

United States Government Accountability Office

*Saving*  
**Our Future**  
*requires*  
**Tough Choices Today**

**National Conference of State Legislatures Annual Meeting  
August 18, 2006**

**The Honorable David M. Walker  
Comptroller General  
of the United States**



**GAO-06-1075CG**

# Fiscal Year 2004 and 2005 Deficits and Net Operating Costs

	Fiscal Year 2004	Fiscal Year 2005
	(\$ Billion)	
On-Budget Deficit	(568)	(494)
Off-Budget Surplus*	155	175
Unified Deficit	(413)	(318)
Net Operating Cost	(616)	(760)

\*Includes \$151 billion in fiscal year 2004 and \$173 billion in fiscal year 2005 in Social Security surpluses and \$4 billion in fiscal year 2004 and \$2 billion in fiscal year 2005 in Postal Service surpluses.

Sources: The Office of Management and Budget and the Department of the Treasury.

# Estimated Fiscal Exposures

(\$ trillions)

	2000	2005
<b>• Explicit liabilities</b>	<b>\$6.9</b>	<b>\$9.9</b>
<ul style="list-style-type: none"> <li>• Publicly held debt</li> <li>• Military &amp; civilian pensions &amp; retiree health</li> <li>• Other</li> </ul>		
<b>• Commitments &amp; contingencies</b>	<b>0.5</b>	<b>0.9</b>
<ul style="list-style-type: none"> <li>• E.g., PBGC, undelivered orders</li> </ul>		
<b>• Implicit exposures</b>	<b>13.0</b>	<b>35.6</b>
<ul style="list-style-type: none"> <li>• Future Social Security benefits</li> </ul>	3.8	5.7
<ul style="list-style-type: none"> <li>• Future Medicare Part A benefits</li> </ul>	2.7	8.8
<ul style="list-style-type: none"> <li>• Future Medicare Part B benefits</li> </ul>	6.5	12.4
<ul style="list-style-type: none"> <li>• Future Medicare Part D benefits</li> </ul>	--	8.7
<b>Total</b>	<b>\$20.4</b>	<b>\$46.4</b>

Source: U.S. government's consolidated financial statements (CFS).

Note: Estimates for Social Security and Medicare are at present value as of January 1 of each year as reported in the CFS and all other data are as of September 30.

# How Big is Our Growing Fiscal Burden?

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

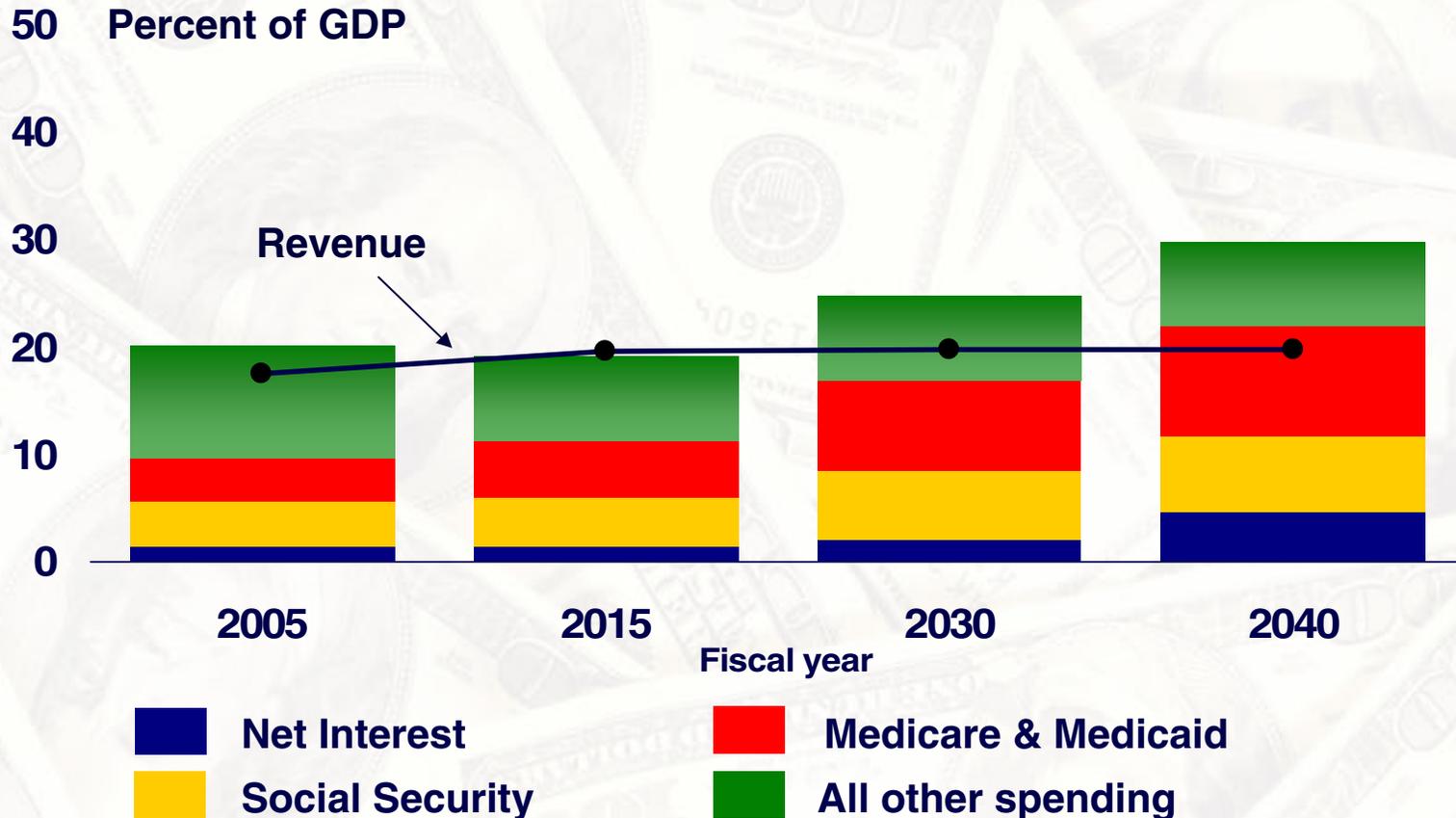
<b>Total fiscal exposures</b>	<b>\$46.4 trillion</b>
<b>Total household net worth<sup>1</sup></b>	<b>\$51.1 trillion</b>
<b>Burden/Net worth ratio</b>	<b>91 percent</b>
<b>Burden<sup>2</sup></b>	
<b>Per person</b>	<b>\$156,000</b>
<b>Per full-time worker</b>	<b>\$375,000</b>
<b>Per household</b>	<b>\$411,000</b>
<b>Income</b>	
<b>Median household income<sup>3</sup></b>	<b>\$44,389</b>
<b>Disposable personal income per capita<sup>4</sup></b>	<b>\$30,431</b>

Notes: (1) Federal Reserve Board, Flow of Funds Accounts, Table B.100, 2005:Q3 (Dec. 8, 2005); (2) Burdens are calculated using total U.S. population as of 9/30/05, from the *U.S. Census Bureau*, full-time workers for 2004, reported by the Bureau of Economic Analysis, in NIPA table 6.5D (Aug. 4, 2005); and households for 2004, reported by the U.S. Census Bureau, in *Income Poverty & Health Insurance Coverage in the US: 2004* (Aug. 2005); (3) U.S. Census Bureau, *Income Poverty & Health Insurance Coverage in the US: 2004* (Aug. 2005); and (4) Bureau of Economic Analysis, *Personal Income and Outlays: October 2005*, table 2, 2005:Q3, (Dec.1, 2005).

Sources: GAO analysis.

# Composition of Spending as a Share of GDP

## Under Baseline Extended

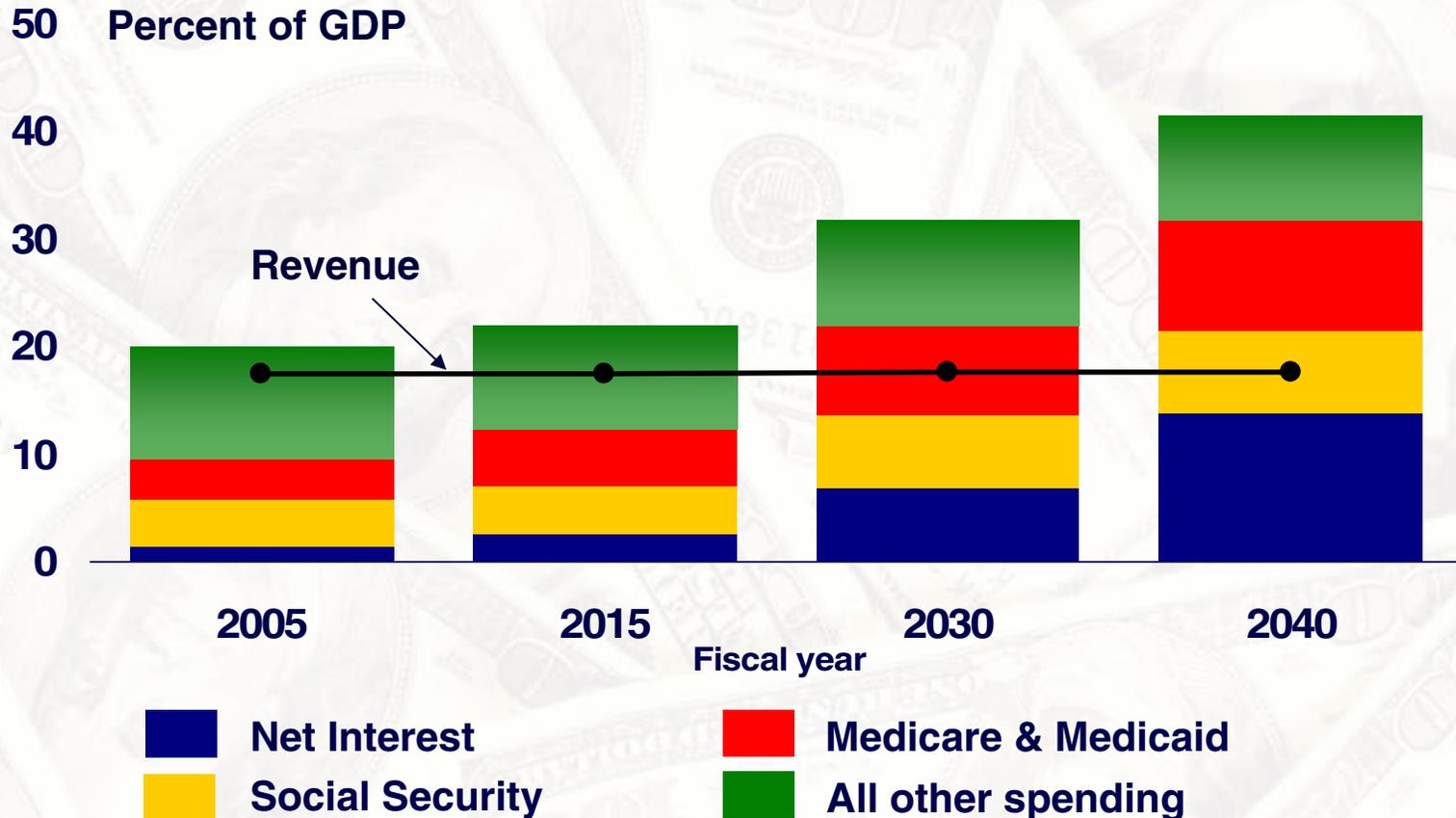


Notes: In addition to the expiration of tax cuts, revenue as a share of GDP increases through 2016 due to (1) real bracket creep, (2) more taxpayers becoming subject to the AMT, and (3) increased revenue from tax-deferred retirement accounts. After 2016, revenue as a share of GDP is held constant.

Source: GAO's May 2006 analysis.

# Composition of Spending as a Share of GDP

Assuming Discretionary Spending Grows with GDP after 2006  
and All Expiring Tax Provisions are Extended



Note: This includes certain tax provisions that expired at the end of 2005, such as the increased AMT exemption amount.

Source: GAO's May 2006 analysis.

# Current Fiscal Policy Is Unsustainable

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

- We face large and growing structural deficits largely due to known demographic trends and rising health care costs.
- GAO’s simulations show that balancing the budget in 2040 could require actions as large as
  - Cutting total federal spending by 60 percent or
  - Raising federal taxes to 2 times today's level

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

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

# Selected State Fiscal Challenges

## **States have many of their own fiscal challenges, including:**

- Unsustainable Medicaid cost increases
- Unfunded liabilities of state retirement systems (e.g. pensions and health)
- Education funding squeezed by competing demands
- Infrastructure maintenance and expansion needs given unparalleled sprawl and congestion
- Emergency preparedness response and recovery needs (e.g. natural disaster, terrorist incident, pandemic flu)

**GAO has ongoing work examining total national fiscal exposure (federal, state, and local).**

# The Way Forward: A Three-Pronged Approach

1. Strengthen Budget and Legislative Processes and Controls
2. Improve Financial Reporting and Performance Metrics
3. Fundamental Reexamination & Transformation for the 21<sup>st</sup> Century

*Solutions Require Active Involvement from Both the Executive and Legislative Branches*

# The Way Forward: Strengthen Budget and Legislative Processes and Controls

- Restore discretionary spending caps & PAYGO rules on both sides of the ledger
- Develop mandatory spending triggers [with specific defaults], and other action-forcing provisions (e.g., sunsets) for both direct spending programs and tax preferences
- Develop, impose & enforce modified rules for selected items (e.g., earmarks, emergency designations, and use of supplementals)
- Require present value cost estimates for any legislative debate on major tax and spending bills. Cost estimates should usually assume no sunset
- Extend accrual budgeting to insurance & federal employee pensions; develop techniques for extending to retiree health & environmental liabilities

# The Way Forward:

## Improve Financial Reporting and Performance Metrics

- Improve transparency & completeness of President's budget proposal:
  - Return to 10-year estimates in budget both for current policies and programs and for policy proposals
  - Include in the budget estimates of long-term cost of policy proposals & impact on total fiscal exposures.
  - Improve transparency of tax expenditures
- Consider requiring President's budget to specify a path to on-budget balance within 10-year window or explain the selection of an alternative deadline
- Require annual OMB report on existing fiscal exposures [liabilities, obligations, explicit & implied commitments]
- Require enhanced financial statement presentation and preparation of summary annual report that is both useful and used
- Develop key national (outcome-based) indicators to chart the nation's position, progress, and position relative to the other major industrial countries

# The Way Forward: Fundamental Reexamination & Transformation

- Restructure existing entitlement programs
- Reexamine and restructure the base of all other spending
- Review & revise existing tax policy, including tax preferences & enforcement programs
- Expand scrutiny of all proposed new programs, policies, or activities
- Strengthen internal agency structures & processes
- Strengthen and systematize Congressional oversight processes

# Key National Indicators

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

# Key National Indicators: Where the United States Ranks

The United States may be the only superpower, but compared to most other OECD countries on selected key economic, social, and environmental indicators, on average, the U.S. ranks

# 16 OUT OF 28

## OECD Categories for Key Indicators (2006 OECD Factbook)

• Population/Migration	• Energy	• Environment	• Quality of Life
• Macroeconomic Trends	• Labor Market	• Education	• Economic Globalization
• Prices	• Science & Tech.	• Public Finance	

# Moving the Debate Forward

- **The Sooner We Get Started, the Better**

- The miracle of compounding is currently working against us
- Less change would be needed, and there would be more time to make adjustments
- Our demographic changes will serve to make reform more difficult over time

- **Need Public Education, Discussion, and Debate**

- The role of government in the 21<sup>st</sup> Century
- Which programs and policies should be changed and how
- How government should be financed

**These Challenges Go Beyond  
Numbers and Dollars—  
It's About**

**VALUES & PEOPLE**



# Key Leadership Attributes Needed for These Challenging and Changing Times

- ***Courage***
- ***Integrity***
- ***Creativity***
- ***Stewardship***

...NOW WE COVER IT WITH STICKS AND LEAVES SO THEY WON'T NOTICE IT UNTIL IT'S TOO LATE.

SOMEHOW, YOU DON'T EXPECT PARENTS TO BEHAVE LIKE THAT.



The Deficit

CHECK THE CLIMATE FORECAST.

TOLES

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## On the Web

Web site: [www.gao.gov/cghome.htm](http://www.gao.gov/cghome.htm)

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