UNITED STATES GOVERNMENT ACCOUNTABILITY OFFICE

21st Century Challenges

Reexamining the Base of the Federal Government

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Preface

The Government Accountability Office has long had a statutory responsibility for monitoring the condition of the nation's finances. Recently, in our role as the auditor of the U.S. government's consolidated financial statements, we included an emphasis paragraph in our audit report for the fiscal year ended September 30, 2004 expressing our concerns that the fiscal policies in place today will—absent unprecedented changes in tax and/or spending policies—result in large, escalating, and persistent deficits that are economically unsustainable over the long term. This conclusion is based on the results of GAO's long-term budget model, which the agency has used since 1992.

Over the long term, the nation's growing fiscal imbalance stems primarily from the aging of the population and rising health care costs. These trends are compounded by the presence of near-term deficits arising from new discretionary and mandatory spending as well as lower revenues as a share of the economy. Absent significant changes on the spending and/or revenue sides of the budget, these long term deficits will encumber a growing share of federal resources and test the capacity of current and future generations to afford both today's and tomorrow's commitments. Continuing on this unsustainable path will gradually erode, if not suddenly damage, our economy, our standard of living and ultimately our national security.

Addressing the nation's long-term fiscal imbalances constitutes a major transformational challenge that may take a generation to resolve. Given the size of our projected deficit we will not be able to grow our way out of this problem—tough choices will be required. In addition, traditional incremental approaches to budgeting will need to give way to more fundamental and periodic reexaminations of the base of government, ultimately covering discretionary and mandatory programs as well as the revenue side of the budget. The nature and magnitude of the fiscal, security, and economic and other adjustments that need to be considered are not amenable to "quick fixes;" rather they will likely require an iterative, thoughtful process of disciplined changes and reforms over many years. Nonetheless, the magnitude of and potential disruption from related changes can be mitigated if the necessary policy changes are made sooner rather than later.

While prompted by fiscal necessity, such a fundamental review of major program and policy areas can also serve the vital function of updating the federal government's programs and priorities to meet current and future challenges. Many current federal programs and policies, in fact, were designed decades ago to respond to trends and challenges that existed at the time of their creation. Given our recent entry into a new century, we have been reminded of how much has changed in the past several decades—whether it be rapid shifts in the security threats facing the nation, the aging of our population, the globalization of economic transactions, escalating health care costs, increased environmental concerns, or the significant advances in technologies and transportation systems. Moreover, given the fiscal constraints we are likely to face for many years to come, such a reexamination may very well be essential to address newly emergent needs without unduly and unfairly burdening future generations of taxpayers.

Having identified the major fiscal challenge facing the nation, and given our role in supporting the Congress, we believe that GAO also has an obligation to provide policymakers with support in identifying issues and options that could help to address these fiscal pressures. In this report, we build on our past and pending work—90 percent of which is requested by the Congress or required by law—to provide policy makers with a comprehensive compendium of those areas throughout government that could be considered ripe for reexamination and review. This report is consistent with other GAO products, such as our high-risk series and budget options reports, where we pull together our insights and previous work for the Congress to help in its budget and programmatic deliberations and oversight activities.[1]

This report is intended to help the Congress in reviewing and reconsidering the base of federal spending and tax programs. It is intended as one input among many that Congress will receive as it decides what its agenda will be for oversight and program review.

[1]GAO, *High-Risk Series: An Update*, GAO-05-207 (Washington, D.C.: January 2005) and *Opportunities for Congressional Oversight and Improved Use of Taxpayer Funds*, GAO-04-649 (Washington, D.C., May 7, 2004).

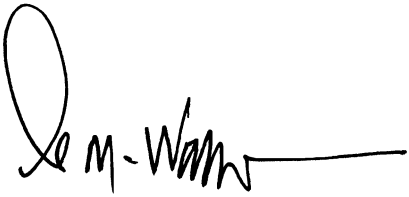
We have framed the issues presented as illustrative questions for policymakers to consider as a supplement to their own efforts. The questions are drawn from GAO's issued work, our strategic plan prepared in consultation with the Congress, input from several inspectors general and the institutional knowledge of our staff. They cover discretionary spending, mandatory spending, including entitlements, as well as tax policies and programs. While answers to these questions may draw on the work of GAO and others, only elected officials can and should decide which questions to address as well as how and when to address them.

The report is organized in three sections. The first section sets the stage by providing the rationale for reexamining the base of the federal government and the scope of GAO's effort. The second section is organized around 12 areas of federal activity and includes narratives discussing emerging changes in each area as well as several illustrative reexamination questions for each area. The third section provides some perspective on various strategies, processes, and approaches that should be considered as a possible means to address the issues and questions raised in this report.

GAO stands ready to assist the Congress in addressing the much needed base-line review of existing federal programs, policies, functions, and activities.

The report was prepared under the direction of Paul Posner, Managing Director for Federal Budget and Intergovernmental Issues in our Strategic Issues team, with the assistance of every GAO team. Ty Mitchell and John Forrester of our Strategic Issues team were the key staff responsible for the development and

publication of this document. Copies of this report are available upon request. In addition this document will be available at no charge on the GAO Web site at http://www.gao.gov.



David M. Walker
Comptroller General
of the United States

Section 1: Introduction

The federal government's financial condition and long-term fiscal outlook present enormous challenges to the nation's ability to respond to emerging forces reshaping American society, the United States' place in the world, and the future role of the federal government. The near-term deficits are daunting—a $412 billion unified budget deficit in fiscal year 2004 (including a $567 billion on-budget deficit and a $155 billion off-budget surplus) and a $368 billion deficit (not including any supplemental appropriations) forecast for fiscal year 2005 by the Congressional Budget Office (CBO). If these near-term deficits represented only a short-term phenomenon prompted by such factors as economic downturn or national security crises—there would be less cause for concern. However, deficits have grown notwithstanding the relatively strong rebound of the economy from the recession in 2001, and the incremental costs of responding to the nation's global war against terrorism and homeland security represent only a relatively small fraction of current and projected deficits. Morever, based on the U.S. Government Accountability Office's (GAO) long-range fiscal simulations, the current fiscal condition is but a prelude to a much more daunting long-term fiscal outlook.

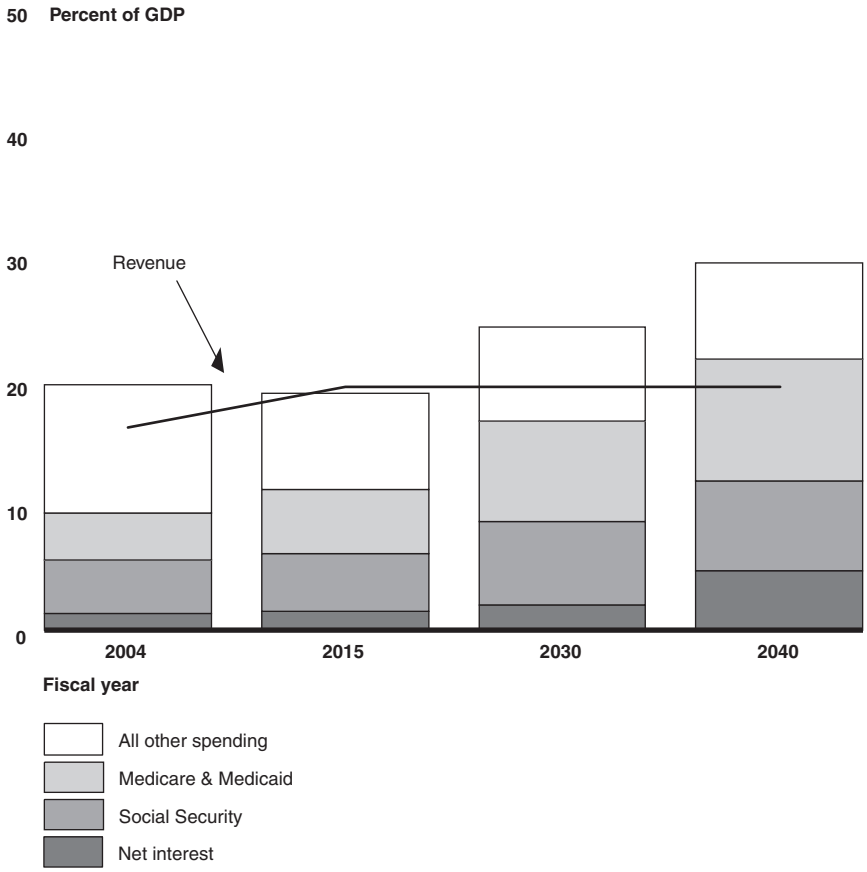
Over the next few decades, as the baby boom generation retires, federal spending on retirement and health programs—Social Security, Medicare, Medicaid, and other federal pension, health, and disability programs—will grow dramatically. Other federal fiscal commitments, ranging from explicit liabilities, such as environmental cleanup requirements to more implicit obligations presented by lifecycle costs of capital acquisitions, will also bind the nation's fiscal future. Absent policy changes on the spending and/or revenue sides of the budget, a growing imbalance between expected federal spending and tax revenues will mean escalating and ultimately unsustainable federal deficits and debt that serve to threaten our future national security as well as the standard of living for the American people. Ultimately, the nation will have to decide what level of federal benefits and spending it wants and how it will pay for these benefits.

The nation's long-term fiscal outlook is daunting under many different policy scenarios and assumptions. For instance, under a

fiscally restrained scenario, if discretionary spending grew only with inflation over the next 10 years and all existing tax cuts expire when scheduled under current law, spending for Social Security and health care programs would grow to consume over three-quarters of federal revenue by 2040. (See fig. 1.) On the other hand, if discretionary spending grew at the same rate as the economy in the near term and if all tax cuts were extended, federal revenues may just be adequate to pay interest on the growing federal debt by 2040. (See fig. 2.) Numerous alternative scenarios can be developed incorporating different combinations of possible policy choices and economic assumptions, but these two scenarios can be viewed as "bookends" showing a range of possible outcomes.[2]

[2]To view alternative scenarios between these "bookends," see the section on The Nation's Long-Term Fiscal Challenge on GAO's Web site (www.gao.gov/special.pubs/longterm/).

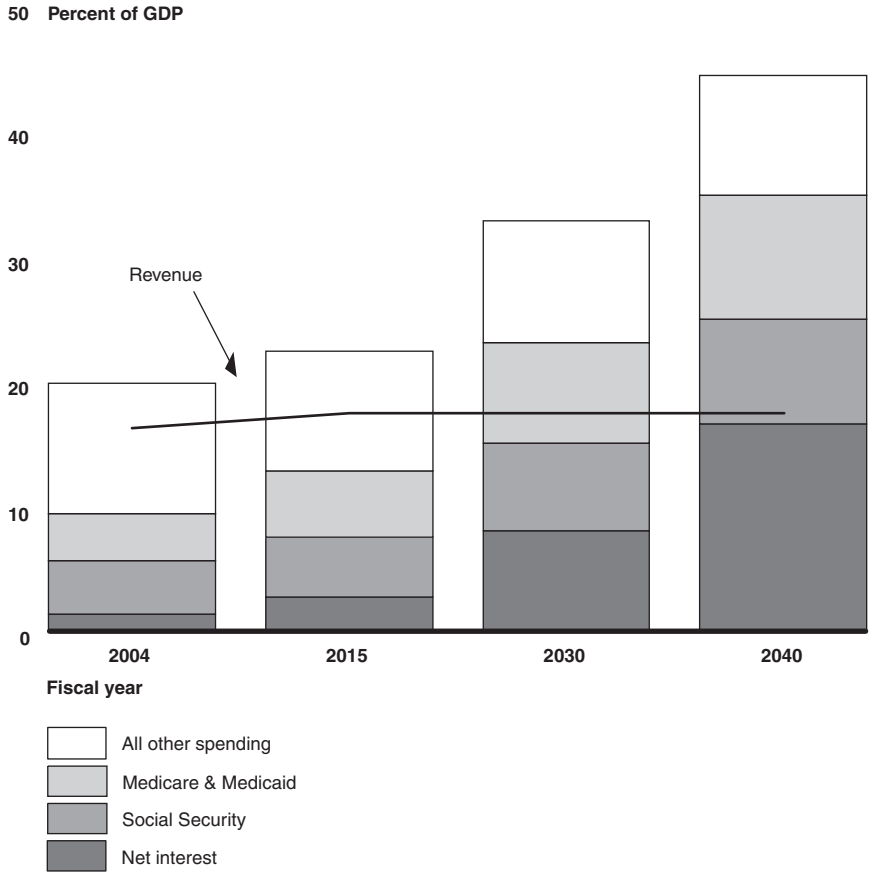
Figure 1: Composition of Spending as a Share of GDP under Baseline Extended



Source: GAO's January 2005 analysis.

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 alternative minimum tax (AMT), and (3) increased revenue from tax-deferred retirement accounts. After 2015, revenue as a share of GDP is held constant.

Figure 2: Composition of Spending as a Share of GDP Assuming Discretionary Spending Grows with GDP after 2005 and All Expiring Tax Provisions Are Extended



Source: GAO's January 2005 analysis.

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.

Addressing the projected fiscal gaps shown here will prompt policymakers to examine the advisability, affordability, and sustainability of existing programs, policies, functions, and activities throughout the entire federal budget—spanning discretionary spending, mandatory spending, including entitlements, and tax policies and programs. Neither slowing the growth of discretionary spending nor allowing tax cuts to expire—nor both options combined—would by themselves eliminate our long-term fiscal imbalance. Additional economic growth is critical and will help to ease the burden, but the projected fiscal gap is so great that it is unrealistic to expect that we will grow our way out of the problem. Clearly, tough choices will be required. Changes in existing budget processes and financial, fiscal, and performance metrics will be necessary to facilitate these choices.

Early action to change existing programs and policies would yield the highest fiscal dividends and provide a longer period for prospective beneficiaries to make adjustments in their own planning. The longer we wait, the more painful and difficult the choices will become. By waiting, an important window is lost during which today's relatively large workforce can increase saving and begin preparing for the necessary changes in fiscal policy, Social Security, health care and other reforms that may very well be part of the solution to this coming fiscal crunch. However, the long-term challenge is fast becoming a short term one as the retirement of the baby boomers' generation will begin as early as 2008 and since overall work force growth has already begun to slow.

Emerging Forces Will Test Existing Policy Frameworks

These challenges would be difficult enough if all we had to do is fund existing commitments. But the nation and the world have and will continue to change in fundamental ways. As a result, a wide range of emerging needs and demands can be expected to compete for a share of the budget pie. Whether it be national security, homeland security, transportation, education, environmental cleanup, or public health, a society with a growing population will generate new claims for federal actions on both the spending and tax sides of the budget. For example, the nation's population itself is projected to grow by about 50 percent over the next 50 years,

generating new needs for public and private resources. Addressing the burdens of existing commitments and providing expanded economic resources are two important strategies to enable future generations to regain the fiscal flexibility to address these needs.

More broadly, major forces are at work that will require the federal government to rethink its entire approach to policy design, priorities, and management to remain relevant to our changing society. In short, government will need to change to become as dynamic as the nation and the changing environment in which it must operate.

GAO's Strategic Plan for Serving the Congress and the Nation (2004-2009), which was prepared in close consultation with the Congress, highlights some of the major forces (See fig. 3.), in addition to the large and growing fiscal imbalances that are at work to reshape our nation and the role of the federal government.

Figure 3: Forces Shaping the United States and Its Place in the World

Large and Growing Long-term Fiscal Imbalance—The U.S. government's long-term financial condition and fiscal outlook present enormous challenges to the nation's ability to respond to forces that shape American society, the United States' place in the world, and the role of the federal government. The short-term deficits are but a prelude to a projected worsening long-term fiscal outlook driven largely by known demographic trends and rising health care costs.

Evolving National and Homeland Security Policies—The dissolution of the Soviet Union in 1991 and the emergence of the more diffuse threats posed by terrorism to the nation's national and homeland security have led to major shifts in strategic threats. While these new security concerns are already prompting changes in defense postures and international relationships, preparedness and responses to these new threats also carry wide ranging and unprecedented implications for domestic policies, programs, and infrastructures.

Increasing Global Interdependence—The rapid increase in the movement of economic and financial goods, people, and information has prompted more widespread realization that the nation is no longer self-contained, either in its problems or their solutions. The growing interdependence of nations, while carrying clear economic and social benefits, also places new challenges on the national agenda and tasks policymakers to recognize the need to work in partnerships across boundaries to achieve vital national goals.

The Changing Economy—The shift to a knowledge-based economy and the adoption of new technology has created the potential for higher productivity but posed new challenges associated with sustaining the investment in human capital and research and development that is so vital to continued growth. While the sustainability of U.S. economic growth has been aided by trade liberalization and increased market competition in key sectors, the sustainability of growth over the longer term will require a reversal of the declining national savings rate that is so vital to fueling capital investment and productivity growth.

Demographic Shifts—An aging and more diverse population will prompt higher spending on federal retirement and health programs. Unless there is strength in the underlying sources of productivity—education, technology and research and development—low labor force growth will lead to slower economic growth and federal revenue growth over the longer term. As labor becomes ever more scarce, a greater share of the work force will be comprised of foreign-born workers, women, and minorities with broad-scale implications for education, training, child care, and immigration policies.

Science and Technology Advances—Rapid changes in science and technology present great opportunities to improve the quality of life and the economy, whether it be finding new sources of energy, curing diseases, or enhancing the nation's information and communications capacities. However, technologies raise their own unique vulnerabilities, risks, and privacy and equity concerns that must be addressed by policymakers.

Quality of Life Trends—Large segments of the population enjoy greater economic prosperity than ever before, and the well being of many Americans has improved dramatically thanks to breakthroughs in health care and improvements in environmental protection. However, these improvements have not been evenly distributed across the nation, as more than 40 million Americans lacking health insurance demonstrate. Prosperity has prompted its own stresses, as population growth and sprawl create demand for new transportation and communication infrastructure.

Diverse Governance Structures and Tools—To deliver on the public's needs and wants, the nation's system will be pressed to adapt its existing policy-making processes and management systems. The governance structures and management processes that emerge will be shaped by the above forces (e.g., increasing interdependency, scientific and technological changes, and security threats), and will depend on having sufficient foresight, a continuous reexamination and updating of priorities, ongoing oversight, and reliable and results-oriented national performance indicators.

Source: GAO.

As the pace of change accelerates in every aspect of American life, these forces work to present government with new and more complex challenges and demands. As the federal role has grown in addressing a wide range of needs, the public has come to expect higher levels of performance and greater responsiveness by public officials and programs.

If government is to effectively address these trends, it cannot accept all of its existing programs, policies, and activities as "givens." Many of our programs were designed decades ago to address earlier challenges, informed by labor markets, security conditions, economic theories, life expectancies, health conditions, organizational structures, technologies, transportation systems, management models, and compensation strategies of prior eras. Outmoded commitments and operations constitute an encumbrance on the future that can erode the capacity of the nation to better align its government with the needs and demands of a changing world and society.

Accordingly, rethinking the base of existing federal spending and tax programs, policies, and activities by reviewing their results and testing their continued relevance and relative priority for a changing society is an important step in this process of fiscal responsibility and national renewal. A periodic reexamination offers the prospect of addressing emerging needs by weeding out programs and policies that are outdated or ineffective. Those programs and policies that remain relevant could be updated and modernized by improving their targeting and efficiency through such actions as redesigning allocation and cost-sharing provisions, consolidating facilities and programs, and streamlining and reengineering operations and processes. The tax policies and programs financing the federal budget can also be reviewed with an eye toward both the overall level of revenues that should be raised as well as the mix of taxes that are used.

We recognize that this will not be a simple or easy process. Such a process reverses the focus of traditional incremental reviews, where disproportionate scrutiny is given to proposals for new programs or activities, not those that are already in the base. Taking a hard look at existing programs and carefully reconsidering their goals and their

financing is a challenging task. Reforming programs and activities leads to winners and losers, notwithstanding demonstrated shortfalls in performance and design. Given prior experience and political tendencies, there is little real "low-hanging fruit" in the federal budget. Moreover, given the wide range of programs and issues covered, the process of rethinking government programs and activities may take a generation to unfold.

We are convinced, however, that reexamining the base offers compelling opportunities to both redress our current and projected fiscal imbalance while better positioning government to meet the new challenges changing expectations of this new century. In this regard, the management and performance reforms enacted by the Congress in the past 15 years have provided new tools to gain insight into the financial, program, and management performance of federal agencies and activities. The information being produced as a result can provide a strong basis to support the review and reprioritization being suggested in this report.

GAO's 21st Century Questions

This report is intended to help the Congress address current fiscal demands as well as future fiscal challenges by providing a series of illustrative questions that could help support a fundamental and broad-based reexamination initiative. Drawing on GAO's institutional knowledge and extensive program evaluation and performance assessment work for the Congress, we present over 200 specific 21st century questions illustrating the types of hard choices our nation needs to face as it reexamines what the federal government does and how it does it.

In developing the 21st century questions, we reflected on the inventory of future forces working to reshape American society, our place in the world, and the various roles and responsibilities of the federal government that were presented in GAO's latest Strategic Plan for Serving the Congress and the Nation (2004-2009). This plan outlines specific trends, as described above, that have no geopolitical boundaries and are expected to challenge what the federal government does and how it does business in the future. These trends, along with GAO's institutional knowledge and issued

work, helped us identify those federal program areas, activities and policy frameworks whose relevance, rationale, and relative priority are likely to be tested in the future. This process was carried out in 12 broad areas, discussed in section 2. We also drew on the collective knowledge and experiences of many others familiar with the various program areas discussed in the next section. We made a concerted effort to solicit input from within the accountability community, including various inspectors general as well as consult with various congressional members, officials, and staff.

The specific questions raised for each area were informed by a set of generic evaluation criteria that are useful to evaluate any government program, policy, function or activity. The criteria are framed as questions in table 1 and are designed to address the legislative basis for the program, its purpose and continued relevance, its effectiveness in achieving goals and outcomes, its efficiency and targeting, its affordability, its sustainability, and its management. We used these criteria to generate specific 21st century questions about those programs and priorities already identified. The resultant 21st century questions illustrate the kinds of issues that a reexamination and review initiative needs to address.

Table 1: Illustrative Generic Reexamination Criteria

Relevance of purpose and the federal role	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?
	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 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?
	Is the current mission fully consistent with the initial or updated statutory mission (e.g., no significant mission creep or morphing)? Is the program, policy, function, or activity a direct result of specific legislation?
Measuring success	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?
Targeting benefits	Is it well targeted to those with the greatest needs and the least capacity to meet those needs?
Affordability and cost effectiveness	Is it affordable and financially sustainable over the longer term, given known cost trends, risks, 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?
Best practices	If it fares well after considering all of these questions, is the responsible entity employing prevailing best practices to discharge its responsibilities and achieve 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)?

Source: GAO.

When taken together, these questions can usefully illustrate the breadth of issues that can be addressed through a systematic reexamination process. Importantly, the questions cover the three major areas—discretionary spending, mandatory spending including entitlements, and tax policies.

Section 2: Twelve Reexamination Areas

This section provides short narratives describing the emerging forces prompting the need to reexamine the goals, designs, and strategies underlying the portfolio of programs in each of 12 broad reexamination areas. As shown in figure 4, the reexamination areas correspond with major federal missions and governmentwide processes.

Figure 4: Twelve Reexamination Areas

Mission Areas	
Defense	Natural Resources, Energy & Environment
Education & Employment	Retirement & Disability
Financial Regulation & Housing	Science & Technology
Health Care	Transportation
Homeland Security	
International Affairs	
Crosscutting Areas	
Governance	Tax System

Source: GAO.

For each area, a summary of challenges and illustrative 21st century reexamination questions demonstrate the type of review needed. Questions are neither exhaustive nor representative of the highest priorities. Nor are they intended to prescribe solutions or constitute GAO findings regarding the program areas they discuss. They do, however, provide examples of the types of questions—based on current trends, future fiscal realities, and GAO's work and expertise—that a fundamental reexamination of the base of federal government policies, programs, functions, and activities could address for each of the 12 areas. The questions were selected for their fiscal significance, their balance between a strategic and operational level, and their relationship to GAO's strategic plan for serving the Congress.

National Defense Challenges for the 21st Century

In the past 15 years, the world has experienced dramatic changes in the overall security environment, with the focus shifting from conventional threats posed during the Cold War era to more unconventional and asymmetric threats evidenced in the events of September 11, 2001. To respond to these events and the ensuing global war on terrorism, the Department of Defense (DOD) has been given a significant infusion of funds, with an annual appropriation totaling over $400 billion for fiscal year 2005 and supplemental funding for homeland defense and overseas military operations approximating $190 billion over the past 3 fiscal years. In addition to providing additional resources to enhance war-fighting capabilities, the Congress has also taken steps to fund enhanced compensation and benefit programs for active duty and reserve personnel.

As DOD seeks to meet the demands of the new security environment, it continues to bear the costs of the past by implicitly maintaining or continuing to pursue many programs and practices from the Cold War era. In this context, the magnitude of funding and potential for current investments and operations to turn into long-term financial commitments are prompting real questions about the affordability and sustainability of the rate of growth in defense spending. For example, in September 2004, the Congressional Budget Office reported that carrying out current defense plans would require annual funding to be sustained over the longer term at higher real (inflation-adjusted) levels than have occurred since 1980, excluding supplemental appropriations. Many factors should be considered, including reassessing the base and rate of growth in defense and related spending. Failure to do so will result in significant waste today and opportunity costs over time. Moreover, the recent 9/11 Commission Report suggests that changes are needed across the government to strengthen national security institutions and move beyond the legacy of the Cold War, including reforming the nation's intelligence organizations and capabilities. As such, meeting the nation's defense needs in the 21st century may prompt decision makers to reexamine fundamental aspects of the nation's national security programs such as how DOD plans and budgets, organizes its forces, manages the total force, acquires new capabilities, positions our forces, and considers alternatives to past approaches.

In addition to maintaining readiness and sustaining the current force, DOD is faced with identifying capabilities, including critical technologies, needed to meet the demands of the new security environment, as well as determining the best way to provide those capabilities and retain the U.S. military's technological superiority. Striking an affordable balance between current and future needs will be an ongoing challenge, particularly with the federal government's current and projected fiscal imbalance. The upcoming quadrennial defense review will provide an opportunity for DOD to move beyond the legacy of the past, assess the capabilities required to meet current, emerging and future threats, establish near-term and long-term priorities, and adopt realistic funding plans.

To adapt to the new security environment, DOD is currently embarked on an effort to transform its war-fighting capabilities and how it does business to support the war fighter. DOD's civilian and military leaders appear committed to reform; however, the department faces significant challenges in accomplishing its transformation goals.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

To successfully transform itself, DOD must overcome cultural resistance to change and the inertia of various organizations, policies, and practices that became well rooted in the Cold War era. Longstanding organizational and budgetary problems need to be addressed, such as the existence of stove-piped or siloed organizations, the involvement of many layers and players involved in decision-making, the allocation of budget allocations on a proportional rather than strategic basis among the military services, and the use of traditional approaches to basing forces and replacing or enhancing capabilities (typically on a platform by platform rather than a joint basis). DOD's current approach to planning and budgeting often results in a mismatch between programs and budgets. And it does not always fully consider long-term resource implications and the opportunity cost of selecting one alternative over another.

▶ *How should the historical allocation of resources across services and programs be changed to reflect the results of a forward-looking comprehensive threat/risk assessment as part of DOD's capabilities-based approach to determining defense needs?*

▶ *Can DOD afford to invest in transformational systems such as the Future Combat System and national missile defense at the same time it continues to pursue large investments in legacy systems such as the FA-22 and new systems like the Joint Strike Fighter, especially if cost growth and schedule delays continue at historical rates?*

▶ *Are sufficient investments being made in capabilities that cross service lines, such as joint communications and interoperable systems? For example, is the Global Information Grid well enough defined and understood to enable sound investments to be made in its key components such as the Transformational Satellite?*

▶ *Given the global availability of rapidly advancing technology, does DOD need to reconsider its approach for identifying critical technologies and protecting those technologies from being exploited in order to maintain its military superiority?*

The global war on terrorism has required the military forces to operate differently from the ways it was organized, equipped, staffed and deployed to operate under post-Cold War planning assumptions based on regional threats. Current operations have required significant numbers of ready forces, both active and reserve, to be mobilized for long periods and created demand for certain skills, such as military police, that exceeds the available supply. While DOD has taken steps to meet short term operational needs, it has not yet determined how it will meet the longer term challenges of reorganizing its forces and identifying the capabilities it will need to protect the country from current, emerging, and future conventional and unconventional security threats.

▶ *Do the role, size, and structure of forces and capabilities comprising the strategic triad need to be adjusted to meet the challenges of providing strategic deterrence in the new security and fiscal environment?*

▶ *Are the active and reserve components appropriately sized, structured, and used to meet the current and future national security demands? Is the current business model sustainable for the reserve component?*

▶ *What is the appropriate role for contractors, especially in forward deployment and conflict areas, to maximize the capabilities of military and contract personnel and to ensure effective integration of contractors into military operations and support cost-effectively?*

▶ *Does DOD's plan for realigning forces at overseas locations and redeploying some forces from overseas to stateside locations provide a significantly improved capability to respond to global threats in the new security environment considering diplomatic, operational, and cost considerations?*

DOD's military personnel outlays are large and growing, increasing from about $76 billion to an estimated $109 billion between fiscal years 2000 and 2005. In fact, personnel costs comprise the second largest component of DOD's total fiscal year 2005 budget. The growth in military personnel costs has been fueled in part by increases in basic pay, housing allowances, recruitment and retention bonuses, incentive pays and allowances, and other special pays. Furthermore, DOD's costs to provide benefits, such as health care, have continued to spiral upward. Expanded health care to reservists and their families and retirees has been the primary cost driver in growing benefits costs. Also, a large portion of DOD's compensation-related costs is in the form of benefits and deferred compensations. In some cases, such benefits exceeded those offered by private sector organizations. As the total and per capita cost to DOD for military pay and benefits grows, questions arise as to whether DOD has the right pay and compensation strategies to cost-effectively sustain the total force in the future. Regarding its civilian workforce, DOD is preparing to implement a congressionally authorized personnel system, which will change the way civilian employees are hired, assigned, compensated, promoted, disciplined, and, if necessary, fired.

▶ *Given the growing encumbrance of pay and benefit costs, especially health care, within DOD's budget, how might DOD's recruitment, retention, and compensation strategies (including benefit programs) be reexamined and revised*

to ensure that DOD maintains a total military and civilian workforce with the mix of skills needed to execute the national security strategy while using resources in a more targeted, evidence-based, and cost-effective manner?

▶ *Is DOD pursuing the design and implementation of its new national security personnel system initiatives in a manner that maximizes the chance of success?*

Given its size and mission, DOD is one of the largest and most complex organizations to manage in the world. While the unparalleled combat effectiveness of U.S. forces has been well evidenced in the Persian Gulf and elsewhere, DOD has not been effective in managing its ongoing business operations. Complicating DOD's efforts are numerous systems problems and a range of other longstanding weaknesses in the key business areas of strategic planning and budgeting, human capital management, infrastructure, supply chain management, financial management, information technology, weapons systems acquisition, and contracting. For example, 8 individual items on GAO's list of high-risk government operations and several of the governmentwide high-risk areas apply to key DOD business operations. These problems that continue to result in substantial waste and inefficiency adversely affect mission performance and result in a lack of transparency and accountability.

▶ *Does DOD need to create a senior management position responsible and accountable for taking a strategic, integrated, and sustained approach to managing the day-to-day business operations of the department, including ongoing efforts to transform DOD's business operations and address the many related and longstanding high-risk areas? Should specific qualifications requirements and periods of tenure or terms be established for selected DOD positions related to key business operations?*

▶ *Are current organizations aligned and empowered to meet the demands of the new security environment as efficiently as possible? What kinds of economies of scale and improvements in delivery of support services would result from combining, realigning, or otherwise changing selected support functions (e.g., combat support, training, logistics, procurement, infrastructure, or health care delivery)?*

Education and Employment Challenges for the 21st Century

The shift to a global economy and changes in technology, the nature of work, and workforce demographics are challenging customary federal approaches to education and employment. The global economy and advances in technology enable work to be shifted to other countries or render some jobs obsolete. If we are to compete effectively in a growing, knowledge-based economy, our educational system must equip children with appropriate skills to meet high standards and provide means for adults to continue to learn new skills and enhance their existing abilities. This will require ensuring that diverse populations have access to postsecondary, vocational, and adult education. As an increasingly volatile job market creates and eliminates jobs, federal programs that train new workers or support workers who lose their jobs must also be capable of responding to sudden changes in the economy. Federal efforts to protect workers must account for changes in the nature of work: membership in organized labor has declined, traditional work arrangements are giving way to alternatives such as temporary employment and teleworking, and lifelong service with a single employer is becoming much less common.

Changes in workforce demographics pose additional challenges. The U.S. labor force has more than doubled in the past 50 years but is now growing at a much slower rate. Women, who helped fuel past workforce growth, are expected to join the workforce at a constant rate, and baby boomers are likely to begin retiring in large numbers in less than 5 years. As a result, those leaving jobs are expected to outnumber those seeking jobs in certain industries. The tighter job market will challenge federal efforts to ensure that employers have enough workers with the right skills to help promote economic growth. This trend also underscores the importance of addressing current pension, disability, health, and immigration policies. With regard to the latter, it will be important to consider whether the number of visas allowed for both employment and education may affect long-term competitiveness, and our ability to build bridges with other nations, their people, and their cultures while addressing our national and homeland security needs.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

With rapid advances in technology, increases in global trade, and the availability of highly educated foreign workers, U.S. workers increasingly need advanced skills to remain competitive. Determining what skills workers need and providing the right opportunities for acquiring those skills will depend, in part, on building partnerships among the multiple federal agencies and other key nonfederal players that support employment training, industries, and employers. In developing these partnerships, avoiding redundancy and ensuring sufficient numbers of workers with the right skills will be crucial. This challenge may become more difficult to address if labor markets tighten over the next 20 years as the baby boom generation retires, labor force participation rates for women remain flat, and immigrants face potential difficulties in obtaining visas given heightened security concerns. These shortages will have implications for the broader economy and budget as well as the Department of Labor's efforts to ensure that employers have sufficient numbers of workers with the right skills.

▶ *Should federally funded training programs operated across multiple federal agencies—9 federal agencies administer 44 such programs—be better integrated and restructured in order to increase their cost effectiveness?*

▶ *How can existing policies and programs be reformed to ensure that employers have sufficient numbers of workers with the right skills (for example, modifying pension policies and regulations so that workers can work part-time and still receive a pension)?*

Many of the federal government's higher education policy tools—especially its grant and loan programs—were designed decades ago to meet the needs of traditional students in traditional academic settings. However, they may not be well suited to an increasingly diverse population that includes working adults, single parents, students with disabilities, and increasing numbers of minorities. In addition, these tools may not be structured to take advantage of the potential for cost savings or widening access provided by distance education technologies. The adoption of tax policy tools in the last decade has resulted in some of these policies working at cross-purposes to traditional grant and loan programs. For example, under the Higher Education Act, students seeking federal grants

and loans are penalized for having saved funds to pay for their education, while the Internal Revenue Code has encouraged saving by exempting individuals from federal income taxation on interest income used to pay for postsecondary education.

▶ *Is there a need for better coordination—or integration—among higher education policy tools (such as grants, loans, and tax preferences) or periodic examination of those policy tools that are not routinely subject to periodic reauthorization or appropriation, such as the Hope and Lifetime Learning tax credits, for which tax filers claimed nearly $5 billion in 2002?*

Higher education is increasingly global in nature as students study outside their country of origin with greater frequency and universities have become multinational institutions. While the United States has long been the global leader in higher education—and the most desired destination of foreign students seeking higher education—recent graduate enrollments have fallen, and institutions in other countries have captured an increasing share of the international student population. The adoption of tighter security requirements has widely been argued as contributing to the decreased enrollments of foreign students in the United States.

▶ *How can the United States balance immigration policies—such as worker and student visa programs—to address employers' need for workers with particular skills, particularly math and science, the nation's need to maintain global leadership in areas such as science and higher education, and the nation's homeland security requirements?*

The large achievement gap between students of different backgrounds has persisted for four decades despite a significant federal investment in educating disadvantaged students during that time. Many disadvantaged children start school with fewer skills than their more advantaged peers. Research shows that early intervention helps children succeed in school and is particularly effective for the most disadvantaged students. It is less clear whether current levels of coordination among the myriad federal and state programs efficiently produce desired results for particular subgroups of children. For example, systematic information is not available on the total number of preschool children receiving

subsidies through various federal programs and/or participating in state-funded preschool. This prevents a comprehensive assessment of how fully the combination of federal and state programs addresses preschoolers' needs. Recent legislative initiatives, such as the No Child Left Behind Act with its emphasis on accountability, may help change this trend and could be aided by retargeting of federal investments. The Elementary and Secondary Education Act was passed in 1965 to provide assistance to states in educating disadvantaged students through Title I, the largest federal program for elementary and secondary education. However, since about 90 percent of school districts receive these Title I funds to improve the education of disadvantaged students, including a growing number with limited English proficiency, an opportunity exists to improve targeting of funds to school districts having the greatest number and percentage of disadvantaged children.

▶ *Is there a need to reexamine the federal investment for early childhood programs (e.g., funds provided under the Child Care and Development Block grant and certain expenditures under Title I) to better coordinate them and support state and local efforts to prepare disadvantaged children to succeed in school?*

▶ *In light of the increasing diversity of the nation's school age population, should the Department of Education reexamine whether there are opportunities to better target limited resources such as Title I funds so that the needs of disadvantaged students including those with limited English proficiency are better addressed?*

Federal agencies that help employers provide safe, healthy, and productive workplaces, such as the Occupational Safety and Health Agency (OSHA), will have to adapt to both changes in workforce demographics—the rising proportion of older workers in general and immigrant workers in some occupations—and the rise of nontraditional workplace arrangements, such as increased use of independent contractors not covered by most worker protection laws.

▶ *Do recent changes in the labor force makeup and work arrangements—such as the growing use of telework and the increasing number of independent contractors—warrant a reconsideration of the Department of Labor's focus, such as through OSHA, on traditional workplaces as part of its efforts to ensure worker safety?*

Financial Regulation and Housing Challenges for the 21st Century

Increased global interdependency and rapid technological advancement in the financial services industry pose significant challenges to U.S. regulatory institutions charged with ensuring well-functioning markets and to government agencies charged with managing loan guarantee or mortgage insurance programs that, to some extent, compete with the private sector. Globalization has become increasingly prevalent as technology allows money to be moved around the world literally at the push of a button, challenging regulators whose authority is defined by national borders. Households can invest in companies worldwide and can be defrauded or have their identities stolen from almost anywhere. The financial services sector has been and continues to be one of the most technologically sophisticated, whether in adapting technology to new uses or providing incentives to develop state-of-the-art products to solve a range of risk management problems. Lastly, immigration patterns, demographic trends, and a range of quality-of-life issues are important factors pushing up housing prices and related rents in certain regions and local real estate markets, which quickly outpace wage growth and put increasing strain on housing affordability in those areas.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

The present federal financial regulatory structure evolved largely as a result of periodic ad hoc responses to crises such as financial panics. In the last few decades, however, the financial services industry, especially as represented by the largest firms, has evolved, becoming more global, more concentrated, complex, and consolidated across sectors, and increasingly converging in terms of product offerings. Multiple specialized regulators bring critical skills to bear in their areas of expertise but have difficulty seeing the total risk exposure at large conglomerate firms or identifying and preemptively responding to risks that cross industry lines.

▶ *Is it time to modernize our financial regulatory system by consolidating various federal regulatory agencies to promote a more coherent and integrated structure, specify goals more clearly, and provide sufficient resources along with the flexibility and incentives to prospectively target resources to risk? To what*

extent can specialized or consolidated regulators effectively address companywide and systemic risks that arise from the potential failure of large, diversified financial firms?

The need to improve consumers' financial literacy—their ability to make informed judgments and effective decisions about the management of money and credit—has become increasingly important. Consumers are faced with an increasingly complicated array of options for managing their personal finances and selecting investments and credit products. In addition, available data show that many consumers are not adequately saving for their retirement, despite concerns about the adequacy of Social Security, private pensions, and retiree health benefits. At the same time, unsecured consumer debt (especially credit card debt) has grown rapidly in the past two decades, bankruptcy filings have increased substantially, and predatory lending has become a growing concern.

▶ *What role should the federal government take in improving financial literacy among consumers, and what are the most effective strategies for doing so? Where are there gaps or overlaps in federal financial literacy programs? How many agencies should be involved? Can disclosures be improved and what are the limitations of improved disclosures in protecting consumers?*

Government-sponsored enterprises (GSE) were created throughout the 20th century to address perceived market imperfections in financing housing, agriculture, and higher education. With the federal benefits they have been provided, the GSEs have linked local lending markets and national capital markets. Two of the housing GSEs, Fannie Mae and Freddie Mac, have played a critical role in establishing a nationwide secondary mortgage market and increasing efficiency through greater standardization of mortgage products. However, with rapid developments spurred by technical change, the private marketplace has evolved dramatically. While one GSE, Sallie Mae, has undergone privatization, the other GSEs have used their special federally provided status and related benefits to expand into new activities. These entities are also taking on more risk and using more sophisticated and less transparent risk management strategies. The public benefits and potential risks to

taxpayers from such expansion, as well as from the continued existence of the GSEs, are a subject of great debate.

▶ *Is the current federal GSE regulatory framework appropriately structured, and do the regulators have the necessary authorities to address the risks of the GSEs? For example, should the Office of Federal Housing Enterprise Oversight be combined with the other housing GSE regulators into one comprehensive housing GSE regulator? What is the GSE track record in achieving homeownership goals, especially for low-income and protected groups? Do the GSEs continue to serve an important public policy purpose? Should their mission focus be restrained to limit expansion into new activities, or adjusted in any way? Should they be privatized?*

New information-based technologies are transforming the credit markets at a rapid pace. Private sector financial institutions have been using credit scoring and other tools to make finer distinctions among potential risks, allowing them to measure and price risk more effectively. Government lenders, loan guarantors, and insurers have been slower to adopt similar tools for their decision making. While federal credit programs can adopt some of the new technologies to better measure risk, lags in such adoption increase the prospect of adverse selection—if the private sector and GSEs take a larger share of lower risk customers, government programs will be left to take on the less well understood and potentially riskier remainder.

▶ *Do federal lending programs need to be reexamined to address the increased risks and potential costs to the government? For example, should the Federal Housing Administration (FHA) continue to fully guarantee mortgages or move to a partial guarantee? If the cost of credit is linked more closely with risk, what role might the federal government play in reducing the cost of borrowing for those borrowers with little or no credit history? For example, should FHA focus more of its activities on those with little or no credit history?*

Homeownership continues to be one of the primary means for many families to accumulate wealth in this country, and is also thought to contribute to stable and vital communities. While the overall homeownership rate is at a historic high, in certain subpopulations the rate lags behind. Numerous tools have been applied to increase home ownership in the United States. Some of

these tools are broadly based, such as the tax deduction for home mortgage interest and GSEs and their effect on mortgage interest rates. Both of these attract capital away from other sectors of the economy and toward the housing sector. Other tools are more narrowly focused on particular areas or populations, such as the FHA mortgage insurance program and other loan programs administered by the U.S. Department of Housing and Urban Development (HUD) and USDA's Rural Housing Service (RHS). In addition, lenders and others have developed mortgage products that permit households to become homeowners sooner than would be the case otherwise.

▶ *To what extent do the tools and incentives increase spending on housing rather than promote affordable housing? Can the tools and incentives provided to homeownership be better targeted toward increasing home ownership among selected groups with less capacity to access credit markets? For example, should the cap on the mortgage interest deduction be more precisely targeted?*

▶ *What are the potential risks of recent homeownership initiatives for borrowers, financial institutions, and taxpayers? Are the recent increases in the home ownership rate sustainable; i.e., how will families and financial markets cope with increases in mortgage interest rates and slower growth in home equity?*

A number of programs provided by HUD, RHS, and other agencies, as well as other tools and incentives, are designed to provide decent rental housing affordable to target populations. Over the years, the emphasis of these incentives has shifted from the supply side (production subsidies) to the demand side (vouchers). In recent years, most construction of federally financed affordable rental housing has resulted from tax provisions. In addition, a number of federally assisted units are eligible to leave some older subsidy programs in the next two decades. Finally, the costs of HUD's housing choice voucher program continue to grow, driven in part by the difference between the eligible population's income growth and the cost of privately owned rental housing; this gap is increasing rapidly in certain markets. HUD and its public housing agency partners have struggled to balance the competing demands of maintaining assistance for a specified number of households while controlling the increasing costs of doing so.

▶ *What are the advantages and disadvantages of demand-based subsidies (vouchers) versus supply-based incentives (production or financing subsidies) for providing affordable housing to target populations? To what extent are these advantages and disadvantages dependent on local housing market conditions? To the extent that market forces drive the housing voucher's program cost, how might the Congress best reconcile the competing demands of continued assistance to a targeted number of households while addressing the long-term budget implications?*

Health Care Challenges for the 21st Century

Between 1992 and 2002, overall health care spending rose from $827 billion to about $1.6 trillion; it is projected to nearly double to $3.1 trillion in the following decade. This price tag results, in part, from advances in expensive medical technology, including new drug therapies, and the increased use of high-cost services and procedures. Many policymakers, industry experts, and medical practitioners contend that the U.S. health care system—in both the public and private sectors—is in crisis. In the public sector, long-term simulations of the federal budget show a large and growing structural deficit resulting, in large part, from known demographic trends and rising health care costs. Since Medicare spending is driven by both these factors, its burden on the budget and the economy will balloon—tripling by 2035 and quintupling by 2075. One of the fastest-growing segments of health care in both the public and private sectors is prescription drugs. In 2004 the Medicare Trustees estimated that over a 75-year period the federal share of the new Medicare benefit would be $8.1 trillion in current dollar terms. In the private sector, employers and other private purchasers of health care services find that the soaring cost of health insurance premiums poses a threat to their competitive position in an increasingly global market, often contributing to company decisions to outsource American jobs overseas, to hire part-time rather than full-time workers, and to minimize cash wage increases and pension costs.

Despite the significant share of the economy consumed by health care, U.S. health outcomes continue to lag behind other industrialized nations. The United States now spends over 15 percent of its gross domestic product on health care—far more than other major industrialized nations. Yet relative to these nations, the United States performs below par in such measures as rates of infant mortality, life expectancy, and premature and preventable deaths. Moreover, evidence suggests that the American people are not getting the best value for their health care dollars. Studies show that quality is uneven across the nation, with a large share of patients not receiving clinically proven, effective treatments. At the same time, access to basic health care coverage remains an elusive goal for nearly 45 million Americans without insurance, with a growing percentage of workers losing their employer-based

coverage. Many more millions of Americans are underinsured or have lost some of the benefits their health plans previously afforded.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

Defining differences between needs, wants, affordability, and sustainability is fundamental to rethinking the design of our current health care system. Americans with good health insurance have access to an array of advanced technology procedures at world-class health facilities, but clinical studies suggest that not all of this care is desirable or needed. Rising health costs are compelling both public and private payers to examine whether these procedures can continue to be financed without better accounting for their clinical effectiveness. Additional health care spending over time will draw resources away from other economic sectors and could have adverse economic implications for all levels of governments, individuals, and other private purchasers of health care.

▶ *How can we perform a systematic reexamination of our current health care system? For example, could public and private entities work jointly to establish formal reexamination processes that would (1) define and update as needed a minimum core of essential health care services, (2) ensure that all Americans have access to the defined minimum core services, (3) allocate responsibility for financing these services among such entities as government, employers, and individuals, and (4) provide the opportunity for individuals to obtain additional services at their discretion and cost?*

The impact that federal health care outlays have on the federal budget cannot be overstated. Medicare and Medicaid—entitlement programs for which federal spending is mandatory—are consuming increasing shares of the federal budget and shrinking the government's flexibility to pay for other federal obligations, such as national and homeland security, environmental cleanup, and disaster assistance. Today, Medicare and Medicaid's combined share of the federal budget—at 20 percent—has more than doubled in the last 2 decades. Moveover, long-term care for chronic illness will be a growing challenge as the aged population continues to grow. In addition, health care expenditures for the Departments of Defense

(DOD) and Veterans Affairs (VA) are increasing. DOD's health care spending has gone from about $12 billion in 1990 to about $26 billion in 2003—in part, to meet additional demand resulting from program eligibility expansions for military retirees, reservists, and the dependents of those 2 groups and for the increased needs of active duty personnel involved in conflicts in Iraq, Bosnia, and Afghanistan. VA's expenditures have also grown—from about $12 billion in 1990 to about $24 billion in 2003—as an increasing number of veterans look to the VA to supply their health care needs.

▶ *How can we make our current Medicare and Medicaid programs sustainable? For example, should the eligibility requirements (e.g., age, income requirements) for these programs be modified?*

▶ *How can the federal government best leverage its purchasing power for health care products and services?*

▶ *What options are there for rethinking the federal, state, and private insurance roles in financing long-term care?*

▶ *How can the benefits, eligibility, and health delivery systems of VA and DOD be optimally structured to ensure quality and efficiency? For example, should changes in eligibility and the benefit structure of VA and the military health system be considered?*

▶ *With billions of federal dollars going to DOD and VA for health care, what options are available to reduce spending growth through increased collaboration in, and integration of, health care delivery between those two agencies?*

In the past several decades, the responsibility for financing health care has shifted away from the individual patient. In 1962, nearly half—46 percent—of health care spending was financed by individuals. The rest was financed by a combination of private health insurance and public programs. By 2002, the amount of health care spending financed by individuals' out-of-pocket spending at the point of service was estimated to have dropped to 14 percent. Tax preferences for insured individuals and their employers have also shifted some of the financial burden for private

health care to all taxpayers. Tax policies permit the value of employees' health insurance premiums to be excluded from the calculation of their taxable earnings and exclude the value of the premium from the employers' calculation of payroll taxes for both themselves and employees. Health savings accounts and other consumer-directed plans, which shift more of health financing to the individual, also have tax preferences. These tax exclusions represent a significant source of forgone federal revenue and work at cross-purposes to the goal of moderating health care spending.

▶ *How can health care tax incentives be designed to encourage employers and employees to better control health care cost? For example, should tax preferences for health care be designed to cap the health insurance premium amount that can be excluded from an individual's taxable income?*

▶ *What reforms will encourage the private health insurance market to sufficiently pool risk and offer alternative levels of affordable coverage to ensure that all Americans have access to essential health care coverage? For example, are there alternatives to employer-based coverage through professional organizations, trade associations, or other entities?*

The variation by geographic region in Americans' use of health care services suggests, in part, quality and efficiency problems. Studies of Medicare patients in different geographic areas have found that despite receiving a greater volume of care, patients in higher use areas did not have better health outcomes or experience greater satisfaction with care than those living in lower use areas. Public and private payers are experimenting with payment reforms designed to foster the delivery of care that is clinically proven to be effective. Ideally, identifying and rewarding efficient providers and encouraging inefficient providers to emulate best practices will result in better value for the dollars spent on care. However, implementing performance-based payment reforms, among other strategies, on a systemwide basis, will depend on system components that are not currently in place nationwide—such as compatible information systems to facilitate the production and dissemination of medical outcome data, safeguards to insure the privacy of electronic medical records, improved transparency through increased measurement and reporting efforts, and

incentives to encourage adoption of evidence-based practices. These same system components would be required to develop medical practice standards, which could serve as the underpinning for effective medical malpractice reform. Policymakers would need to consider the extent to which federal leadership could foster these system components.

▶ *How can technology be leveraged to reduce costs and enhance quality while protecting patient privacy?*

▶ *How can industry standards for acceptable care be established and payment reforms be designed to bring about reductions in unwarranted medical practice variation? For example, what can or should the federal government do to promote uniform standards of practice for selected procedures and illnesses?*

▶ *How can a medical information infrastructure be fostered, complete with privacy safeguards, that will help reduce the occurrence of medical errors and malpractice litigation and will furnish health outcomes data to better inform consumer choice?*

▶ *What reforms will help control health care costs associated with medical liability without undercutting provider accountability?*

The attacks of September 11, 2001, and subsequent anthrax incidents—as well as disease outbreaks, such as the West Nile virus and SARS—have elevated to priority status concerns about the quality and availability of the nation's public health resources at the federal, state, and local levels. In recent years, it has been apparent that, despite improvements, the nation's public health infrastructure remains too fragmented and uncoordinated and lacks the capacity to effectively manage a large epidemic or bioterrorist attack. Since fiscal year 2002, substantial federal funding has gone to state and local governments to improve disease surveillance systems, laboratory capacity, communication systems, and workforces. Federal funds directed at basic biomedical research to improve treatment and vaccinations for infectious diseases caused by biological agents have also been substantial. In an era of growing demand and shrinking resources, however, it may be prudent to determine how best to target the nation's public health dollars.

▶ *What are the most effective strategies for tracking emerging infectious diseases and targeting resources to prepare for treating these diseases?*

▶ *How can our international agreements encourage the equitable sharing of financial responsibility for developing pharmaceuticals and other medical technologies and eradicating AIDS and other worldwide disease outbreaks? For example, what can be done to facilitate more international burden-sharing for prescription drug research and development currently financed through public expenditures and higher U.S. prices?*

Global interdependence and efficient transportation systems have heightened U.S. vulnerability to a broad range of infectious diseases, such as SARS and avian influenza. Moreover, HIV/AIDS, tuberculosis, and malaria are increasingly viewed as a threat to economic growth and political stability in many nations. The number of people with HIV/AIDS will grow significantly by 2010, driven by the spread of the disease in five populous and strategically significant countries—China, India, Nigeria, Russia, and Ethiopia. To combat the spread of these diseases, the United States pursues multiple approaches, including partnerships with international organizations, such as taking the lead in support of the World Health Organization (WHO). At the same time, the United States also supports numerous bilateral programs to strengthen other countries' health care systems. The increasingly global spread of infectious diseases presents a challenge to these approaches and prompts the need to reexamine the balance between and possible integration of these approaches.

▶ *Should the United States reexamine its central role in supporting WHO in global efforts to control the spread of emerging diseases such as SARS and encourage other nations to provide more support to WHO with their personnel and resources? Do U.S. commitments to infectious disease interventions abroad, such as those for HIV/AIDS, need to be reexamined to better ensure human well-being, economic growth, and political stability in many nations? For example, can better coordination or integration of current multilateral and bilateral approaches to combating disease achieve greater effectiveness and efficiency?*

Homeland Security Challenges for the 21st Century

The terrorist attacks of September 11, 2001, evoked with stunning clarity the face and intent of enemies very different from those the nation has faced before—terrorists such as al Qaeda, willing and able to attack us in our territory using tactics designed to take advantage of our relatively open society and individual freedoms. In the 3 years since the attacks, the nation has begun confronting the enemy abroad and domestically at the federal, state, local, and private levels. For example, the Congress enacted legislation creating the Department of Homeland Security (DHS) and strengthening other security measures in law enforcement and border and transportation security. Military action destroyed many terrorist sanctuaries and support networks. The new Northern Command provided additional resources and authority for homeland defense. Law enforcement disrupted terrorist cells and worked with international authorities to identify and disrupt other terrorist threats and target terrorist financing. National strategies, such as the National Strategy for Homeland Security, set initiatives in many homeland security areas. A series of homeland security presidential decision directives provided further guidance and objectives in areas such as critical infrastructure protection, national warning systems, and national preparedness goals and metrics.

However, the threat of terrorism will persist well into the 21st century. Terrorists are dispersed in loosely organized, self-financed, international networks of terrorists, some of which are cross-national. Domestic terrorist groups remain a security threat, though currently to a much lesser extent than the international terrorist movement. We must fundamentally reexamine our approaches to terrorism and homeland security—the nature of the terrorist threat, its long-term impact, and the impact of our strategies. While most believe we are safer than we were on the day of the September 11 attacks, we still are not safe.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

Defining an acceptable, achievable (within constrained budgets) level of risk is an imperative to address current and future threats. Many have pointed out, as did the Gilmore and 9/11 Commissions,

that the nation will never be completely safe and total security is an unachievable goal. Risks have been exposed in many aspects of normal life, with perhaps many of the greatest dangers posed in areas that Americans have simply taken for granted, such as air and water supplies, food production chains, information systems, airports and train stations, ports, borders, and shopping malls. However, we cannot afford to protect everything against all threats—choices must be made about protection priorities given the risk and how to best allocate available resources. While risk-based allocation decision-making is still evolving, we must take a more systematic, reasonable approach to allocating resources. Adoption of management system standards, such as the National Fire Protection Association 1600 standard for national preparedness, can also aid in assessing risk and defining key homeland security activities.

▶ *What is an acceptable level of risk to guide homeland security strategies and investments, particularly federal funding? For example, how should risk be managed in making sound threat, risk, and criticality assessments, developing countermeasure options, and implementing those options considered the most effective and the most efficient? What criteria should be used to target federal funding for homeland security in order to maximize results and mitigate risk within available resource levels?*

Confronting asymmetric threats requires new international and domestic strategies and related tactics on our part. International and domestic terrorists will not be defeated by conventional force projection and weapons systems, law enforcement, or infrastructure protection alone. Instead, our tactics will hinge more on intelligence, diplomatic efforts, and domestic partnerships across many actors. Understanding the underlying causes of terrorism—the isolation and alienation that feeds violence—and focusing on mitigating those causes is likely to be the only way to truly diminish the levels of terrorism globally and domestically. For example, the international terrorist movement draws on a hatred of what is seen as the corrupting influences of western culture and values. Instigators of terrorism can find recruits for violent actions among those who see themselves with little or nothing to lose. Thus, efforts to confront ideological differences and offer hope for the

future are essential to the long-term effectiveness of combating terrorism. Public diplomacy will be challenged to target and better reach audiences in areas where new threats are emerging.

▶ *What new international and domestic strategies and related tactics will effectively confront the asymmetric tactics we now face and, for the longer term, address the root causes of terrorism? For example, how can we best anticipate, and thus counter, asymmetric threats such as suicide attacks, biological and chemical terrorism, and cyber attacks? What approaches will address the root causes of terrorism, whether from domestic or international groups? For example, should the current U.S. approach to overseas broadcasting be realigned to target and better reach audiences in areas where new threats are?*

Establishing effective federal, state, and local government; private sector; nongovernmental; and nation-state partnerships is crucial to addressing risk across the nation. The Constitution requires the federal government to "provide for the common defense" and to "repel invasions." Many would interpret those requirements to justify homeland security and related counterterrorism activities as an inherently governmental obligation. However, the vast majority of the targets that require protection are those owned by the private sector—critical infrastructure such as water and power sources and information systems. Many of the emergency response and recovery capabilities are those with nonfederal or not-for-profit entities, such as public health facilities.

▶ *Are existing incentives sufficient to support private sector protection of critical infrastructure it owns, and what changes might be necessary? How can intelligence and information on threats be shared with other levels of government and other critical entities, yet be held secure?*

Measuring progress in the current war on terrorism is very much a work in progress. Measures in use—such as the number of terrorists detained or arrested worldwide or kept on the run—may be extremely limited or meaningless without knowing if such actions seriously destroy, degrade, or disrupt terrorists' plans or seriously degrade or dissuade their recruitment efforts and community support. The apparent lack of international terrorist attacks within our borders since the September 2001 attacks suggests positive

results from our homeland security actions, but it may also simply reflect terrorist choice of the time and place of another attack. Small-scale domestic terrorist attacks still occur. Fully addressing the range of threats posed by terrorism and its causes requires more sophisticated ways to gauge progress.

▶ *What is the most viable way to approach homeland security results management and accountability? For example, how should progress in the current war on terrorism be measured and assessed? What are the appropriate goals for prevention, vulnerability reduction, and response and recovery? Who is accountable for the many components of homeland security when many partners and functions and disciplines are involved? How can these actors be held accountable and by whom?*

Traditionally, state and local governments have had the primary responsibility for financing first responders' preparation for and response to disasters, whether natural or manmade, which are generally local in their cause and effect. Prior to September 11, 2001, the federal government's role was limited primarily to providing guidance, some grants for planning, mitigation, and equipment, and disaster response and recovery assistance after such major disasters as hurricanes, earthquakes, and floods. Since September 11, 2001, the federal government has provided billions of dollars to state and local governments for planning, equipment, and training to enhance the capabilities of first responders to respond to both smaller scale natural disasters and terrorist attacks. However, the federal financial assistance provided in the last several years has not been guided by a clear risk-based strategic plan that outlines the role of federal, state, and local governments in identifying, enhancing, maintaining, and financing critical first responder capabilities for emergencies. Moreover, while planning and assistance has largely been focused on single jurisdictions and their immediately adjacent neighbors, well-documented problems with first responders from multiple organizations to communicate at the site of an incident and the potential for large scale terrorist incidents have generated a debate on the extent to which first responders should be focusing their planning and preparation on a regional and multi-governmental basis. In addition, no standards have been established on which to determine the equipment, skills,

and capacities that first responders need given the risks individual locations may face. In the absence of risk-based performance standards that could be used to establish baseline capabilities and critical capacities, state and local governments have used their own criteria for determining how federal grant funds should be spent. The absence of standards has also made it difficult for first responders to define the gap between what is and what should be and measure their progress in achieving defined performance goals.

▶ *What should be the role of federal, state, and local governments in identifying risks—from nature or man—in individual states and localities and establishing standards for the equipment, skills, and capacities that first responders need?*

▶ *What costs should be borne by federal, state, and local governments or the private sector in preparing for, responding to, and recovering from disasters large and small—whether the acts of nature or man, accidental or deliberate?*

▶ *To what extent and how should the federal government encourage and foster a role for regional or multistate entities in emergency planning and response?*

International Challenges for the 21st Century

The United States faces rising challenges and threats to its national and economic security. These threats include terrorism, regional conflicts, and global instability sparked by growing gaps between the "haves" and "have nots," as well as by corruption, ethnic hatred, and disease. At the same time, the world grows increasingly interconnected through more open markets, rapidly developing technology, and efficient transportation systems.

In this environment, advancing and protecting U.S. international interests requires the use of all available instruments of power—military, diplomatic, and economic. The United States has periodically employed its armed forces and civilian agencies, often in conjunction with U.S. allies and the international community, to address various threats to regional and international peace and stability. The United States also maintains a vast network of embassies and consulates at about 260 locations around the world, staffed by about 60,000 U.S. and foreign national employees, to carry out foreign policy and public diplomacy programs. In addition, the United States seeks to advance its interests by participating in a wide variety of multilateral organizations. While trying to anticipate and address emerging threats, the U.S. government also seeks to promote foreign policy goals, national and economic security objectives, sound trade policies, and other strategies to advance the interests of the United States and its trading partners and allies. The 21st century will bring increased challenges in balancing security concerns with the desire to maintain strong economic and cultural ties essential to domestic well being.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

The continuing proliferation of biological, chemical, and nuclear weapons and delivery systems poses serious threats to the security of the United States and its allies. The increasing likelihood that a rogue regime or terrorists will attempt to threaten or attack the United States or its allies with weapons of mass destruction (WMD) will challenge the U.S. nonproliferation and counterproliferation efforts and preparations for the consequences of WMD use. For example, the great majority of Russian chemical weapons remain vulnerable to theft or diversion by terrorists or rogue states.

▶ *Do U.S. efforts to reduce or prepare for such WMD threats need to be reexamined? For example, does U.S. nonproliferation assistance, currently provided almost exclusively to Russia, need to be extended to other countries, such as Libya, that have WMD assets that must be eliminated or secured? What U.S. and international responses are needed to better deal with the increased security threats posed by rogue states and terrorists seeking to acquire and use WMD? How can the United States better work with our allies and others to prevent the spread of WMD?*

Protecting U.S. strategic interests in the face of new tests has presented challenges for alliances established decades ago. For example, serious disagreement with North Atlantic Treaty Organization (NATO) allies France and Germany over U.S. policy in Iraq exposed fundamental differences over how the alliance should respond to security threats. Conflict interventions to make or keep peace, stabilize failed states, and end terrorist regimes have dominated U.S. foreign policy actions in recent years. Such interventions will likely continue to play a prominent role in efforts to stabilize regions where U.S. interests are undermined or threatened.

▶ *Do we need to reexamine the U.S. force structure used for nation building and peacekeeping activities by the United Nations, NATO, and other international institutions? Should the United States have a separate force devoted to such functions? What role should the United Nations, NATO, and other international institutions perform in connection with such functions?*

Increasing global interdependency and shifting trade patterns create a range of challenges for policymakers. The high level of U.S. trade deficits, rapid increases in imports from nations such as China, and the increase in services trade have led to questions about the best way to ensure that trade is fair and contributes to the well-being of the American people. To date, new trade concerns, such as offshoring of high-tech services and currency interventions, have generally not been dealt with directly by traditional U.S. trade policy tools, such as trade agreements, and will challenge policymakers to develop new strategies for dealing with them. Moreover, the globalization of economic activity is bringing an increasing share of the U.S. economy under the domain of international agreements.

Economic activity historically viewed as isolated from international trade agreements, such as local government procurement practices, may come under the scrutiny of other parties to the trade agreements, and increasingly be subject to their enforcement machinery.

▶ *Does the U.S. portfolio of international trade policy tools, such as its heavy reliance on industry-specific trade agreements, need to be reexamined for its effectiveness and relevance in addressing new trade concerns such as offshoring and currency interventions?*

▶ *What types of policy commitments and programs, such as agricultural subsidies and import restrictions on textiles, may need to be reexamined for their consistency with broader international trade goals?*

Although the United States' commitment to foreign aid has spanned more than half a century, questions persist about the effectiveness of bilateral U.S. aid to developing countries and multilateral aid provided by international financial institutions. The United States recently established a new foreign assistance program, the Millennium Challenge Account (MCA), to function alongside the U.S. Agency for International Development. MCA's goal is to reduce global poverty through economic growth in countries that govern justly, invest in their people, and encourage economic freedom. However, like other foreign assistance efforts, MCA will face challenges such as inconsistent political will, ineffective donor coordination, and limited capacity of recipient nations to absorb donor resources. Moreover, few, if any, countries that have received bilateral aid have significantly reduced poverty, and rapid advances in technology have caused poorer countries to fall further behind. Regarding multilateral aid, the World Bank and International Monetary Fund (IMF) did not prevent or quickly resolve the recent financial crisis in Argentina, although Argentina had implemented reform programs funded by those institutions since at least the early 1990s. Similarly, despite 9 years of ongoing efforts by the World Bank and IMF, the debt problems of the poorest nations will likely continue for decades.

▶ *Should the United States reevaluate its approach to reducing world poverty? For example, what role should continued bilateral U.S. aid or support of loans and grants through multilateral agencies play? Should certain existing multilateral development loans be forgiven? Are international financial institutions structured to achieve the long-term financial health and stability of the countries they seek to help?*

U.S. embassies and consulates are on the front lines, conducting diplomatic activities and operating programs that are critical to achieving a wide range of foreign policy interests. In addition to interacting with foreign governments, embassies and consulates conduct public diplomacy, promote trade, screen visa applicants wishing to visit the United States, assist American citizens overseas, and play a key role in fostering military alliances and providing military and economic aid. Security priorities after 9/11 have further complicated their mission. The demands placed on embassies and consulates by a rapidly changing world challenge their existing ways of organizing themselves and matching their resources and skills to meet those demands. While there have been attempts to review how overseas resource allocations are made, the rapidly changing world prompts the need to continually reexamine mission priorities to determine the "who, where, and when," as well as the mix of U.S. government and nongovernmental personnel that should be overseas. Concerns over security for staff assigned overseas and fiscal pressures will also prompt the consideration of alternative ways of doing business overseas, such as streamlining or outsourcing functions and performing functions from the United States or other remote locations.

▶ *How can the U.S. presence overseas be rationalized to "right place" as well as "right size" embassies and consulates and ensure secure and cost-effective overseas operations while continuing to meet key foreign policy objectives and priorities?*

Natural Resources, Energy, and the Environment Challenges for the 21st Century

Following passage of major environmental legislation in the 1970s, the nation made a number of gains in its air and water quality, and expressed a commitment to improved management of our natural resources. As the nation moves into the 21st century, it is becoming increasingly apparent that the current approach to natural resource use (including energy) and environmental protection may need modification to successfully address the long-term stresses affecting so many of our nation's and the world's natural ecosystems. Evidence of this stress can be found on many fronts, including depleted fresh water supplies, deteriorating fisheries, multiple energy crises, and accelerated loss of biodiversity. Similarly, the globalization of agribusiness coupled with increasing concentration in the nation's agriculture sector raises questions about whether the historic agriculture subsidy and support structures remain appropriate.

In this context, the broad, long-term challenge is determining how the nation can reconcile the desire for consumption today with the need to protect resources to sustain the future. From the available evidence, there is reason to reexamine existing programs to determine the balance between supporting the needs of today's economy with our stewardship obligations to the generations to come. Federal regulatory and economic programs, policies, and approaches devised and implemented decades ago may need to be reassessed, and new approaches, such as pricing strategies, need to be considered to ration scarce resources. Natural resource, energy, and environmental concerns are inextricably linked.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

Land use planning practices that do not adequately consider land, water, and petroleum availability can contribute to sprawling development and a host of problems. Such practices have had a part in automobile usage reaching new highs each year, open space dwindling, air pollution becoming more difficult to control, and the reliance on imported oil continuing to climb. Likewise, population growth, particularly in arid regions of the country, may soon face a limiting obstacle—the availability of fresh water. In fact, water managers in 36 states expect water shortages to occur within the

next 10 years under even normal conditions. In many parts of the country, drought conditions are giving an early indication of what may occur on a much more widespread basis in the future. Federal transportation and other incentive structures have played a role in current land use planning results. In this context, it may be time to examine land use planning and associated federal incentive structures to ensure that they are not having unintended consequences. Relatedly, federal natural resource allocation and usage decisions are distorted when the federal government does not charge fair market value when offering these resources for sale. Whether it be oil and gas, timber, grazing rights, or water, the federal government has a history of selling its assets at much lower prices than others or perhaps even below the cost of delivering the asset. When this occurs, the federal government shortchanges the Treasury and distorts markets for these resources.

▶ *Can alternative federal approaches to transportation, land management, and water policies be adjusted to better promote sustainable management of our nation's land and water resources? For example, given projected water supply shortages, is there a need to reassess the balance between urban expansion in water-scarce regions and continuance of existing crop irrigation practices? Additionally, should steps be taken to ensure that user fees commensurate with fair market value or the costs of providing services are collected when federal natural resources are sold?*

The nation's energy consumption is significant and growing. Today, according to our analysis of U.S. Department of Energy (DOE) data, total U.S. energy consumption is equivalent to about 790 billion gallons of gasoline per year, which is nearly 2,800 gallons consumed by every man, woman, and child each year. Energy consumption is expected to increase about 30 percent over the next 20 years. As a result of these ever-increasing demands, energy reliability, affordability, efficiency, and sustainability remain a concern. Not only has our nation experienced multiple energy crises, but our systems remain perpetually on the cusp of critical supply/demand imbalances. These imbalances can quickly lead to price volatility that burdens consumers and the industry and adversely affects our economy. While there are differences of opinion as to how long the nation can rely on finite fossil energy

supplies to meet the majority of its energy needs, there seems little doubt that at some point the nation will need to transition to alternatives. Enhanced conservation could delay this transition point, but many believe that without a vision for a sustainable energy future, our nation's energy markets in the 21st century will likely continue to experience the turmoil of the past with increasing frequency. The recent collapse of the energy grid in northeastern and midwestern states and the cascading blackouts that followed, as well as the increases in gasoline and heating oil prices, may be early warning signs of more pressing problems to come. In this context, in addition to aggressively pursuing opportunities to increase production, it may be time to consider placing a similar emphasis on and investment in demand reduction strategies and development of alternative or renewable energy supplies and technologies. Preparing the nation for its long-term energy future may be dependent on an approach that adequately balances all its options.

▶ *To what extent are federal energy policies and incentive structures adequately preparing the nation to satisfy its energy needs over the long term? What is the appropriate balance between efforts to promote enhanced production of fossil fuels, alternative renewable energy sources, and energy conservation?*

While the nation has made great strides in improving the quality of our air and water, questions are increasingly being raised about whether the current policies, strategies, regulatory approaches, and organizational structures—that in some cases were put in place in the 1970s—will be up to the challenge of protecting our air and water quality in the decades to come. Our nation's urbanized areas are continually battling to keep air pollution in check, and the regional dimensions of air-quality problems are being increasingly exposed by concerns over the spread of pollution from coal-fired power plants and other industrial sources in the Midwest into the Northeast states. Likewise, it continues to be a challenge to restore and protect national treasures such as the Chesapeake Bay and the Great Lakes. Despite hundreds of millions of dollars being spent, efforts to restore these waters to healthy conditions are not showing as much progress as hoped. In addition, the nation faces a more than $150 billion burden over the next two decades to repair, replace, and upgrade the nation's over 55,000 community drinking

water and wastewater systems to protect public health. A reexamination of current approaches to address these problems may be in order to better achieve overall environmental outcomes while providing more flexibility in achieving them. The establishment and institutionalization of a science-based, widely accepted set of environmental indicators to improve the quality of air and water quality data is an essential prerequisite to evaluate alternative approaches.

▶ *Does the existing federal regulatory approach for controlling air and water pollution need to be modernized to generate improved results? In particular, can the current prescriptive "command and control" regulatory structure be changed to more cost effectively reduce pollution and better protect the environment?*

▶ *Is there a way for the federal government to implement environmental regulations more efficiently and effectively by taking into account the cumulative costs of multiple environmental regulations to state, local, and tribal governments while at the same time ensuring benefits to human health and the environment?*

It is also unclear whether current agricultural practices and the federal policies that have promoted them remain appropriate and sustainable. When federal agricultural policies were first implemented, the United States was a largely rural nation. Farming and its related federal support were the lifeblood of many rural communities. Today, the U.S. agricultural sector is dominated by a relatively small number of agribusiness giants and very large farming operations that operate globally. For example, while there are still over 2 million farms in the United States, less than 10 percent of them provide 70 percent of the nation's food and fiber and account for the vast majority of the $60 billion worth of agricultural exports that help sustain the sector. Federal support for agriculture exceeds $25 billion annually. Critics question the need for this level of subsidies, which mostly go to larger producers, particularly considering the government's current and projected fiscal imbalance. In addition, while the Congress recently passed legislation to phase out support to tobacco growers, large subsidies remain for a number of crops that are often criticized in the international marketplace as being anticompetitive. Furthermore, farming and livestock operations have become highly concentrated,

and the associated fertilizer, pesticide, and animal waste run-off are being increasingly recognized as major contributors to water pollution. Finally, rural communities have changed as well. Farming is no longer the dominant activity in many rural communities, and many of the large-scale electrification and related infrastructure development programs are logical candidates for reexamination. Accordingly, new approaches to agricultural programs and policies better oriented to modern challenges may be in order.

▶ *Do current federal agricultural policies and programs, which largely rely on subsidies, remain relevant to the modern agricultural sector? In addition, are current policies contributing to unfair trade practices?*

▶ *Can these policies and programs be sustained? Could alternative approaches produce desired results more economically, effectively, and efficiently? For example, could the federal crop insurance program be expanded to play a larger role in the federal safety net for farmers?*

▶ *Are government supports for or ownership of energy production and electricity generation in rural areas and particular regions still necessary given fundamental changes in the past 50 years in energy market infrastructure?*

According to the combined estimates from DOE, DOD, and the U.S. Environmental Protection Agency (EPA), it could cost in excess of $500 billion in current dollars to clean up (1) the radioactive wastes accumulated during 50 years of nuclear weapons production at DOE facilities, (2) unexploded ordnance, discarded munitions, and related contamination at current or former U.S. military sites, and (3) hundreds of thousands of Superfund and other hazardous waste sites created by private sector activities. Some of the contamination in these sites may take 50 to 70 years to clean up; at other sites, the contamination is so extensive that it may be irreversible and the site may be irretrievable. Frequently, the progress in cleaning up these sites does not meet expected time frames and the costs dramatically exceed available funding levels. For example, DOE's projects for treating and storing radioactive and hazardous waste, a by-product of nuclear weapons production at DOE facilities, are estimated to cost more than $140 billion and could take decades to complete. Furthermore, the current

approaches to cleaning up DOE, DOD, and EPA sites are not consistent and, in some cases, not especially efficient or effective; development of more innovative incentives and approaches may be needed. The enormity of this task, combined with the fiscal constraints facing the nation, raises questions about whether existing cleanup standards are realistic.

▶ *Does the current pace and cost of nuclear and hazardous materials cleanup activities at DOE, DOD, and EPA sites suggest the need for alternative approaches to address these issues? Can the nation afford to cleanup radioactive and hazardous waste sites to the standards currently being applied? For example, are there opportunities for DOE to apply risk factors, just as EPA assigns risk factors to Superfund sites, to determine the most cost-effective approach to clean up a site, possibly resulting in disposal of more waste at current sites rather than moving it to the planned underground repository?*

Retirement and Disability Policy Challenges for the 21st Century

One of the great American achievements of the 20th century was the development of a comprehensive national social insurance system. A core element of the system was a sturdy retirement component—with Social Security as a foundation, supplemented by a private pension system and individual savings arrangements—which sought to conquer the long-standing economic fear of poverty in old age. For the last half century, millions of American workers were able to look forward to their retirement as a time of dignity, respect, and security. The Congress later extended these social insurance protections to those workers who were unable to engage in gainful economic activity because of disability. Indeed, insuring workers and their families from the potentially devastating income loss caused by unexpected injury, illness, or death removed another great risk to their economic well-being.

The challenges facing retirement and disability programs are long-term, severe, and structural in nature. A successful policy response to these challenges will require a fundamental and comprehensive reassessment of each of the key components of our national retirement and disability system.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

Social Security faces severe, long-term, structural financing challenges that if not addressed, could lead to the depletion of its trust funds. The unfunded obligation for the Old Age, Survivors, and Disability Insurance (OASDI) trust funds for the next 75 years is $3.7 trillion in present value as of 2004. Projected tax income to the OASDI trust funds will begin to fall short of outlays in 2018 and, by 2042, trust fund balances will be insufficient to fully finance benefits promised under the current program. Social Security faces this long-term financing shortfall largely because of several concurrent demographic trends, namely that people are living longer, spending more time in retirement, and having fewer children. For example, average time in retirement grew from 11.5 years in 1950 to 18 years for the average male worker as of 2003. Women are also having fewer children. In the 1960s, the fertility rate was an average of 3 children per woman, but by 2030 it is expected to fall to 1.95—a rate that is below replacement. Taken

together, these trends threaten the financial solvency and sustainability of Social Security as well as the federal budget as a whole. Social Security could be brought into balance over the next 75 years in various ways, including an immediate increase in payroll taxes of 15 percent or an immediate reduction in currently promised benefits of 13 percent (or some combination of the two). Ensuring the sustainability of the system beyond 75 years will require even larger changes. Encouraging older workers to extend their labor force participation can also improve program solvency while contributing to overall economic growth. Lastly, highlighting the need for early action, even greater adjustments in scheduled benefits and revenues will be required the longer Social Security's financial challenges remain unaddressed.

▶ *How should Social Security be reformed to provide for long-term program solvency and sustainability while also ensuring adequate benefits (for example, increase the retirement age, restructure benefits, increase taxes, and/or create individual accounts)?*

▶ *How can existing policies and programs be reformed to encourage older workers to work longer and to facilitate phased retirement approaches to employment (for example, more flexible work schedules or receiving partial pensions while continuing to work)?*

Serious weaknesses have become manifest in our nation's private pension system. Despite sustained large federal tax subsidies, total pension coverage continues to hover at about half of the total private sector labor force. The number of traditional defined benefit plans in which employers rather than employees bear the risk of investment has been contracting for decades, and recent plan terminations by bankrupt sponsors of large defined benefit plans have threatened the solvency of the Pension Benefit Guaranty Corporation (PBGC), the federal agency that insures certain benefits under such plans. Recognizing the long-term challenges facing PBGC, GAO has placed PBGC's single-employer pension program on its high-risk list of programs needing further attention and congressional action. As of the end of fiscal year 2004, the agency's single-employer pension program registered a net negative accumulated position of $23.3 billion. While growth in the number

and coverage of defined contribution plans—where each worker has an individual account that receives contributions—has somewhat mitigated the decline of more traditional defined benefit plans, these plans have also experienced problems. Many workers covered by defined contribution pension plans continue to choose not to participate, potentially leaving them with an inadequate retirement income. The risk burden of defined contribution plans requires individual employees to be knowledgeable about investment and other retirement decisions, yet information and education are not always available. Large holdings of company stock in such plans may add to employees' risk that their retirement savings will be inadequate to provide levels of income needed in retirement. Finally, workers receiving their retirement benefit in a lump sum and the ability to withdraw or borrow money from retirement saving plans prior to retirement to supplement current consumption can drain workers' accounts of needed benefits well before retirement. Policymakers will need to consider how to best encourage wider pension coverage and adequate and secure pension benefits that are preserved for retirement purposes for the current and the future labor force, and how such pensions might best interact with changes to the Social Security program.

▶ *What changes should be made to enhance the retirement income security of workers while protecting the fiscal integrity of the PBGC insurance program (for example, increasing transparency in connection with underfunded plans, modifying PBGC's premium structure and insurance guarantees, reforming plan funding rules, or restricting benefit increases and the distribution of lump sum benefits in connection with certain underfunded plans)?*

▶ *How can existing policies be reformed to encourage income preservation strategies so that retirement income lasts an individual's entire life (for example, benefit annuitization)?*

Meanwhile, federal disability programs, such as those at the Social Security Administration (SSA) and the Department of Veterans Affairs (VA), have experienced significant growth over the past decade and are expected to grow even more as increasing numbers of baby boomers reach their disability-prone years. Moreover, the composition of the disability rolls has changed significantly, with a

larger proportion of beneficiaries with mental impairments receiving benefits today than in the past. At the same time, recent scientific advances as well as economic and social changes have redefined the relationship between impairments and work. Advances in medicine and technology have reduced the severity of some medical conditions and have allowed individuals to live with greater independence and function in work settings. Moreover, the nature of work has changed in recent decades as the national economy has moved away from manufacturing-based jobs to service- and knowledge-based employment. Given the projected slowdown in the growth of the nation's labor force, it is imperative that those who can work are supported in their efforts to do so. Yet federal disability programs remain mired in concepts from the past and are poorly positioned to provide meaningful and timely support for workers with disabilities. Further, in light of a congressionally established commission to study the appropriateness of veterans' benefits, VA may be faced with the need to reform its eligibility criteria. Over the last decade, GAO has built a body of work examining these issues and, more recently, has called for the fundamental transformation and modernization of federal disability programs, including SSA's Disability Insurance and Supplemental Security Income programs and VA's disability programs. In January 2003, GAO added modernizing federal disability programs to its high-risk list.

▶ *How can federal disability programs, and their eligibility criteria, be brought into line with the current state of science, medicine, technology, and labor market conditions (for example, which jobs are based on knowledge and skills rather than on strength and endurance)? How can such programs better facilitate the participation of people with disabilities in the workforce and society (for example, earlier intervention in providing vocational rehabilitation or assistive technology devices such as voice synthesizers or standing wheelchairs)?*

▶ *What options could be considered for reforming VA's current disability benefits structure for veterans (such as revisiting the definition of service-connected benefits) that would ensure appropriate and adequate benefits?*

Scientific and Technological Innovation Challenges for the 21st Century

For society and government, developments in science and technology present great opportunities to improve the quality of life, the performance of the economy and the government, and the relationship of government to its citizens. Advances in science and technology in the United States have historically been fueled by combined public and private sector research and development investments of about $284 billion annually. These investments, along with the nation's strong research and development infrastructure and intellectual property protections, have long ensured the United States a leadership position in the development and commercialization of scientific advances and have helped nurture entrepreneurship and dissemination of information on new technologies. The benefits of applying technological innovation, such as information technology, in the United States, have not only resulted in many positive outcomes but have also presented many new challenges, concerns, and vulnerabilities.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

As the pace of innovation has quickened over the past 30 years, competition in the global economy has also accelerated and other nations are increasingly gaining in their ability to commercialize technological advances, educate highly skilled technical workforces, and offer world-class research opportunities to the best and brightest minds. These strides in global scientific and technological innovation are beginning to challenge the United States' preeminent position.

▶ *How can the federal government develop a more coordinated and targeted approach to setting the U.S. research agenda that also ensures the best return on investment? For example, can the current patchwork of federal investments in scientific research provided by multiple agencies and programs be integrated or better coordinated to more effectively and efficiently identify and prioritize critical emerging technologies?*

▶ *Are different kinds of federal incentives needed to encourage greater private sector collaboration and nurture interdisciplinary research and development approaches that can enhance U.S. competitiveness and productivity? For*

example, does the current research tax credit actually stimulate private sector research spending that would not have occurred otherwise? Are the types of research being done by businesses that claim most of the tax credit enhancing U.S. competitiveness and productivity?

▶ *Can existing program structures and funding processes maintain the nation's position as a critical collaborator in jointly funded international scientific research and ensure that the United States can continue to attract global investments in new technologies? For example, how can the U.S. nanotechnology research and development effort effectively collaborate with global nanotechnology research and development efforts without compromising the nation's intellectual property or competitiveness?*

Compounding these external challenges are domestic demographic and educational changes that have reduced the size and quality of the U.S. scientific workforce, such as the lagging performance of U.S. students in science, math, and engineering; the large numbers of U.S. scientists reaching retirement age; and reduced numbers of foreign-born scientists and researchers coming to the United States because of heightened security concerns and opportunities in other nations.

▶ *How can the United States better develop a world-class technical and scientific domestic workforce that is not as dependent on large inflows of international students and researchers? For example, are different educational tools or targeted funding strategies needed to enhance U.S. student achievements in math and the sciences?*

▶ *Do current workforce retraining programs provide adequate incentives to help the United States develop lifelong learning strategies and proactive training programs that will meet the needs of a rapidly changing technological environment? For example, should the federal government consider providing training tax credits to employers or individuals so that U.S. workers can obtain the training they need to stay current in a knowledge-based economy?*

Information technology advancements have contributed to substantial gains in U.S. productivity, opened the workforce to people who were previously barred because of physical disabilities or geographic distances, and have begun to alter the way citizens

interact with their government. However, interconnectivity has also raised the potential for unauthorized access to personal and confidential data and created new vulnerabilities to the nation's critical operations and the infrastructures they support.

▶ *How can the federal government effectively utilize advanced technologies to further enhance homeland security while also protecting the privacy of U.S. citizens? For example, should the federal government encourage states to use biometric technologies that could help ensure that drivers licenses are issued only to authorized and authenticated individuals?*

▶ *What cybersecurity technologies can be applied to protect critical infrastructures from attack given current threat assessments and what implementation challenges, such as effective information sharing among key public and private stakeholders, will have to be addressed?*

Similarly, despite many successes in the exploration of space, the loss of life, unsuccessful missions, and unforeseen cost overruns have recently increased the level of concern over the benefits of such exploration, particularly with regard to human space flight activities. Since its inception, the National Aeronautics and Space Administration (NASA) has undertaken programs that have greatly advanced scientific and technological knowledge. However, a painful symbol of the difficult environment in which NASA must perform its mission, as well as the risks associated with human space exploration, is the recent loss of Shuttle Columbia and its crew. The complexities NASA faces in returning the remaining three shuttles to flight so that construction can resume on the International Space Station and the debate over the potential cost and the federal government's role in implementing the administration's vision for space exploration are emblematic of the challenges the nation will need to resolve in the years ahead.

▶ *What objectives are both appropriate and affordable for the U.S. space program? For example, can all existing programs continue to be effectively implemented at current resource levels and without substantial involvement by the private sector?*

Transportation Challenges for the 21st Century

The nation's economic vitality and the quality of life of its citizens depend significantly on the soundness, security, and availability of its physical infrastructure. The nation's transportation system presents particularly complex policy challenges, because it encompasses many modes—air, water, highway, transit, and rail—on systems owned, funded, and operated by both the public and private sectors. Increasing passenger and freight travel has led to growing congestion, and policymakers face the challenge of maintaining the safety and condition of the transportation system while preventing congestion from overwhelming it. Transportation decisions are inextricably linked with economic, environmental, and energy policy concerns, and coordination across levels of government and different sectors is daunting and complex. New security imperatives in a world after 9/11 present additional challenges for all modes of transportation that must be addressed in a rapidly changing demographic and technological landscape. Successfully addressing transportation needs in the face of these complex, crosscutting challenges requires strategic and intermodal approaches, effective tools and programs, and coordinated solutions involving all levels of government and the private sector.

These requirements, in combination with the looming fiscal crisis faced by all levels of government, challenge the nation to fundamentally reexamine existing government transportation programs and commitments, to ask whether existing program constructs and financing mechanisms are relevant to the challenges of the 21st century, and to make tough choices in setting priorities and linking resources to results.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

The transportation grant programs funded by the Highway Trust Fund—including the nation's highway and transit programs—have evolved slowly since the Trust Fund was created in 1956. While the program was created for the purpose of constructing the interstate highway system, and the interstate is complete, the basic construct of the program, in terms of its financing and delivery mechanisms, has not changed. In addition, this and other federal transportation programs do not have the mechanisms to link funding levels with

the accomplishment of specific performance-related goals and outcomes, such as improvements in mobility and security. Most highway grant funds are apportioned by formula, without regard to the needs or capacity of recipients. Because many state and local governments select most projects receiving this funding, there is little assurance that the projects selected and funded best meet the nation's mobility and security needs.

▶ *How narrowly or broadly should the federal role and interest in the nation's transportation system be defined? For example, should federal programs and spending be more closely aligned with specific national interests and purposes, such as interstate freight mobility or national and homeland defense? Concurrently, should responsibilities and authority for projects that support regional mobility and other needs be devolved to state and local governments along with the revenue sources that support them?*

▶ *Should the federal transportation formula grant programs for state and local governments be revised to better consider factors such as need, performance, capacity, and level of effort by the states and localities?*

Transportation programs and funding mechanisms are largely stovepiped by modes of transportation. For example, while passenger and freight travel occurs on all modes, federal funding and planning requirements focus largely on highway, transit, and aviation passenger travel. This framework makes it difficult for intermodal projects and other modal projects (e.g., freight or passenger rail) to be integrated into the transportation system.

▶ *Can intermodal solutions to the needs of modes such as freight, air, and passenger rail service be effectively carried out within the framework of the existing trust funds and other transportation programs or is another model needed? Do the existing tools and delivery mechanisms, such as existing trust funds dedicated only to certain modes of transportation, have the wherewithal to provide intermodal, efficient, cost-effective solutions to mobility and security challenges?*

While the trust funds were originally based on the concept of having users pay for the transportation systems, this concept is beginning to fray. Revenues to the Highway Trust Fund, which funds the

majority of highway and surface transportation safety spending and a large portion of transit spending, are drawn from fuel taxes and user fees. The purchasing power of these revenues is declining and future fuel tax revenues will be further eroded by the increasing fuel efficiency of vehicles. Aviation Trust Fund revenues are also declining, in part because of lower cost airline tickets and other factors. The Federal Aviation Adminstration will face significant challenges in supporting its four major accounts, which include operations, facilities and equipment, airport improvement program, and research, engineering, and development. Many experts question whether the current financing scheme for transportation is ultimately sustainable. As a result, decisionmakers are increasingly looking more to the general fund to finance transportation programs, and state and local governments are increasingly relying on property and sales taxes to fund transportation improvements.

▶ *Should the federal government continue to provide public financing through grant programs or develop alternative, targeted, market-driven incentives, such as credit enhancements, to stimulate private financing, particularly in areas such as freight, maritime, and aviation where a mix of private and public beneficiaries exist?*

The use of tolls, congestion pricing, and user fees holds promise for helping to solve congestion and mobility problems and provide new revenues for infrastructure improvements. However, the availability of competing federal grant funds and federal restrictions on tolling, pricing, and fees can work at cross purposes by dissuading state and local governments and transportation service providers from adopting these tools.

▶ *What other mechanisms are available—e.g., tolls, pricing, demand management, or user fees—that could be used to a greater degree than today to help finance the nation's transportation infrastructure that are both sustainable and would promote efficiency in the use of infrastructure and better capture revenue from beneficiaries?*

Governance Capacity to Meet Challenges in the 21st Century

The federal government must address and adapt to a range of major trends and challenges in the nation and the world—a long-term, structural fiscal imbalance; a transformation from an industrially based to a knowledge-based economy; revolutionary changes in technology that have altered how we communicate and do business globally; greater reliance on market forces and competition; and changing national security threats. To respond to these trends and challenges, government must have the institutional capacity to plan more strategically, identify and react more expediently, and focus on achieving results.

There are signs of transformation as the Congress has established agencies that can meet evolving challenges. For example, recognizing growing security threats, the Congress created the Department of Homeland Security to fundamentally transform how the government is structured to respond to these threats and has recently restructured the intelligence community to ensure the nation has the critical information it needs to defeat these threats. Likewise, agencies including the Federal Bureau of Investigation (FBI), GAO, National Aeronautics and Space Administration (NASA), the Department of Defense (DOD), and the U.S. Postal Service are undertaking major efforts to transform their operations. Furthermore, the government is partnering with the private sector to devise a comprehensive set of key national indicators to provide the nation with quality data that the public, media, policymakers, and both government and nongovernment institutions can use to assess the nation's progress in addressing key challenges.

Yet, in many cases, the government is still trying to do business in ways that are based on conditions, priorities, and approaches that existed decades ago and are not well suited to addressing 21st century challenges. For example, some agencies do not yet have all the necessary abilities, more flexible legal authorities, and leadership and management capabilities to transform their cultures and operations. Consequently, to successfully navigate transformations across the government, it must fundamentally reexamine not only its business processes, but also its outmoded organizational structures, management approaches, and in some cases, outdated missions.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

To be a leading democracy in the information age may very well mean producing unique public sources of objective, independent, scientifically grounded, and widely shared quality information so that we know where the United States stands now and what the trends are on both an absolute and relative bases—including comparisons with other nations. By ensuring that the best facts are made more accessible and usable by the many different members of our society, we increase the probability of well-framed problems, good decisions, and effective solutions. The stakes are high, including considerations regarding allocating scarce public resources, strengthening the economy, creating jobs, stimulating future industries, enhancing security, promoting safety, strengthening our competitive edge, and sustaining the environment.

▶ *Is the federal government effectively informed by a key national indicator system about the position and progress of the nation as a whole—both on an absolute and relative bases compared to other nations—as a guide to helping set agency and program goals and priorities?*

▶ *Is the federal statistical system adapting effectively to the nation's needs for information? Is it effective at all levels and sectors of society to meet evolving information requirements? Are the large amounts of data that it collects being effectively disseminated to the widest possible audiences, with due consideration to privacy and confidentiality issues?*

Most major outcomes of federal activities are supported by multiple programs and tools that, in turn, are often sponsored by many different federal agencies. Although these individual programs address common or similar performance goals, they result in an overly fragmented delivery network and at times work at cross purposes. For example, federal food safety programs are carried out by 12 agencies with differing enforcement criteria and inspection practices. The fragmentation of federal programs reflects a policymaking process that is overly stovepiped by agency and program, with insufficient focus on how individual programs

contribute to overarching, crosscutting goals and missions. As a result, the capacity to periodically reexamine the alignment and relevance of policy portfolios in a changing society is limited. The Government Performance and Results Act (GPRA) provided for a governmentwide performance plan to address these issues, but this plan has not yet been developed by the executive branch. Furthermore, the federal government lacks a governmentwide strategic plan to provide a framework for addressing crosscutting goals.

▶ *How can the executive branch and the Congress have a more strategic, crosscutting focus on policy and budget decisions to address goals that cut across conventional agency and program boundaries? Can the governmentwide performance plan required by GPRA be implemented to provide the necessary crosscutting focus?*

▶ *How can agencies partner or integrate their activities in new ways, especially with each other, on crosscutting issues, share accountability for crosscutting outcomes, and evaluate their individual and organizational contributions to these outcomes? How can agencies more strategically manage their portfolio of tools and adopt more innovative methods to contribute to the achievement of national outcomes? For example, how can the myriad federal food safety programs managed across several federal agencies be consolidated to better promote safety and the integrity of the nation's food supply?*

Increasingly, the government relies on new networks and partnerships to achieve critical results and develop public policy, often including multiple federal agencies, domestic and international non- or quasi-government organizations, for-profit and not-for-profit contractors, and state and local governments. The federal government uses an array of different tools and program designs to work in this environment, such as direct service delivery, loans and loan guarantees, tax preferences, insurance programs, grants, and regulations. Ranging from education to homeland security, a complex network of governmental and nongovernmental entities shape the actual outcomes achieved, whether it be through formal partnerships in grant programs or through independent actions of each acting locally to address common problems. Notwithstanding the increased linkages in our system, each level of government often

makes decisions on these interrelated programs independently, with little interaction or intergovernmental dialogue. While the magnitude of the nation's challenges calls for a concerted effort across sectors, there are insufficient opportunities for leaders of those sectors to come together to reach consensus about the kinds of mutual commitments that are necessary.

▶ *How can greater coordination and dialogue be achieved across all levels of government to ensure a concerted effort by the public sector as a whole in addressing key national challenges and problems? For example, what mechanisms might usefully bring together leaders across governments to address joint problems, perhaps through establishing commissions or other vehicles for promoting dialogue?*

More specifically, government has also begun to fundamentally change who does its business—recognizing that it could better partner with the private sector in new, more cost-effective ways. Agencies are assessing what functions and transactions the private sector could perform and asking their employees to compete with private entities for this business to improve quality and reduce costs. But the government does not yet know how this trend is affecting its workforce and its ability to refocus more on strategic needs or the extent to which it has delivered real cost savings. Collecting and evaluating data to ensure such transformations are implemented effectively and deliver the desired results will be critical.

▶ *Has the government's approach to competitive sourcing—using the private sector to do more of the government's business—proven successful? Should it be modified to improve results and reduce costs in a timely, fair, and equitable manner? For example, should federal agencies be more consistent in determining what work is inherently governmental and, therefore should be performed by federal employees? For work that is not inherently governmental, should agencies be required to develop plans for competing this work in order to achieve measurable efficiencies and performance improvements?*

Performance, mission, cost, schedule, and other risks are inherent in major federal programs and investments such as weapons systems, homeland security, federal buildings and other infrastructure, transportation subsidies, environmental clean-up, and information

technology systems. Despite these risks, federal agencies often lack comprehensive risk management strategies that are well integrated with program, budget, and investment decisions. As one example among many, homeland security investments are designed to reduce risks to the nation's communities and assets, but the availability of a common set of analytical tools and procedures on how agency management should use them can be improved to better align the allocation of homeland security resources with risk-related measures, such as relative risk and risk reduction per dollar invested. Governmentwide guidance generally does not fully integrate risk management into all aspects of decision-making such as policy making, program planning, implementation, and monitoring. More broadly, the Congress and the executive branch face a series of difficult and contentious trade-offs as they re-examine, re-prioritize, and restructure the base of federal programs in response to current budget demands and long-term fiscal challenges and the changing risk profiles faced by programs and agencies change. As was discussed in section 1, much of the base of the federal government was put in place in response to the wants, needs, and affordabilities of an earlier era. For example, some risks to farmers and to the aging population as discussed elsewhere in this section have changed over the decades, as have the tools for evaluating and communicating risk about costs and other outcomes. A more thorough and disciplined approach to identifying and managing risk across the federal government could help in structuring and informing the daunting decisions that need to be made.

▶ *How could the federal government consistently apply a comprehensive risk management framework to help guide federal programs and apply resources efficiently and to best effect? For example, can the Office of Management and Budget and the Department of Homeland Security develop guidance for Homeland Security to better align federal investments in preparedness with the potential risk and threat facing the nation's assets and communities? To what extent should federal agencies, such as DOD or NASA, consider and report on the uncertainty of cost estimates for major procurements in budget requests? To what extent can changing risks be monitored across federal programs and how can these changes be used to review the base of ongoing federal commitments?*

A range of individual agencies need to successfully complete their specific transformation initiatives. For example, the U.S. Postal Service is under increasing financial pressure as the Internet, electronic bill payment, and growing competition from private delivery companies are changing the nation's communication and delivery sectors and adversely affecting mail volume. Yet the Postal Service's ability to address these challenges is hindered by an outmoded business model that relies on mail volume growth to cover rising costs. The service is working to cut costs, improve productivity, reduce its workforce, and make other needed changes, but it will need attention and support as it adapts a new and more competitive business model.

▶ *How should agencies, including the U.S. Postal Service, transform their services, infrastructure, legal framework, operations, and workforce to keep pace with rapid changes in technology as well as in the communications, labor, and other sectors of the economy?*

▶ *What are the specific leadership models that can be used to improve agency management and address transformation challenges? For example, should we create chief operating officer or chief management officer positions with term appointments within selected agencies to elevate, integrate, and institutionalize responsibility and authority for business management and transformation efforts?*

The government has not transformed, in many cases, how it motivates and compensates its employees to achieve maximum results within available resources and existing authorities. Even though people are critical to any agency's successful transformation, define its culture, develop its knowledge, and are its most important asset, a number of agencies still try to manage this asset with a "one-size-fits-all" approach. For example, employees are compensated through an outmoded system that (1) rewards length of service rather than individual performance and contributions, (2) automatically provides across-the-board annual pay increases, even to poor performers, and (3) compensates employees living in various localities without adequately considering the local labor market rates for these employees. To address these problems and provide the services the public expects, the federal civil service

system must be reformed governmentwide, and this reform must be guided by a set of consistent principles, criteria, and practices.

▶ *How should the federal government update its compensation systems to be more market-based and performance-oriented? For example, should poor performers be guaranteed pay increases? How can these systems ensure pay comparability and provide reasonable annual pay adjustments while also competing for critical occupations or in higher cost locations? In addition, how can the government make an increasing percentage of federal compensation "at risk" or dependent on achieving individual and organizational results by, for example, providing more compensation as one-time bonuses rather than as permanent salary increases?*

More than 30 federal agencies control about $328 billion in real property assets worldwide, and maintain a "brick and mortar" buildings and office presence in 11 regions across the nation. But this organization and infrastructure reflects a business model and the technological and transportation environment of the 1950s. Many of these assets are no longer needed; others are not effectively aligned with, or responsive to, agencies' changing missions; and many others are in an alarming state of deterioration, potentially costing taxpayers tens of billions of dollars to restore and repair. The Congress and several agencies have recognized and begun to address this issue, but this financial liability still looms.

▶ *In a modern society with advanced telecommunications and electronic information capabilities, does the government still need 11 regions? Which agencies still need a physical presence in all major cities?*

▶ *What opportunities exist to more strategically manage the federal government's real property assets, such as disposing of excess federal facilities or better leveraging surplus in the private sector to make the federal portfolio more relevant to current missions and less costly?*

Tax System Challenges in the 21st Century

American taxpayers paid about $1.9 trillion in combined federal taxes, including income, payroll, and excise taxes, in fiscal year 2004. These taxes, along with over $4 trillion in deficit borrowing, funded the federal government. The tax revenue raised represented about 16 percent of gross domestic product—at the low end of the range of federal taxes as a share of GDP for the last 40 years.

Beyond funding government, any tax system, including the current one, has profound effects on the economy as a whole and on individual taxpayers, both for today and tomorrow. Taxes affect decisionmaking throughout the economy, including decisions concerning how much and where to work, save, and invest. These decisions, in turn, affect economic growth and future income, and thus future tax revenues.

Concerns about the tax system's effect on future economic performance are one driver of the current debate about the future of that system. The U.S. position in the worldwide economy has fundamentally changed and the structure and composition of our economy has shifted. U.S. workers and firms must now succeed in a world of fast-paced technological change and constantly evolving global competition. Also, as noted in section 1, the imbalance between federal revenues and expenditures, if allowed to persist long term, will affect economic growth. Addressing the imbalance will require greater scrutiny of both tax revenues and expenditures.

The following challenges and illustrative questions provide a framework for thinking about these issues in the future.

The success of our tax system hinges very much on the public's perception of its fairness and understandability. Fairness is ultimately a matter of personal judgment about issues such as how progressive tax rates should be and what constitutes ability to pay. Fairness also depends on the extent to which taxpayers believe their friends, neighbors, and business competitors are complying with the tax laws and actually paying their taxes. Compliance is influenced by the effectiveness of the Internal Revenue Service's (IRS) enforcement efforts but also by Americans' attitudes about the tax system and government. Disturbing recent polls indicate that about 1 in 5 respondents say it is acceptable to cheat on their taxes.

▶ *Given our current tax system, what tax rate structure is most likely to raise sufficient revenue to fund government and satisfy the public's perception of reasonableness and fairness?*

▶ *How can we best strengthen enforcement of tax laws to give taxpayers confidence that their friends, neighbors, and business competitors are paying their fair share? For example, can we increase compliance with the tax laws and reduce the need for IRS enforcement activities through greater use of withholding and information reporting? Would improved compliance data allow IRS to better allocate its enforcement resources? Could increased penalties and disclosure reduce the use of abusive tax shelters?*

Over the years the federal tax system and especially the federal income tax has become more complex, less transparent, and subject to frequent revision. Some complexity is understandable in an economy as diverse and sophisticated as ours. However, tax system complexity and frequent revisions make it more difficult and costly for taxpayers who want to comply to do so and for IRS to explain and enforce the tax laws. Many argue that complexity creates opportunities for tax evasion, through vehicles such as tax shelters, which in turn motivate further changes in tax laws and regulations and perhaps more complexity. A lack of transparency also risks creating disrespect for the tax system and the government.

▶ *What opportunities exist to streamline and simplify the current tax system and thereby make it more transparent to taxpayers, reduce opportunities for tax evasion, and decrease the compliance burden on taxpayers? For example, can the Alternative Minimum Tax be eliminated? Can the Earned Income Tax Credit eligibility rules be simplified? Could the measurement of income be simplified?*

The growing complexity of the tax system stems in part from the extensive use of tax incentives to promote social and economic objectives. The tax system includes hundreds of billions of dollars of such incentives—the same magnitude as total discretionary spending. For instance, the Low Income Housing Tax Credit is the federal government's largest program for creating new affordable housing units and the Earned Income Credit is its largest cash assistance program for low-income families. However, tax

incentives do not compete in the annual budget process and effectively are "fully funded" before any discretionary spending is considered. Further, relatively little is known about the effectiveness of tax incentives in achieving the objectives intended by the Congress. As far back as 1994, GAO concluded these incentives deserved more scrutiny.

▶ *Which tax incentives need to be reconsidered because they fail to achieve the objectives intended by the Congress, their costs outweigh their benefits, they duplicate other programs, or other more cost-effective means exist for achieving their objectives? For example, could health-related tax incentives, including the treatment of employer-provided health insurance, which has been estimated to be over $180 billion in both income and certain payroll taxes, be better used to promote broader health care access, more efficient health care delivery, and more effectively control costs?*

▶ *Rather than reconsider specific types of tax incentives, is it time to consider another 1986-style tax reform (broadening and simplifying the tax base by eliminating many tax preferences thus allowing tax rates to be minimized)?*

Incentives for savings are a particular concern. Private sector savings are near historical lows and government savings, due to federal budget deficits, are negative. Low rates of domestic saving force the nation to rely on foreign lenders to finance new investment. The tax code includes many incentives intended to increase savings to finance retirement, health care, higher education, and so on. These savings incentives, which exempt some income from tax, have moved the current tax system in the direction of a consumption base. These incentives, however, are complex and, although not completely settled, researchers have raised questions about how much, if any, net new savings they stimulate.

▶ *How effective are existing tax incentives at increasing savings for their targeted purposes? How effective are they at increasing overall national savings? Could the myriad savings incentives (IRAs, health savings accounts, several education savings incentives, etc.) that complicate the current tax system be consolidated and simplified while promoting increased savings?*

The debate about the future tax system is partly about whether the goals for the nation's tax system can be best achieved using the current structure, which is heavily dependent on income taxes, or a fundamentally reformed structure, which might include more dependence on consumption taxes, a flatter rate schedule, and fewer tax incentives. Increasing globalization, which makes it easier to move assets, income, and jobs across international borders, is another motivator for the debate. As policymakers grapple with such issues, they will have to balance multiple objectives such as economic growth, equity, simplicity, transparency, and administrability while raising the needed revenue. The appropriate balance among these objectives may also be affected by (1) how, if at all, to take into account that, including both the employer and the employee share, an estimated two-thirds of taxpayers would pay more in 2004 in payroll taxes—which are levied to fund social security and Medicare benefits—than they pay in income taxes and (2) whether and how to tax wealth.

▶ *Is the federal income-based tax system sustainable and administrable in a global economy? How should we tax the income of U.S. multinational corporations that is earned outside of the U.S.?*

▶ *Should the basis of the existing system or any new reforms be changed from an income to a consumption base (today we actually have a hybrid system)? Would such a change help respond to challenges posed by demographic, economic, and technological changes? How would such a change affect savings and work incentives?*

▶ *Regardless of whether a consumption tax is created, the current income tax is revised, or other fundamental tax system changes are made, how should the burden be allocated among taxpayers? Who should pay more and who should pay less? How can burden be distributed according to policymakers' decisions while minimizing complexity and preserving the desired benefits of any fundamental tax policy changes?*

▶ *How would the interrelationships between the federal and state and local tax systems and with the payroll tax system be taken into account when changing the federal tax system? How should wealth be taxed, if at all, in either an income or consumption based tax system and in any conversion to a consumption tax? How should transfers of wealth be taxed, if at all?*

Section 3: Where Do We Go From Here?

The reexamination questions posed in this report constitute both a challenge and an opportunity. Given the size of the fiscal imbalances looming in the future, business as usual will not suffice. The real question is not whether we deal with the fiscal imbalance, but how and when. Our policy process will be challenged to act with more foresight to take early action on problems that may not constitute an urgent crisis but pose important longer term threats to the nation's fiscal, economic, security, and societal future. To address these issues, policymaking institutions will also be challenged to shift from the traditional focus on incremental changes in spending or revenues to look more fundamentally at the underlying relevance, relative priority and results of various federal programs, policies, functions, and activities in addressing current and emerging national needs and problems across all major areas of the federal budget—discretionary spending, entitlements and other mandatory spending, and tax policies and programs.

While not easy, the periodic reexamination of existing portfolios of federal programs offers the prospect of weeding out ineffective or outdated programs while strengthening and updating those programs that are retained. Thus, such a process addresses not only fiscal imbalances but also can improve the responsiveness and effectiveness of government in addressing 21st century needs and challenges. As discussed in section 1 of this report, the nation's current fiscal policy path is unsustainable. The questions posed in section 2 of this report can be considered as one input among many that Congress will receive as it decides how to address these issues. While answers can draw on the work of GAO and others, only elected officials can and should decide whether, how, and when to move forward.

Fiscal Challenges Prompt the Need for a New Approach

The stakes associated with federal programs are large, both for beneficiaries of those programs and the nation's taxpayers. These programs serve important constituencies and provide significant current benefits. Accordingly, challenging the underlying basis, rationale, and results achieved by these programs is never simply an analytic exercise, but rather a political process involving players with strongly felt views and differing interests.

The conflicts and uncertainties entailed in budgeting and policymaking are often mitigated by focusing decisions on incremental changes in resources each year. As a result, this incremental process focuses disproportionate attention on proposed changes to existing programs and proposals for new programs, with the base of programs being taken as "given." This traditional process helps ensure stability and certainty in federal funding commitments and helps target the limited time and attention of policymakers on new proposals or proposals to change existing activities. While this approach may be appropriate in periods of stability and fiscal strength, it may be insufficient during a time of change and fiscal challenge.

Moreover, the process routinely examines only the one-third of federal spending subject to the annual appropriations process. By definition, entitlement programs and tax expenditures are generally not reviewed or reauthorized annually, and many of these programs are not even subject to periodic reauthorization to ensure that they are periodically reviewed. As the nation enters a period when the existing portfolio of programs is unaffordable and unsustainable at current levels of taxation, a more fundamental review of all major existing spending and tax policies and programs is not only appropriate but essential.

The size of the problem is so large that across-the-board approaches to distributing cuts broadly across many individual programs and accounts cannot really work. In addition, such approaches can result in retaining fat while cutting muscle—specifically, across-the-board cuts risk cutting effective programs while leaving ineffective, outdated, or lower priority programs in the base. An across-the-board approach also constitutes a missed opportunity to address at a fundamental level the drivers of long-term deficits. Given the size of the long-term fiscal imbalances, all major spending and revenue programs in the budget should be subject to periodic reviews and reexamination. While it is important to focus on the major programs driving the long-term outlook—Medicare, Medicaid and Social Security—our recent fiscal history suggests that exempting major areas from reexamination and review can undermine the credibility and political support for the entire process. Given the

size of the long-term fiscal imbalances, it is highly unlikely that this problem can be "solved" by reforms in any one sector.

Building Support for a Reexamination Process

We recognize that reexamining the base is a challenging process for both leaders and stakeholders alike. Just as the traditional process limits choices and political conflict, putting entire programs up for review periodically can increase the stakes and conflict associated with budget decisions. Accordingly, a process to review established programs and priorities will need to be supported by a strong and publicly compelling rationale.

The challenge for leaders is to frame the fiscal challenges as something with important consequences for the values and interests that affect American citizens, both now and in the future. As participants at GAO's recent budget forum noted, leaders have been able to make a compelling case for fiscal sacrifice before, but it is never easy.[3] While current deficits are troubling, they are but a prelude to the daunting long-term fiscal challenges highlighted in section 1 that are significant, structural and unsustainable in nature. However, long-term issues can be difficult to address, particularly when the most significant impact is beyond the 10 year baseline time horizon.

Effective and sustained leadership will be necessary to gain support among the public and other key players for addressing these long-term fiscal issues. Taking a long-term perspective can provide important dividends for leaders in making the case to the broader public for initiating a reexamination process sooner rather than later. Early action can turn the power of compounding from an enemy to an ally, as reduced deficits usher in reduced debt, interest costs and economic growth. Moreover, early action can enable leaders to phase in changes over many years to permit future program beneficiaries to more easily adjust to policy changes by altering their own private choices for savings, retirement, or other issues. Finally, reexamination can also be used as a way to free funding for new

[3]GAO, *Comptroller General's Forum: The Long-Term Fiscal Challenge*, GAO-05-282SP (Washington, D.C.: February 2005).

programs and investments, thereby providing more immediate support for the exercise.

Perhaps the most compelling reason to begin the review process now is the dire consequences of waiting for a crisis. If we wait for deficits to rise to levels that seriously alarm markets or other economic actors to the point of approaching or reaching a "tipping point," the nation will be forced to adopt major and precipitous policy actions that would have significant disruptive consequences for the lives of retirees and workers alike.

Given the severity of the nation's fiscal challenges and the wide range of federal programs, the hard choices that need to be considered may take a generation to address. Beginning the reexamination and review process now would enable decision makers to be more strategic and selective in choosing areas for review over a period of years. Reexamining selected parts of the budget base, over time rather than all at once, will lengthen the process, but it may also make the process more feasible and less burdensome for decision makers. And by phasing in change to programs or policies that might otherwise have prohibitively high costs of transition, the burden of change can be spread out over longer time periods.

Notwithstanding the challenges associated with reexamination, reviewing the base of programs and operations has ample precedent. The federal government, in fact, has reexamined and reformed selected programs and priorities in the past. From a programmatic perspective, such reexaminations have included, for example, the 1983 Social Security reform, the 1986 tax reform, and the 1996 welfare reform. They have also included reforms such as the creation of the Department of Homeland Security and, most recently, the ongoing reorganization of the U.S. intelligence community. From a broader fiscal standpoint, the 1990s featured significant deficit reduction measures adopted by the Congress and supported by the President that made important changes to discretionary spending, entitlement program growth, and revenues that helped eliminate deficits and bring about budgetary surpluses.

Some may be skeptical as to whether our political system is able to address long-term problems or commitments. However, such skepticism ignores past examples of attention to long-term goals. The interstate highway program took a generation to plan and complete. The Social Security system was created with very long time horizons in mind and has undergone major restructuring in both 1977 and 1983, with an eye toward improving the program's longer-term sustainability. As a nation, we also anticipated, and as a result met, the educational capacity needs of the baby boom all the way from primary school to college.

States and other nations also have engaged in reexamination exercises. States have variously examined their bases, through cutback management, performance and strategic planning, budget reform, and privatization/contracting out. In recent years, various states have reexamined their various programs and priorities through such mechanisms as efficiency commissions and reprioritization exercises. For instance, the state of Washington adopted what it calls a statewide results-based approach to budgeting called "Priorities of Government" to address a budgetary shortfall of $2.4 billion for the 2003-2005 biennium. Under this system, programs and activities were reviewed and ranked based on their relative contribution to eleven broader performance goals, leading to cuts for programs below the line of available revenues.

Other nations, too, have undertaken comprehensive reexamination efforts. New Zealand, Australia, Canada, and the Netherlands, for example, have undergone performance-based budgeting and performance management reforms aimed at reprioritizing the base of their respective governmental activity and budget that spanned a number of years. In Canada, an OECD study concluded that a program review exercise delivered $18.8 billion in savings above previously-planned reductions (cumulative over 3 years) announced in the 1995 and 1996 budgets and to that extent certainly contributed to achieving—and in fact exceeding—the original deficit-to-GDP target of 3 percent by 1996-97. In the Netherlands, reconsideration reviews are conducted on particular programs selected for each budget cycle, with participation by working groups of central budget and departmental staff as well as external experts, resulting in a public report with recommendations to be considered

in the budget process. According to OECD, the process has been in place since 1981 and has lead to significant savings as well as many reforms of major policy areas.[4]

Multiple Approaches Can Facilitate Reexamination

In our system a successful reexamination process will in all likelihood rely on multiple approaches over a period of years. Rules and process can play a role in facilitating decisions and supporting leaders in making tough choices. However, processes cannot by themselves force decisions. Leadership, a sense of stewardship for the future, and an agreement that tough choices and meaningful actions are required and essential for success.

Some congressional observers believe a deceptively simple approach may hold the most promise: reliance on the existing reauthorization, oversight, appropriations, and budget processes. They have been deployed to review and change existing programs on a selective or episodic basis, but each also is perceived to have certain constraints that have prompted calls for change:

- *The reauthorization process.* The reauthorization process affords the Congress the opportunity to probe into the effectiveness of a program and to terminate or make any changes before providing funding for the reauthorized program. Reauthorization is the purview of authorizing committees in the Congress and authorizations generally precede appropriations. However, some programs have authorizations that are permanent and do not expire while others are subject to periodic reauthorizations, are funded by permanent appropriations, such as the Veterans Affairs Pensions Benefits program. Furthermore, concerns have been expressed that the authorization process has increasingly been made less effective by the continuation of funding in appropriations bills even when programs' authorizations have expired, such as the Federal Bureau of Investigation (FBI) and the Federal Prison System, which were funded in fiscal year 2005 with expired authorizations of appropriations.

[4]Organisation for Economic Co-operation and Development, *Reallocation: The Role of Budget Institutions* (GOV/PUMA/SBO (2003)15), May 16, 2003.

- *The oversight process.* Although oversight can and does occur with authorizations and appropriations, the Congress also has a separate oversight process available outside the traditional reauthorization/appropriations discussions. This oversight process provides the Congress the means to hold agencies accountable for the economy, efficiency, and effectiveness of existing policies, programs, and agency operations. The committees primarily responsible for exercising this oversight are the Senate Committee on Homeland Security and Governmental Affairs and the House Committee on Government Reform, although authorizing committees also engage in oversight reviews and hearings in connection with matters within their jurisdiction. GAO and agencies' inspectors general support congressional oversight with analysis, evaluations, investigations, and reviews of various programs and operations. Concerns have been expressed by a number of observers regarding the need to increase attention to oversight in the Congress and the lack of legislative follow-through for findings of oversight investigations and hearings.

- *The appropriations process.* For the approximately one-third of the federal budget that is subject to the annual appropriations process, this process gives the Congress the opportunity to annually review programs and operations. Although this process does not touch the major drivers of the long-term deficit (e.g., Medicare, Medicaid, Social Security) it does cover programs important to citizens and the nation (e.g., defense, homeland security, health research, transportation, national parks, education, environment). The squeeze created by the growth in mandatory spending increases the need to ensure that this part of the budget is reexamined and adapted to the 21st century.

- *The budget process.* The congressional budget process is the annual vehicle through which the Congress articulates both an overall fiscal stance—overall targets for spending and revenue—and its priorities across various broad categories. The process provides the overall constraints for spending and revenue actions by the Congress for each year and the rules of procedure that can be used to constrain new entitlement and tax legislation not

assumed in the annual budget resolution. Directions contained in the budget resolution for reconciliation legislation trigger the review of existing programs by directing congressional committees to propose cuts to meet savings targets contained in the resolution. The budget rules that were grounded in statute—including discretionary spending caps and "PAYGO" limits on mandatory spending and tax cuts—and enforced by executive actions if violated, expired at the end of fiscal year 2002; the only constraints are those contained and enforced through congressional budget resolutions, and reinforced by points of order.

Other specific approaches and processes have been proposed to supplement the existing congressional processes and entities. While these are generally aimed at addressing perceived limitations with existing processes and to prompt greater incentives or support for review and reexamination, each have their own set of potential benefits as well as limitations that have historically constrained their use or success:

- *Special temporary commissions.* Special temporary commissions have been convened to formulate recommendations for specific policy or functional areas. Temporary commissions are appealing because they provide a safe haven for developing policy alternatives, often are bipartisan in nature, may involve both executive and legislative branch representatives, and typically include experts both within and outside of government. Most commissions are designed to address issues in a timely manner and then are dissolved. Commissions can be very promising, but their ultimate success depends on the extent to which the Congress and the executive branch agree about the need for action, on the need to use a nontraditional approach to reach agreement or to develop a specific proposal, and on their general willingness to address the recommendations of such commissions. This can be seen in the differing results of some examples: Social Security reform (e.g., Greenspan Commission and Moynihan Commission), terrorism and intelligence reform (e.g., 9-11 Commission), military base realignment and closures (e.g., BRAC Commission), and Medicare (e.g., Breaux Commission).

- *Sunset provisions.* Proposals have been made to institute across-the-board provisions terminating all existing programs after a certain number of years to trigger their reexamination. Although numerous specific programs contain fixed period authorizations that are like sunset provisions, such as the federal highway funding and the Temporary Assistance for Needy Families (TANF) program, a broad federal sunset law has never been adopted. Concerns about this approach include the burden of a crosscutting provision and the lack of targeting those programs most in need of reexamination. In addition, some have noted that fixed-period authorizations are, in effect, sunset provisions. The reauthorization process can offer the same opportunity for reexamination—and if appropriations are not forthcoming in the absence of a reauthorization, then fixed-term authorizations effectively constitute sunsets.

- *Executive reorganization authority.* In the past, the Congress has provided the president with authority to propose and gain fast-track consideration of changes in structures and responsibilities of federal agencies and programs. However, such authority has been progressively limited over the years. The fundamental issue raised by granting reorganization authority to the President is whether and how the Congress wishes to change the nature of its normal deliberative process when addressing Presidential proposals to restructure the federal government. The Congress may want to consider different tracks for proposals that propose significant policy changes versus those that focus more narrowly on government operations.

- *Biennial Budgeting.* Shifting appropriations to a biennial cycle has been proposed as a way to promote more systematic congressional oversight and review in the "off" year. However, skeptics note that whether this reform in fact frees more congressional time depends on whether the budget remains relatively unchanged during the off year. The Congress has been passing annual supplemental appropriations in recent years and this is expected to continue for several more years. Moreover, some argue that reducing appropriations reviews to once every other year would serve to reduce the opportunities for the Congress to routinely examine and review programs and

executive operations. Although some states use biennial budgeting (e.g., Texas, Connecticut, and Ohio), their experiences are mixed, with the governor having more budgeting power than the President.

Performance and analytic tools may be as important as or more important than specific process reforms in facilitating reexamination. In this regard, the performance metrics and plans ushered in by the Government Performance and Results Act of 1993 (GPRA) have led to a growing supply of increasingly sophisticated measures and data on the results achieved by various federal programs. Agencies and OMB have been working over the years to strengthen the links between this information and the budget. Under the Program Assessment Rating Tool (PART), for example, OMB plans to rate the effectiveness of each program in the budget over a 5-year period.

While these initiatives provide a foundation for a baseline review of federal policies, programs, functions, and activities, several changes are in order to support the type of reexamination we have in mind. First, the PART focus on individual programs will provide important new assessments, but it needs to be supplemented by a more crosscutting assessment of the relative contribution of portfolios of programs and tools to broader outcomes. Most key performance goals of importance—ranging from low income housing to food safety to counterterrorism—are addressed by a wide range of discretionary, entitlement, tax, and regulatory approaches that cut across a number of agencies. While OMB is moving to include some crosscutting assessments in the fiscal year 2006 PART, fully developing the governmentwide performance plan provided for under GPRA would provide a more systematic vehicle for addressing the performance of programs cutting across agencies to broader goals. Second, the Congress could consider the need to focus its oversight and review on these important overarching goals and missions by considering adopting a performance agenda of its own. One potential approach we have suggested is a performance resolution that could be included as part of the annual budget resolution to help target congressional activity on key program areas or performance problems. Once program areas or problems are selected, special collaborative initiatives among GAO, CRS, CBO,

IGs, and even OMB could be undertaken to identify and evaluate various performance issues and alternatives for congressional consideration, including identifying specific programs ripe for reorganization, consolidation, or other reforms.

Conclusion

As the foregoing discussion suggests, there are a range of available reexamination approaches and strategies. Assuming that reexamination is pursued by the Congress adopted as a congressional objective, we suggest that the challenge for the Congress is at least threefold: (1) building support within the Congress itself, the Administration, and ultimately the broader public to justify a base-line reexamination of existing federal policies, programs, functions, and activities as discussed in section 1, (2) identifying those areas that congressional and executive leaders agree need review along the lines of the illustrative questions offered in section 2, and (3) choosing reexamination approaches and strategies that are appropriate for the particular areas being examined as discussed in this section.

The choice among reexamination approaches will be informed by many factors. Initially, the choice of reexamination tools or approaches may be determined depending on such factors as how frequently an issue arises and the degree of political support and complexity. For example, a commission may be well suited to moving along ideas for problems that occur infrequently and that require "cover" to reach political agreement, such as Social Security reform. The reauthorization and oversight processes may be better suited for problems that occur more frequently, but not every year, as is the case with TANF reauthorization and oversight hearings on the activities of federal agencies. The appropriations process may be more conducive to policy matters requiring congressional action every year, such as the funding of national defense. In fact, a mix of different approaches has often been used to reexamine and reform specific policy areas in the recent past, as shown in figure 5.

Figure 5: Selected Reforms and Reexamination Approaches

Congress has enacted major reforms in recent years which were promoted and considered through the use of various reexamination processes and tools

Intelligence reform—The Intelligence Reform and Terrorism Prevention Act of 2004 aimed to unify, coordinate, and make more effective the U.S. intelligence community. Congress drew on the reexamination agenda put forward by the National Commission on Terrorist Attacks Upon the United States (9-11 Commission), in developing the actual legislation through its committee system.

Department of Homeland Security—The Homeland Security Act of 2002 brought together 22 organizations and created the Department of Homeland Security. In its proposal for a Department of Homeland Security, the President included several provisions similar to those proposed by reexamination effort of the U.S. Commission on National Security/21st Century (Hart-Rudman Commission). Congress tailored the actual legislation following hearings and consideration by its authorizing and oversight committees.

Farm reform—The Federal Agriculture Improvement and Reform Act of 1996 changed the federal government's approach to farm support from a policy based on managing crop production and supporting farm income to a policy that allows producers flexibility in what they plant. The need for new legislation was triggered by the provision in permanent law that would have rebased subsidies to levels authorized in 1949-leading to higher subsidies and federal costs.

Social Security reform—The 1983 Amendments to the Social Security Act made changes in Social Security coverage, financing, and benefit structure. The reform was made necessary by projections showing insufficient fund assets to pay all benefits. A bipartisan executive-legislative commission developed the proposal that led to legislation receiving widespread bipartisan congressional support.

Source: GAO.

Other important factors that will drive the specific approaches used include the public's readiness and familiarity with the issues being reexamined, the need for some kind of budgetary constraint or incentive to prompt review, the desire for consensus among stakeholders, and the stage of development of the issue itself.

Figure 6 demonstrates how different approaches might be appropriate at differing stages of the development of an issue, ranging from the need to simply raise awareness about the related, perhaps not widely perceived, reexamination issues all the way to the need to develop specific proposals for dealing with relatively well-defined problems. Studies by GAO or other independent and qualified organizations could be used to raise public awareness of issues and problems ("agenda setting"). Congressional hearings and other forums (e.g., regional sessions) could be used to educate the broader public about the need for change. When prioritizing the issue among other concerns, the Congress might use the occasion of the annual budget resolution, the oversight agenda, or perhaps

develop a new performance resolution to rank its reexamination and review priorities. For developing policy proposals, the Congress can rely on existing authorization processes, or can rely on a temporary special commission to develop new policy proposals or recommendations for particularly complex or controversial areas. As a reexamination unfolds, then, a combination of approaches may be needed.

Figure 6: Reexamination Maturity Model

Different developmental stages of reexamination	May require…	Different reexamination approaches, such as:
• *Agenda setting*—raising awareness of issues by collecting information and defining the nature, timing and scope of new issues and problems with existing programs.	→	• Studies by GAO or other independent and qualified organizations
• *Educating*—informing the broader public about need for change.	→	• Congressional hearings or other forums
• *Prioritizing and aggregating*—validating the basis for problem definition, and prioritizing and grouping assessments of current programs.	→	• Leadership prioritization initiatives • Annual congressional budget resolution/oversight agenda
• *Developing policy proposals*—providing a menu of options, exploring differences, making recommendations.	→	• Temporary special commissions • Reauthorization process • Executive reorganization authority

Source: GAO.

Regardless of the specific combination of reexamination approaches adopted, the ultimate success of this process will depend on several important overarching conditions

- Sustained leadership to champion changes and reforms through the many stages of the policy process.
- Broad based input by a wide range of stakeholders.
- Reliable data and credible analysis from a broad range of sources that provides a compelling fact based rationale for changing the base of programs and policies for specific areas.

- Clear and transparent processes for engaging the broader public in the debate over the recommended changes.

In conclusion, our nation faces large, growing and structural long-term fiscal imbalances that we cannot simply grow our way out of. Rather, hard choices based on a fundamental reexamination of government policies, programs, functions, and activities will be necessary in order to address our long-term fiscal imbalance. This will include consideration of what the federal government should do, how it should do business, and how it should be financed in the future. The resolution of these problems must invariably entail difficult political choices among competing programs that promise benefits to many Americans but are collectively unaffordable at current revenue levels. However, given the fiscal challenges, a reexamination of government can be expected, whether initiated through a public decision making process or forced on us by a crisis.

The questions provided in this volume are designed to illustrate the kinds of issues that such a review can address, not the answers that such a process will reach. Such a review will be difficult and the process may take a generation or more to unfold. The reexamination process will in fact proceed through various processes and venues. However, the nation will be better served if such a process begins sooner rather than later.

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