World-Class Professional Services Organization *in the areas of ...*

- Client and customer satisfaction
- Strategic leadership
- Institutional knowledge and experience
- Process improvement
- Employer of choice

### CORE VALUES

Accountability

Integrity

Reliability

# GAO's High-Risk List 2005

| High-Risk Areas  | Designated High Risk |
|--|----------------------|
| <b>Addressing Challenges in Broad-based Transformations</b>  |                      |
| Protecting the Federal Government's Information Systems and the Nation's Critical Infrastructures  | 1997                 |
| Strategic Human Capital Management <sup>a</sup>  | 2001                 |
| U.S. Postal Service Transformation Efforts and Long-Term Outlook <sup>a</sup>                      | 2001                 |
| Managing Federal Real Property <sup>a</sup>  | 2003                 |
| Implementing and Transforming the Department of Homeland Security                                  | 2003                 |
| Establishing Appropriate and Effective Information-Sharing Mechanisms to Improve Homeland Security | 2005                 |
| DOD Approach to Business Transformation <sup>a</sup>   | 2005                 |
| DOD Supply Chain Management (formerly Inventory Management)  | 1990                 |
| DOD Weapon Systems Acquisition   | 1990                 |
| DOD Business Systems Modernization   | 1995                 |
| DOD Financial Management   | 1995                 |
| DOD Support Infrastructure Management  | 1997                 |
| DOD Personnel Security Clearance Program   | 2005                 |
| <b>Managing Federal Contracting More Effectively</b>   |                      |
| DOE Contract Management  | 1990                 |
| NASA Contract Management   | 1990                 |
| DOD Contract Management  | 1992                 |
| Management of Interagency Contracting  | 2005                 |
| <b>Assessing the Efficiency and Effectiveness of Tax Law Administration</b>                        |                      |
| Enforcement of Tax Laws <sup>a, b</sup>  | 1990                 |
| IRS Business Systems Modernization <sup>c</sup>  | 1995                 |
| <b>Modernizing and Safeguarding Insurance and Benefit Programs</b>                                 |                      |
| Medicare Program <sup>a</sup>  | 1990                 |
| HUD Single-Family Mortgage Insurance and Rental Housing Assistance Programs                        | 1994                 |
| Medicaid Program <sup>a</sup>  | 2003                 |
| Modernizing Federal Disability Programs <sup>a</sup>   | 2003                 |
| Pension Benefit Guaranty Corporation Single-Employer Insurance Program <sup>a</sup>                | 2003                 |
| <b>Other</b>   |                      |
| FAA Air Traffic Control Modernization  | 1995                 |

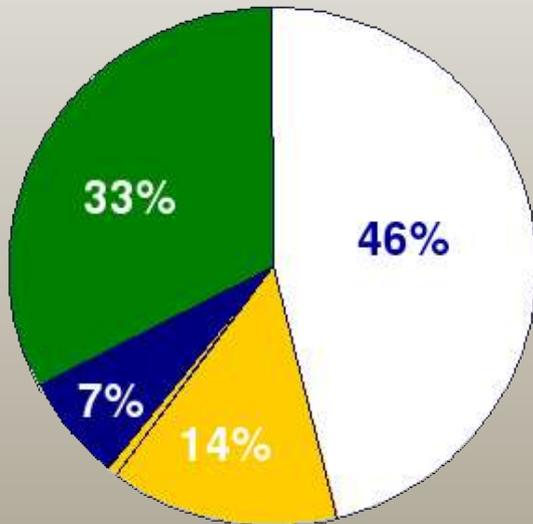
<sup>a</sup>Legislation is likely to be necessary, as a supplement to actions by the executive branch, in order to effectively address this high-risk area.

<sup>b</sup>Two high-risk areas—Collection of Unpaid Taxes and Earned Income Credit Noncompliance—have been consolidated to make this area.

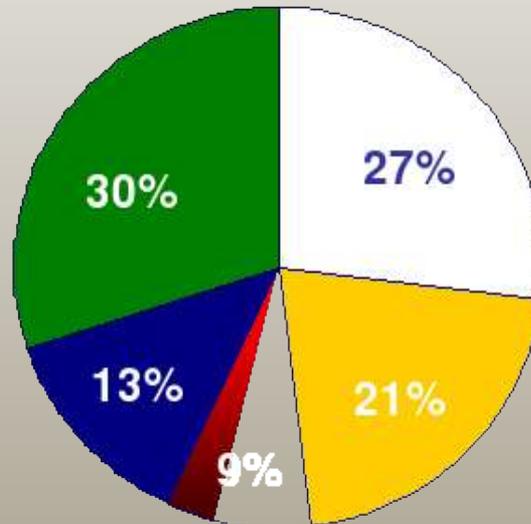
<sup>c</sup>The IRS Financial Management high-risk area has been incorporated into this high-risk area.

# Composition of Federal Spending

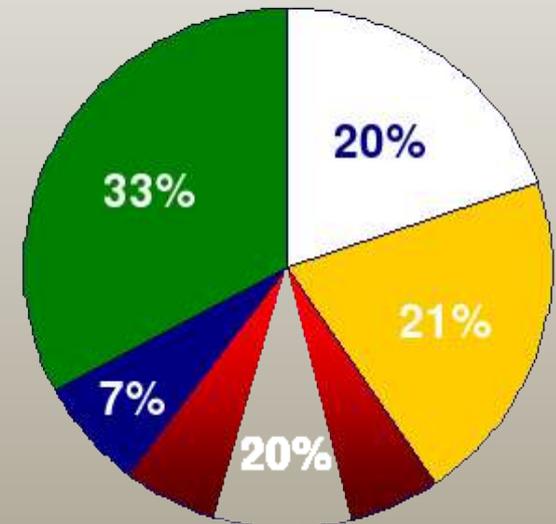
1964



1984



2004\*



Defense



Social Security



Medicare & Medicaid



Net interest



All other spending

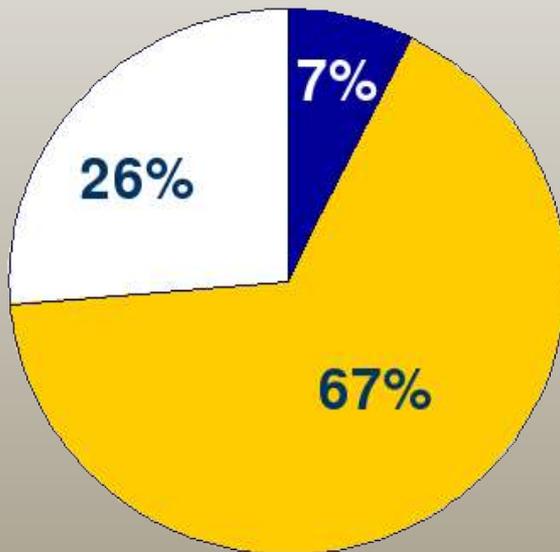
\*Current services estimate.

Note: Numbers may not add to 100 percent due to rounding.

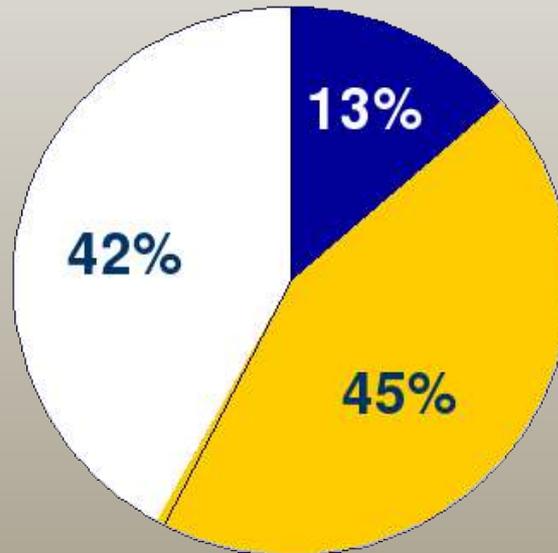
Source: *Budget of the United States Government, Fiscal Year 2005* (February 2004) and *Budget of the United States Government, Fiscal Year 2005, Mid-session Review* (July 2004), Office of Management and Budget.

# Federal Spending for Mandatory and Discretionary Programs

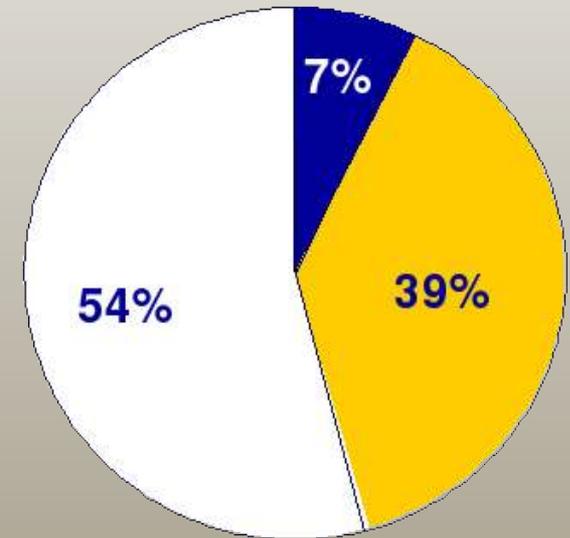
1964



1984



2004\*



 Net Interest

 Discretionary

 Mandatory

\*Current services estimate.

Note: Numbers may not add to 100 percent due to rounding.

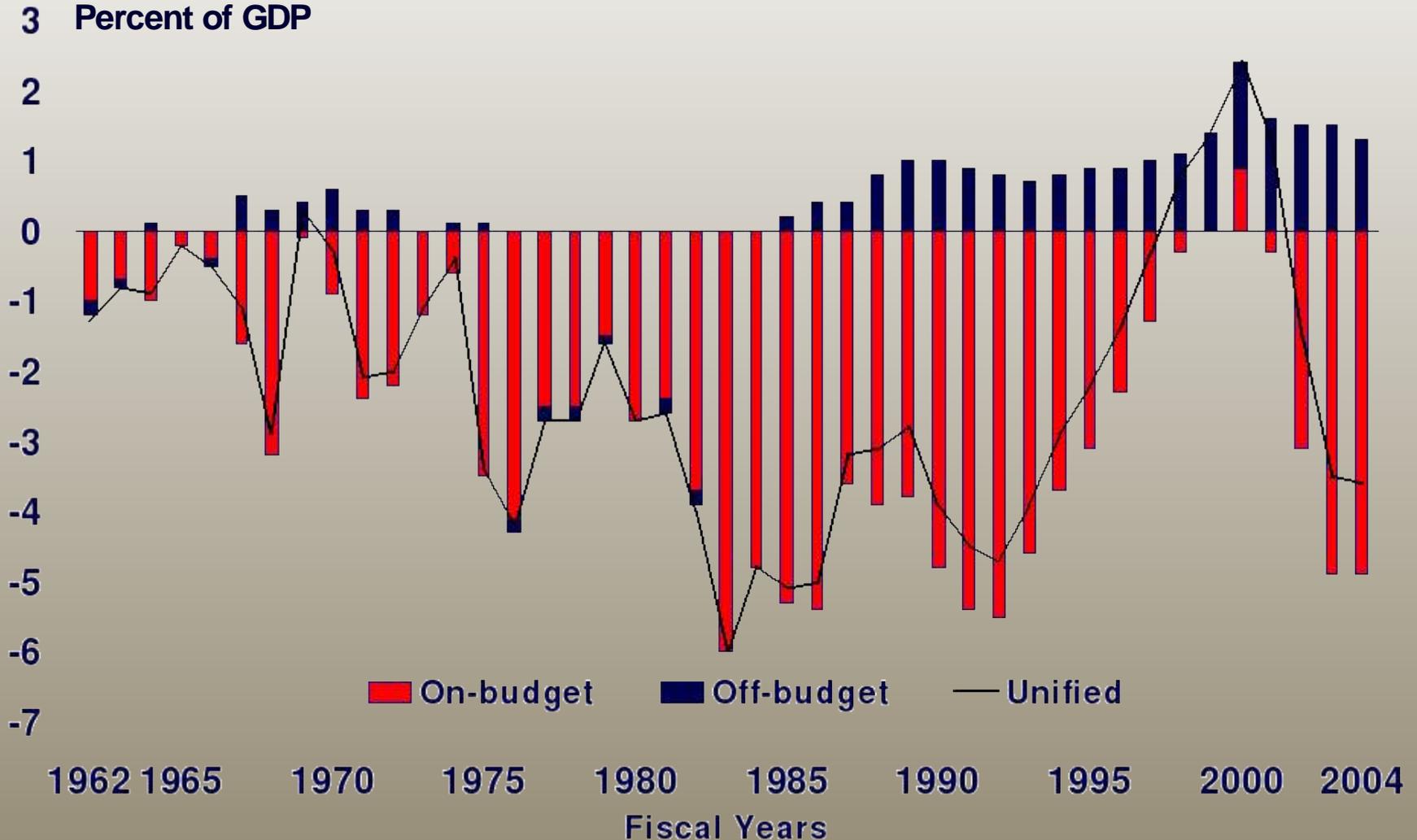
Source: *Budget of the United States Government, Fiscal Year 2005* (February 2004) and *Budget of the United States Government, Fiscal Year 2005, Mid-session Review* (July 2004), Office of Management and Budget.

# Fiscal Year 2004 Deficit Numbers

|                         |       | \$ Billion | % of GDP |
|-------------------------|-------|------------|----------|
| On-Budget Deficit       | (568) | (4.9)      |          |
| Social Security Surplus | 151   | 1.3        |          |
| Unified Deficit         |       | (413)      | (3.6)    |

# Surplus or Deficit as a Share of GDP

Fiscal Years 1962-2004



# Selected Fiscal Exposures: Sources and Examples 2004<sup>a</sup>

| Type  | Example (dollars in billions)  |
|---|--|
| Explicit liabilities  | Publicly held debt (\$4,297)   |
|   | Military and civilian pension and post-retirement health (\$3,059)                             |
|   | Veterans benefits payable (\$925)  |
|   | Environmental and disposal liabilities (\$249)   |
|   | Loan guarantees (\$43)   |
| Explicit financial commitments  | Undelivered orders (\$596)   |
|   | Long-term leases (\$39)  |
| Financial contingencies   | Unadjudicated claims (\$4)   |
|   | Pension Benefit Guaranty Corporation (\$96)  |
|   | Other national insurance programs (\$1)  |
|   | Government corporations e.g., Ginnie Mae   |
| Exposures implied by current policies or the public's expectations about the role of government | Debt held by government accounts (\$3,071) <sup>b</sup>  |
|   | Future Social Security benefit payments (\$3,699) <sup>c</sup>                                 |
|   | Future Medicare Part A benefit payments (\$8,236) <sup>c</sup>                                 |
|   | Future Medicare Part B benefit payments (\$11,416) <sup>c</sup>                                |
|   | Future Medicare Part D benefit payments (\$8,119) <sup>c</sup>                                 |
|   | Life cycle cost including deferred and future maintenance and operating costs (amount unknown) |
|   | Government Sponsored Enterprises e.g., Fannie Mae and Freddie Mac                              |

<sup>a</sup> All figures are for end of fiscal year 2004, except Social Security and Medicare estimates, which are as of January 1, 2004.

<sup>b</sup> This amount includes \$845 billion held by military and civilian pension funds that would offset the explicit liabilities reported by those funds.

<sup>c</sup> Figures for Social Security and Medicare are net of debt held by the trust funds (\$1,531 billion for Social Security, \$256 billion for Medicare Part A, and \$24 billion for Medicare Part B) and represent net present value estimates over a 75-year period. Over an infinite horizon, the estimate for Social Security would be \$10.4 trillion, \$21.8 trillion for Medicare Part A, \$23.2 trillion for Medicare Part B, and \$16.5 trillion for Medicare Part D.

Source: GAO analysis of data from the Department of the Treasury, the Office of the Chief Actuary, Social Security Administration, and the Office of the Actuary, Centers for Medicare and Medicaid Services.

# Another Way to Think About These Numbers

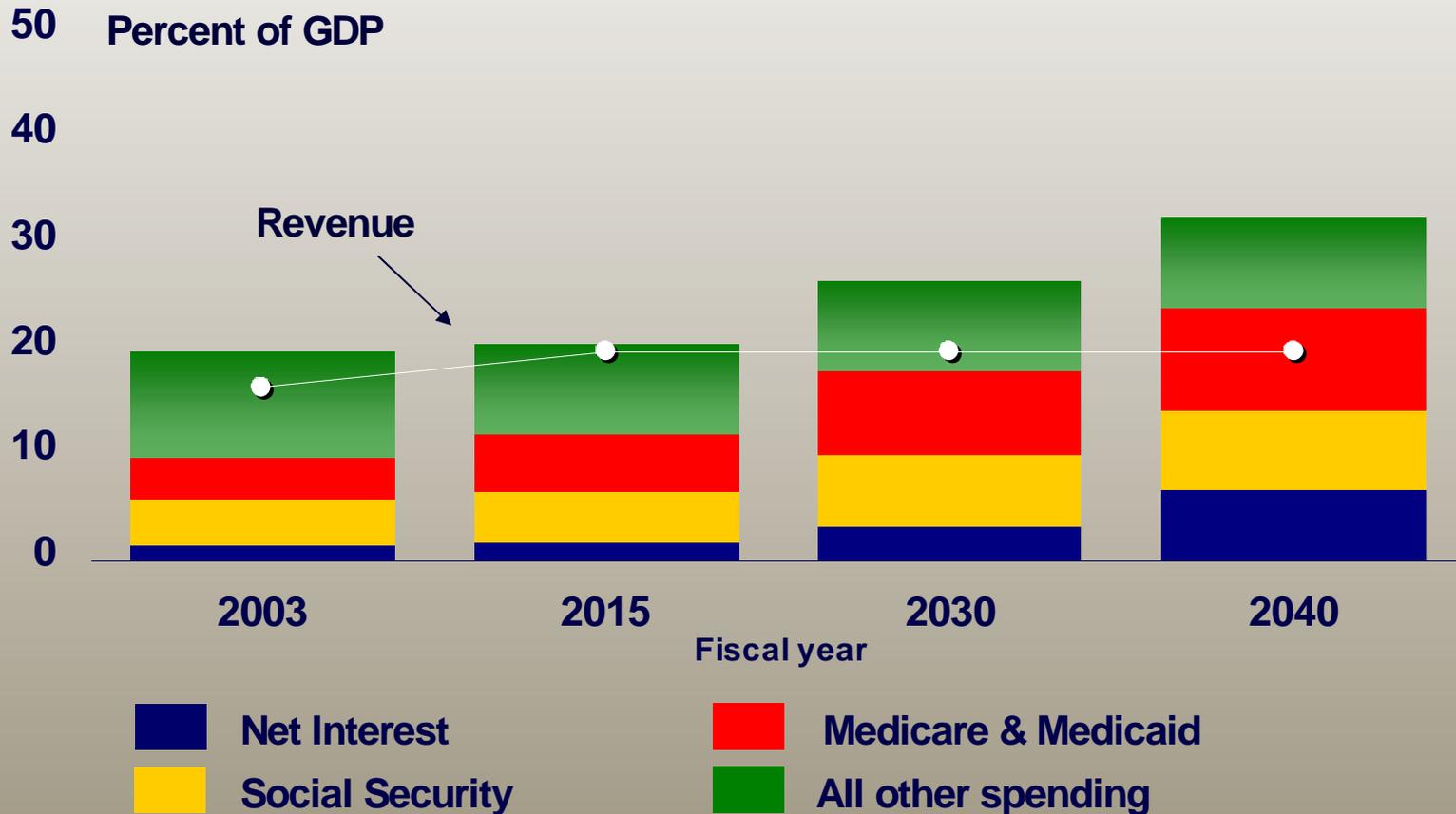
- Debt held by the public—\$4.3T
- Trust fund debt—\$3.1T
- Gross debt—\$7.4T
- Gross debt per person—about \$25,000
- If we add everything on the previous slide that is not included in gross debt, the burden rises to more than \$145,000 per person or more than \$350,000 per full-time worker. Alternatively, it amounts to a total unfunded burden of more than \$43 trillion in current dollars, which is about 19 times the current annual federal budget or about 4 times the current annual GDP.

Note: The calculations are based on 75-year projections for Social Security and Medicare.

Updated 12/17/04

# Composition of Spending as a Share of GDP

## Under Baseline Extended

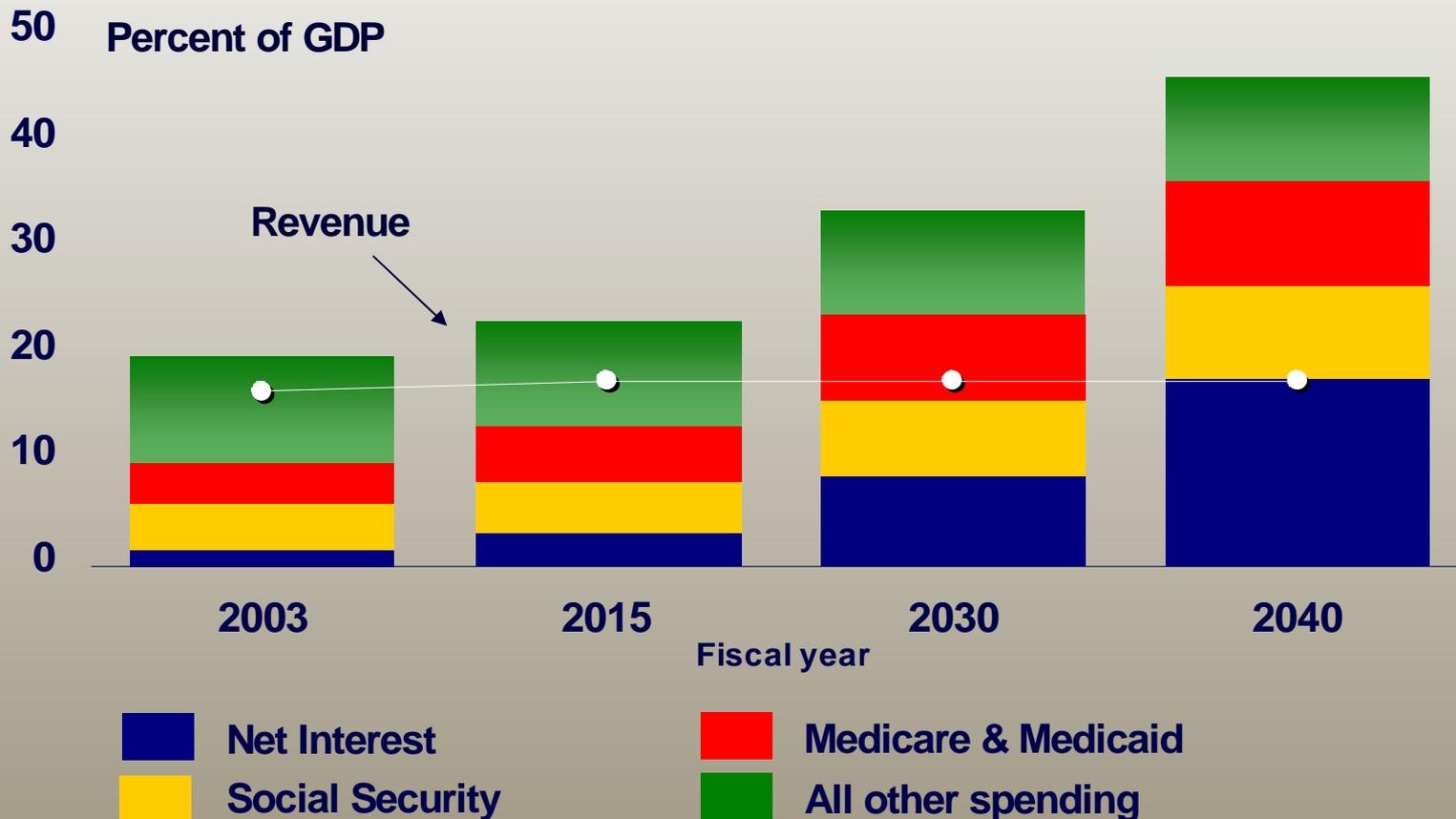


Notes: In addition to the expiration of tax cuts, revenue as a share of GDP increases through 2014 due to (1) real bracket creep, (2) more taxpayers becoming subject to the AMT, and (3) increased revenue from tax-deferred retirement accounts. After 2014, revenue as a share of GDP is held constant. Budgetary effects due to passage of the Working Families Tax Relief Act of 2004 are not reflected in this simulation.

Source: GAO's September 2004 analysis.

# Composition of Spending as a Share of GDP

Assuming Discretionary Spending Grows with GDP after 2004  
and All Expiring Tax Provisions are Extended



Notes: Although expiring tax provisions are extended, revenue as a share of GDP increases through 2014 due to (1) real bracket creep, (2) more taxpayers becoming subject to the AMT, and (3) increased revenue from tax-deferred retirement accounts. After 2014, revenue as a share of GDP is held constant.

Source: GAO's September 2004 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 about 60 percent or
    - Raising taxes to about 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 responsible 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 Sooner We Get Started, the Better**
  - Less change would be needed, and there would be more time to make adjustments.
  - The miracle of compounding would work with us rather than against us.
  - Our demographic changes will serve to make reform more difficult over time.

# The Way Forward

- Implement new accounting and reporting approaches and new budget control mechanisms for considering the impact of spending and tax policies and decisions over the long term
- Develop new metrics for measuring the impact of policies and decisions over the long term (e.g., key national indicators to measure our Nation's position and progress over time and in relation to other countries)
- Reexamine the base—question existing programs, policies and activities

# Long-term Fiscal Challenges

## Demand New Metrics, Mechanisms, and Processes

- Accounting and reporting policies for trust funds, Social Security, Medicare, Veterans benefits, among other things, need to be reviewed and revised (e.g., possible fiscal burden statement with per capita and intergenerational figures)
- The current budget time horizon [2-year, 5-year, 10-year] does not capture many long-term costs—e.g. Social Security, Medicare, pension insurance—and other major tax and spending provisions
- Cash and obligations-based budgeting is misleading for insurance and some benefit programs
- Budget controls have expired—and we need to go beyond “holding the line” to “changing the base” in spending and tax policies

# Improved Metrics, Measures and Processes: Some Ideas

- Provide information on long-term costs of major spending and tax proposals before they are voted on, including showing long-term costs even for proposals that sunset
- Establish an OMB annual report on fiscal exposures, including appropriate measures and how to address them
- Consider fiscal targets, triggers, sunset provisions and points of order with focus on limiting growth of long-term commitments
- Move to accrual budgeting for employee pension, retiree health; disclose “risk assumed” [missing premium] for insurance
- Reinststitute budget controls (caps & PAYGO)

# We Need a Multifaceted Approach to Close the Long-Term Fiscal Gap

## **Policy:**

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

## **Operations:**

- Reassess and revise how the government does business (e.g., management, planning and operational issues)
- Consider who should provide government services (e.g., sourcing strategy)

# Illustrative Generic Re-examination Questions

- Is the program, policy, function or activity a direct result of specific legislation?
- Is the current mission fully consistent with the initial or updated statutory mission (e.g., no significant mission creep or morphing)?
- Does it relate to an issue of nationwide interest? If so, is a federal role warranted based on the likely failure of private markets or state and local governments to address the underlying problem or concern? Does it encourage or discourage these other sectors from investing their own resources to address the problem?
- Have there been significant changes in the country or the world that relate to the reason for initiating it?

# Illustrative Generic Re-examination Questions

- If the answer to the last question is yes, should the activity be changed or terminated, and if so, how? If the answer is unclear as to whether changes make it no longer necessary, then ask, when, if ever, will there no longer be a need for a federal role? In addition, ask, would we enact it the same way if we were starting over today? Has it been subject to a comprehensive review, reassessment and re-prioritization by a qualified and independent entity? If so, when? Have there been significant changes since then? If so, is another review called for?
- How does it measure success? Are the measures reasonable and consistent with the applicable statutory purpose? Are the measures outcome-based, and are all applicable costs and benefits being considered? If not, what is being done to do so?
- If there are outcome-based measures, how successful is it based on these measures?
- Is it well targeted to those with the greatest needs and the least capacity to meet those needs?

# Illustrative Generic Re-examination Questions

- Is it affordable and financially sustainable over the longer term, given known cost trends and future fiscal imbalances?
- Is it using the most cost effective or net beneficial approaches when compared to other tools and program designs?
- What would be the likely consequences of eliminating the program, policy, function, or activity? What would be the likely implications if its total funding was cut by 25 percent?
- If it fares well after considering all of these questions, is the responsible entity employing prevailing best practices to discharging its responsibilities and achieving its mission (e.g., strategic planning, organizational alignment, human capital strategy, financial management, technology management, acquisitions/sourcing strategy, change management, knowledge management, client/customer service, risk management)?

# Selected 21<sup>st</sup> Century Questions

- Do we need all three elements of the current triad nuclear deterrent strategy and if so, do we need to reconsider the size and nature of each component?
- What opportunities exist to dispose of excess federal facilities or better leverage surplus in private sector capacity to make the federal portfolio more relevant to current mission and less costly?
- How should Social Security be reformed to make it both solvent and sustainable while better aligning it with 21<sup>st</sup> century economic, demographic and fiscal realities?
- Do tax incentives and preferences need to be reconsidered? For example, can adequate health care coverage be achieved at less cost and greater equity through fundamental redesign of the current health tax preferences?

# Key National Indicators

- **WHAT:** A portfolio of economic, social, environmental and security related outcome-based statistics that could be used to help assess the nation's and other governmental jurisdictions' position and progress
- **WHO:** Many countries and several states and localities have already undertaken related initiatives (e.g., Australia, New Zealand, Canada, United Kingdom, Oregon, Washington, and Charlotte)
- **WHY:** Development of such a portfolio of indicators could have a number of possible benefits, including
  - Serving as a framework for related strategic planning efforts
  - Enhancing performance and accountability reporting
  - Informing public policy decisions, including much needed baseline reviews of existing government policies, programs, functions, and activities
  - Facilitating public education and debate as well as an informed electorate
- **WAY FORWARD:** Consortium of key players led by the National Academies domestically and related OECD efforts internationally

# **Trans** **FORMATION**

## **Webster's definition**

**An act, process, or instance of  
change in structure appearance, or  
character**

**A conversion, revolution,  
makeover, alteration, or renovation**

# The Case for Change

- **Government is on a “burning platform,” and the status quo way of doing business is unacceptable for a variety of reasons, including:**
  - Past fiscal trends and significant long-range challenges
  - Rising public expectations for demonstrable results and enhanced responsiveness
  - Selected trends and challenges having no boundaries
  - Additional resource demands due to recent terrorism events in the United States
  - Government performance/accountability and high risk challenges, including the lack of effective human capital strategies

# Transformation Has Different Dimensions

**DOD**

**DHS**

**U. S. Postal Service**

**IRS**

**DOE**

**NASA**

**Human Capital Strategy**

**Financial Management**

**Information Technology**

**Sourcing Strategy**

**Disability Programs**

**Real Property Management**

Note: All of the above are on GAO's High Risk List to one extent or the other.

# Transformation: A New Model for Government Organizations

## Government organizations will need to:

- Become less hierarchical, process-oriented, stovepiped, and inwardly focused.
- Become more partnership-based, results-oriented, integrated, and externally focused.
- Achieve a better balance between results, customer, and employee focus.
- Work better with other governmental organizations, non-governmental organizations, and the private sector, both domestically and internationally, to achieve results.

# Keys to Making Change Happen

- Commitment and sustained leadership (e.g., “leading by example” and “tone at the top”)
- Demonstrated need for change (i.e., burning platform)
- Start at the top and with the new people (transformation takes 7+ years)
- Process matters (e.g., employee involvement) – Don't fight a two-front war
- 15-percent rule
- Identifiable and measurable progress over time
- Communication, communication, communication
- Figure out what's right versus what's popular
- Patience, persistence, perseverance to pain before you prevail

# Key Transformation Elements

- People
- Process
- Partnerships
- Technology
- Environment

The most important of the five is **PEOPLE** —  
an agency's human capital.



Transformation is about **CREATING**  
the future rather than **PERFECTING**  
the past.

Effective **HUMAN CAPITAL** strategy  
is key to any **SUCCESSFUL**  
transformation effort

# Key Dates Highlight Long Term Challenges of the Social Security System

| <b>Date</b>              | <b>Event</b>   |
|--------------------------|--|
| 2008                     | Social Security cash surplus begins to decline   |
| 2018                     | Annual benefit costs exceed cash revenue from taxes  |
| 2028                     | Trust fund ceases to grow because even taxes plus interest fall short of benefits            |
| 2042 (SSA)<br>2052 (CBO) | Trust fund exhausted, annual revenues sufficient to pay about 73% – 81% of promised benefits |

Sources: Social Security Administration, *The 2004 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds*. Washington, DC, March 2004. Congressional Budget Office, *The Outlook for Social Security: Potential Range of Social Security Outlays and Revenues Under Current Law*. Washington, DC, June 2004.

# **Social Security: The Bottom Line**

## **Illustrative Questions and Answers Based on the Latest Trustees' Reports**

- Does Social Security have a financing problem? [Yes]
- Will the Social Security program ever go bust? [No]
- Will the Social Security trust fund balance ever be exhausted? [Yes]
- Should the trust fund solvency date be the primary action-forcing event for Social Security reform? [No]
- What other factors should be considered?
  - Cash flow
  - Total unfunded commitments
  - Percent of the budget and GDP
  - Percent of taxable payroll

# Questions and Answers (cont'd)

- Should we act sooner rather than later to reform Social Security? [Yes]
  - Time is working against us
  - We have an opportunity to exceed the expectations of every generation of Americans
  - We have bigger problems that we ultimately will have to address
  - A successful reform effort would help to improve the credibility of government and enhance confidence in government

# Questions and Answers (cont'd)

- Will individual accounts solve the problem by themselves?  
[No]
- Should they be considered as part of a more comprehensive reform proposal? [Yes]
- What other types of reforms need to be considered?
  - Strengthening progressivity (e.g., replacement rates)
  - Indexing formulas
  - Retirement ages
  - Tax base and rates

# Questions and Answers (cont'd)

- What is an example of a government retirement system that includes private accounts? [The Federal Thrift Savings Plan]
- Would individual accounts involve significant transition costs? [Yes]
- What other possible implications would individual accounts have?
  - Personal savings rate
  - Rates of return on Social Security payroll taxes
  - Pre- and post-retirement survivors' benefits
  - Savings and investment education
  - Supplemental retirement savings vehicle

# Questions and Answers (cont'd)

- Should we consider both promised and funded benefits in analyzing Social Security Reform proposals? [Yes]
- Should we consider both cash and present value related costs and implications of Social Security reform proposals? [Yes]
- Can Social Security reform exceed the expectations of all generations of Americans? [Yes]
- Does the Social Security reform process matter? [Yes]
- Should Social Security be about the public good versus political gain? [Yes]

# GAO Criteria For Evaluating Social Security Reform Proposals

Reform proposals should be evaluated as packages that strike a balance among individual reform elements and important interactive effects.

Comprehensive proposals can be evaluated against three basic criteria:

- Financing sustainable solvency
- Balancing adequacy and equity in the benefits structure
- Implementing and administering reforms

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