



THE NATION'S
GROWING
Fiscal Imbalance

GAO's Strategic Plan



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

MISSION

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

THEMES

- Long-Term Fiscal Imbalance
- National Security
- Global Interdependence
- Changing Economy
- Demographics
- Science and Technology
- Quality of Life
- Governance

GOALS & OBJECTIVES

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

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

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

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

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

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

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

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

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

CORE VALUES

Accountability

Integrity

Reliability

GAO's High-Risk List

2005

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

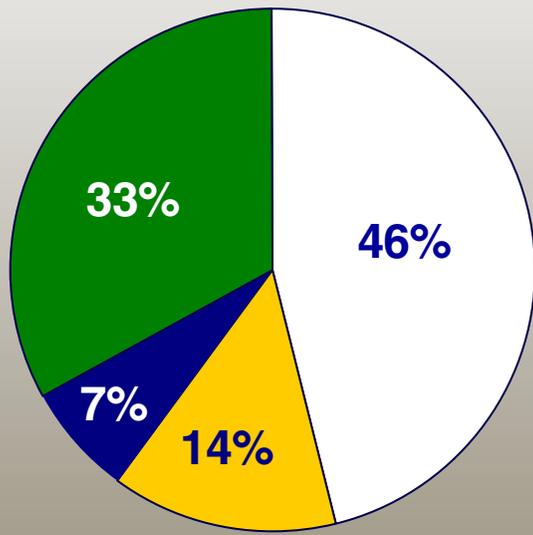
^a Legislation is likely to be necessary, as a supplement to actions by the executive branch, in order to effectively address this high-risk area.

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

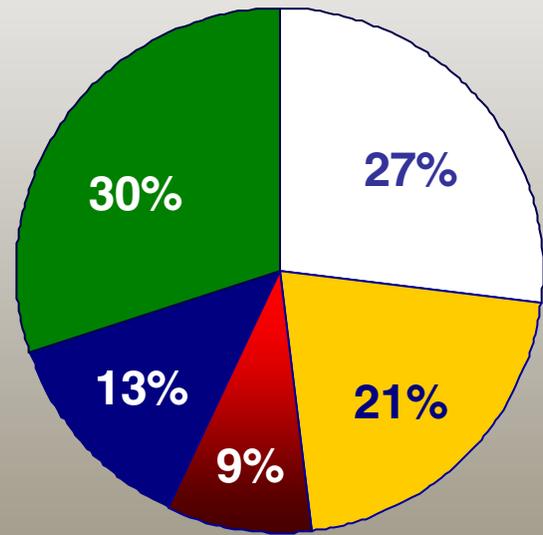
^c The IRS Financial Management high-risk area has been incorporated into this high-risk area.

Composition of Federal Spending

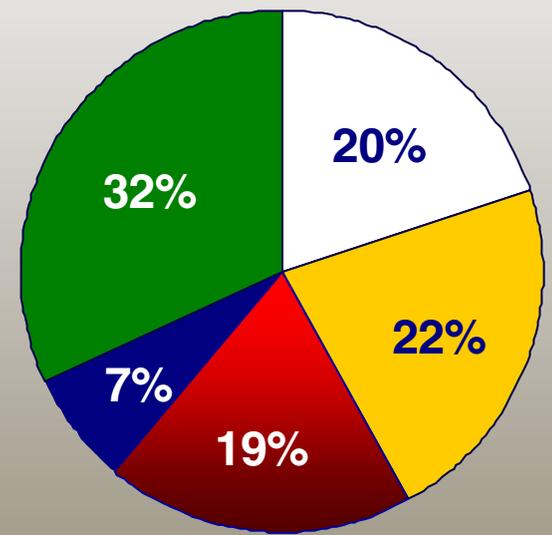
1964



1984



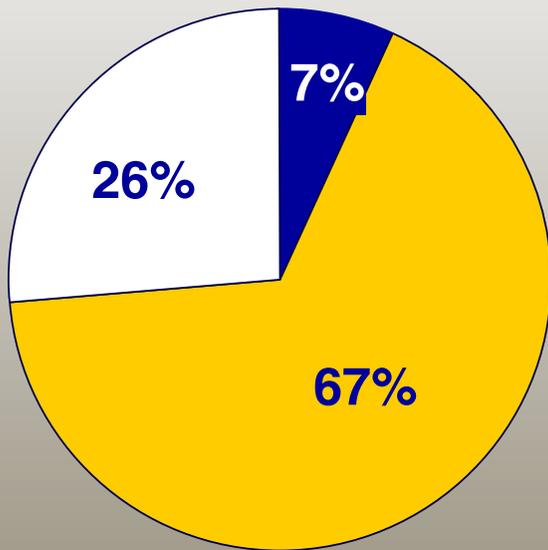
2004



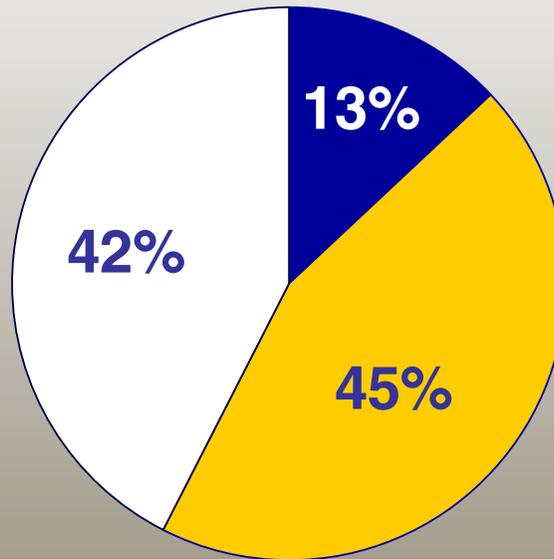
Source: Office of Management and Budget.

Federal Spending for Mandatory and Discretionary Programs

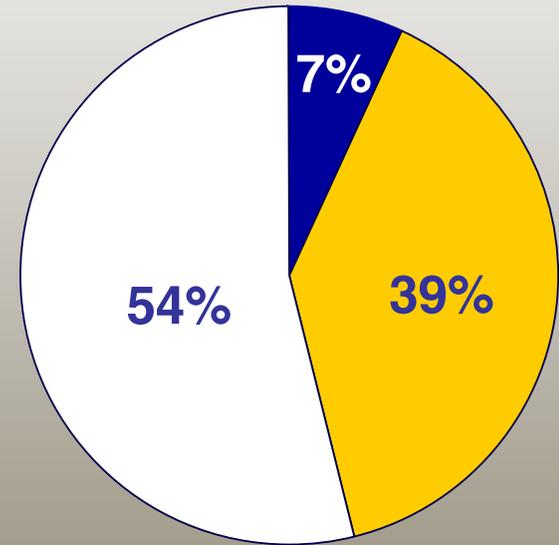
1964



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2004



 Net Interest

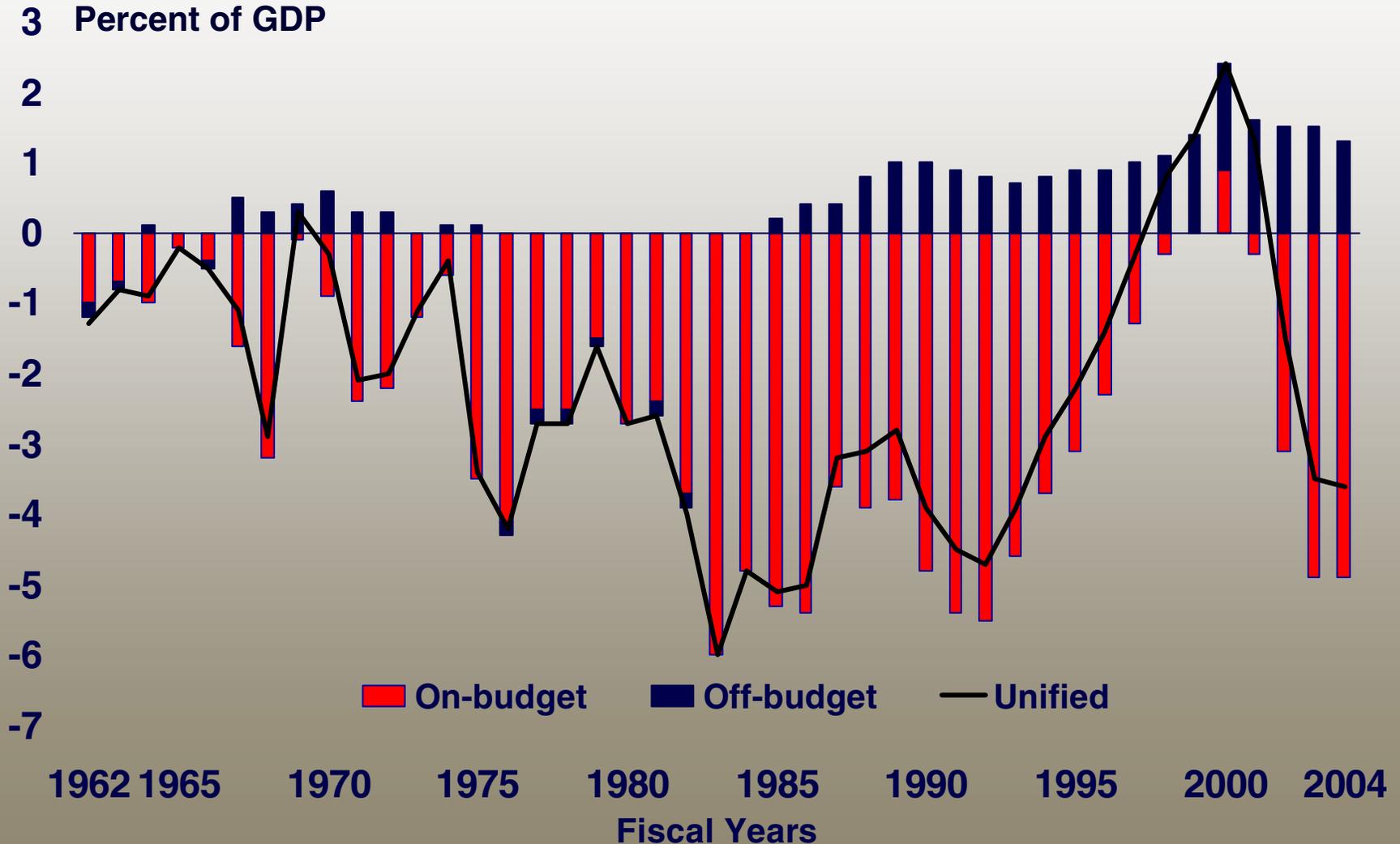
 Discretionary

 Mandatory

Source: Office of Management and Budget.

Surplus or Deficit as a Share of GDP

Fiscal Years 1962-2004



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

Fiscal Year 2004 Deficit Numbers

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

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

March 2005

Selected Fiscal Exposures: Sources and Examples 2005^a

Type	Example (dollars in billions)
Explicit liabilities	Publicly held debt (\$4,297) Military and civilian pension and post-retirement health (\$3,059) Veterans benefits payable (\$925) Environmental and disposal liabilities (\$249) Loan guarantees (\$43)
Explicit financial commitments	Undelivered orders (\$596) Long-term leases (\$39)
Financial contingencies	Unadjudicated claims (\$4) Pension Benefit Guaranty Corporation (\$96) Other national insurance programs (\$1) Government corporations e.g., Ginnie Mae
Exposures implied by current policies or the public's expectations about the role of government	Debt held by government accounts (\$3,071) ^b Future Social Security benefit payments (\$4,017) ^c Future Medicare Part A benefit payments (\$8,561) ^c Future Medicare Part B benefit payments (\$12,384) ^c Future Medicare Part D benefit payments (\$8,686) ^c Life cycle cost including deferred and future maintenance and operating costs (amount unknown) Government Sponsored Enterprises e.g., Fannie Mae and Freddie Mac

^a All figures are for end of fiscal year 2004, except Social Security and Medicare estimates, which are as of January 1, 2005.

^b This amount includes \$845 billion held by military and civilian pension and post-retirement health funds that would offset the explicit liabilities reported by those funds.

^c Figures for Social Security and Medicare are net of debt held by the trust funds (\$1,687 billion for Social Security, \$268 billion for Medicare Part A, and \$19 billion for Medicare Part B) and represent net present value estimates over a 75-year period. Over an infinite horizon, the estimate for Social Security would be \$11.1 trillion, \$24.1 trillion for Medicare Part A, \$25.8 trillion for Medicare Part B, and \$18.2 trillion for Medicare Part D.

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

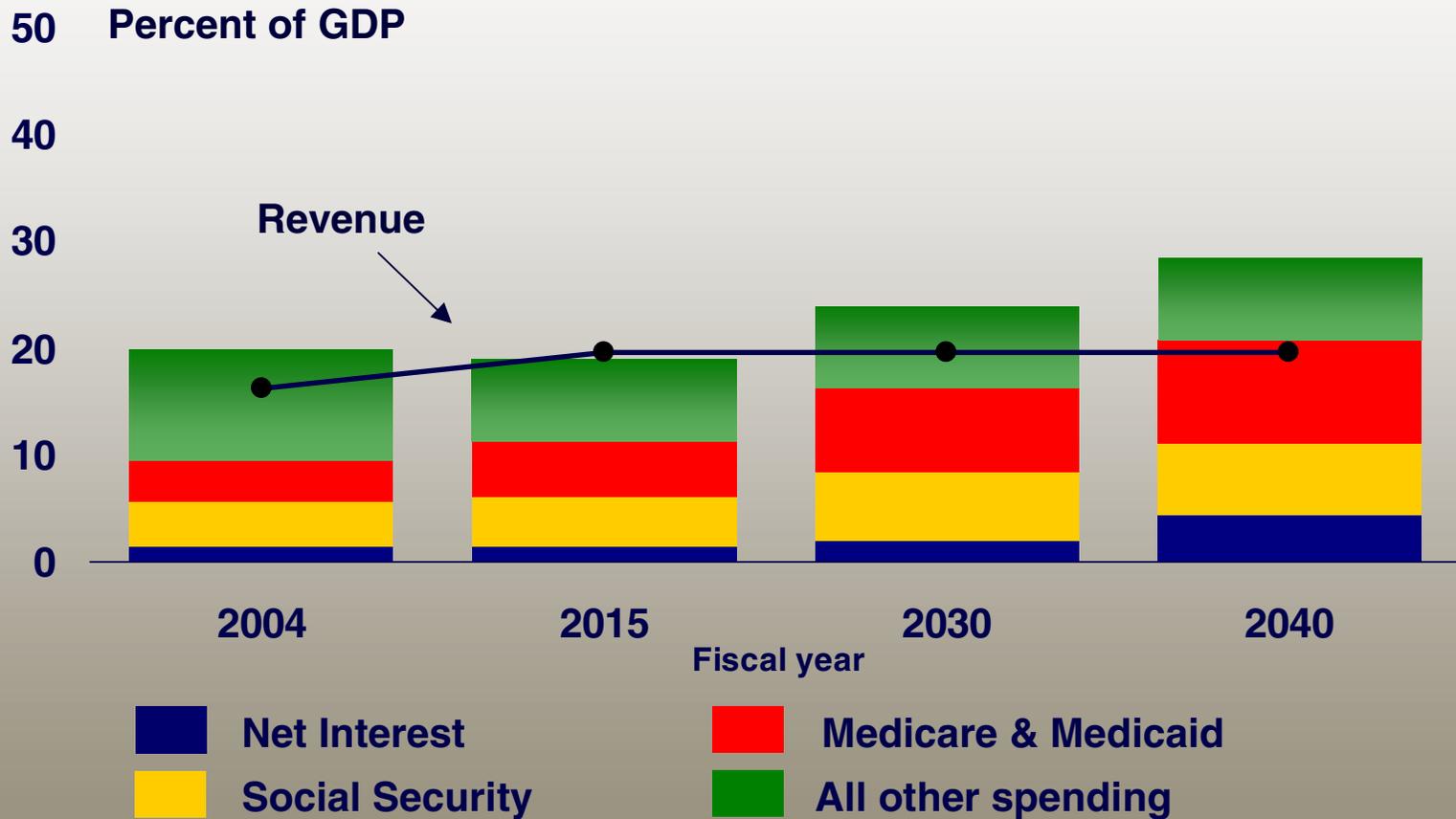
Another Way to Think About These Numbers

- Debt held by the public—\$4.3T
- Trust fund debt—\$3.1T
- Gross debt—\$7.4T
- Gross debt per person—about \$25,000
- If we add everything on the previous slide, the burden is more than \$150,000 per person or more than \$365,000 per full-time worker. Alternatively, it amounts to a total burden of more than \$45 trillion in current dollars, which is about 18 times the current annual federal budget or about 3.7 times the current annual GDP. This compares with an estimated \$48.5 trillion in total net worth, including home equity, for all Americans.

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

Composition of Spending as a Share of GDP

Under Baseline Extended

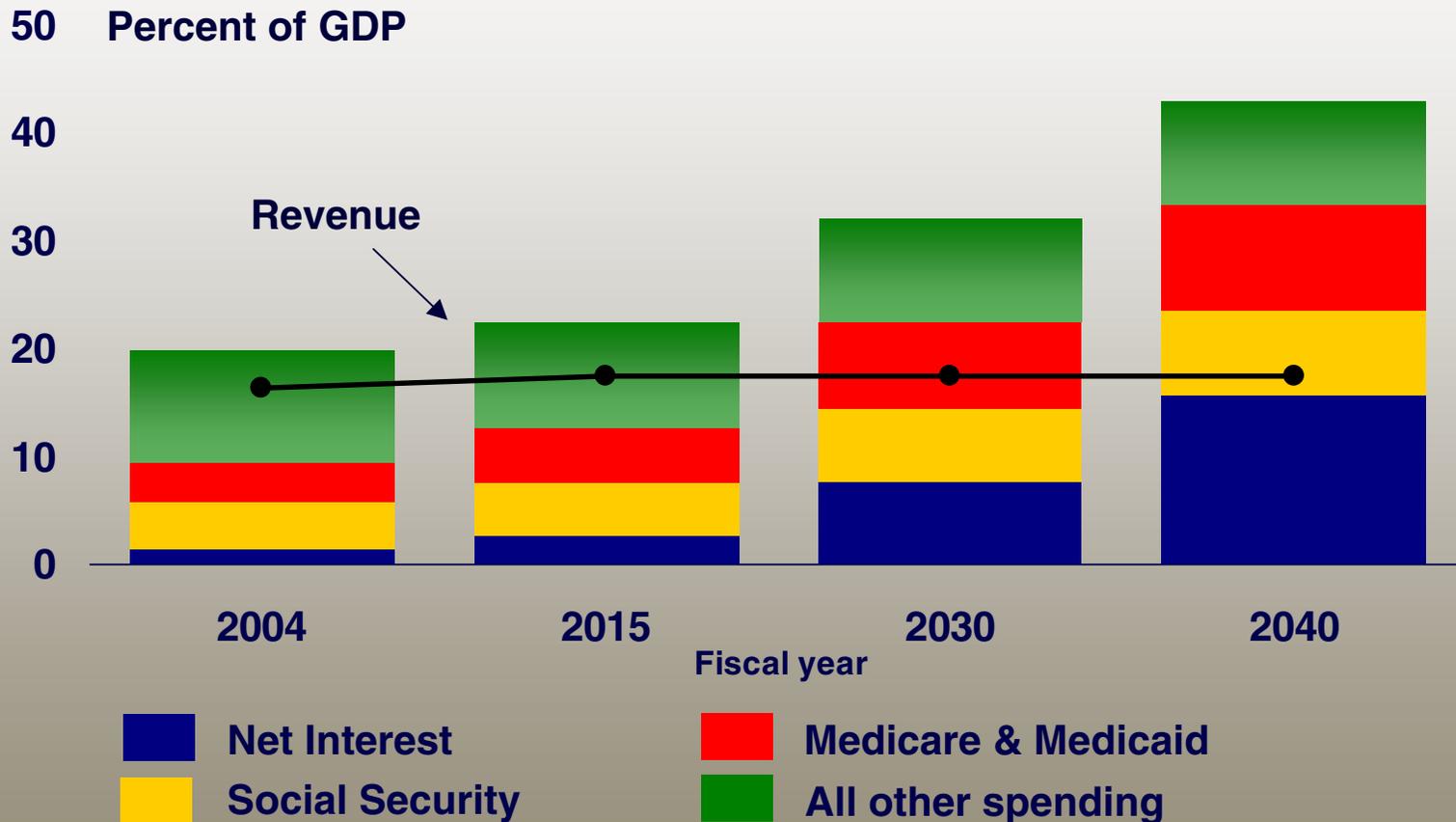


Notes: In addition to the expiration of tax cuts, revenue as a share of GDP increases through 2015 due to (1) real bracket creep, (2) more taxpayers becoming subject to the AMT, and (3) increased revenue from tax-deferred retirement accounts. After 2015, revenue as a share of GDP is held constant.

Source: GAO's March 2005 analysis.

Composition of Spending as a Share of GDP

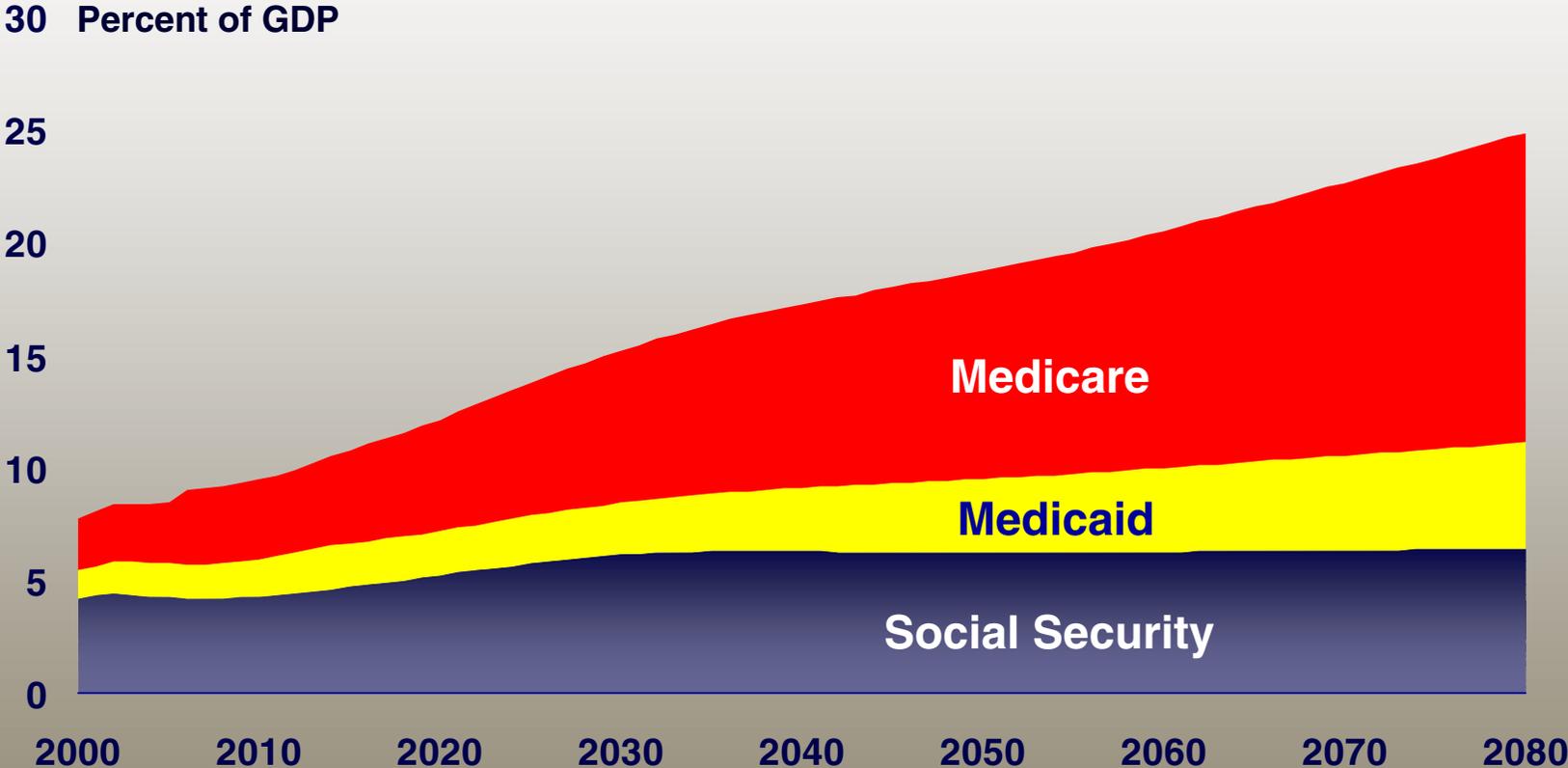
Assuming Discretionary Spending Grows with GDP after 2005
and All Expiring Tax Provisions are Extended



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

Source: GAO's March 2005 analysis.

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



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

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

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 as much as 60 percent or
 - Raising taxes up to 2.5 times today's level
- **Faster Economic Growth Can Help, but It Cannot Solve the Problem**
 - Closing the current long-term fiscal gap based on responsible assumptions would require real average annual economic growth in the double digit range every year for the next 75 years.
 - During the 1990s, the economy grew at an average 3.2 percent per year.
 - As a result, we cannot simply grow our way out of this problem. Tough choices will be required.

The Way Forward

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

Long-term Fiscal Challenges Demand New Metrics, Mechanisms, and Processes

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

New Metrics, Mechanisms and Processes: Some Ideas

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

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

Policy:

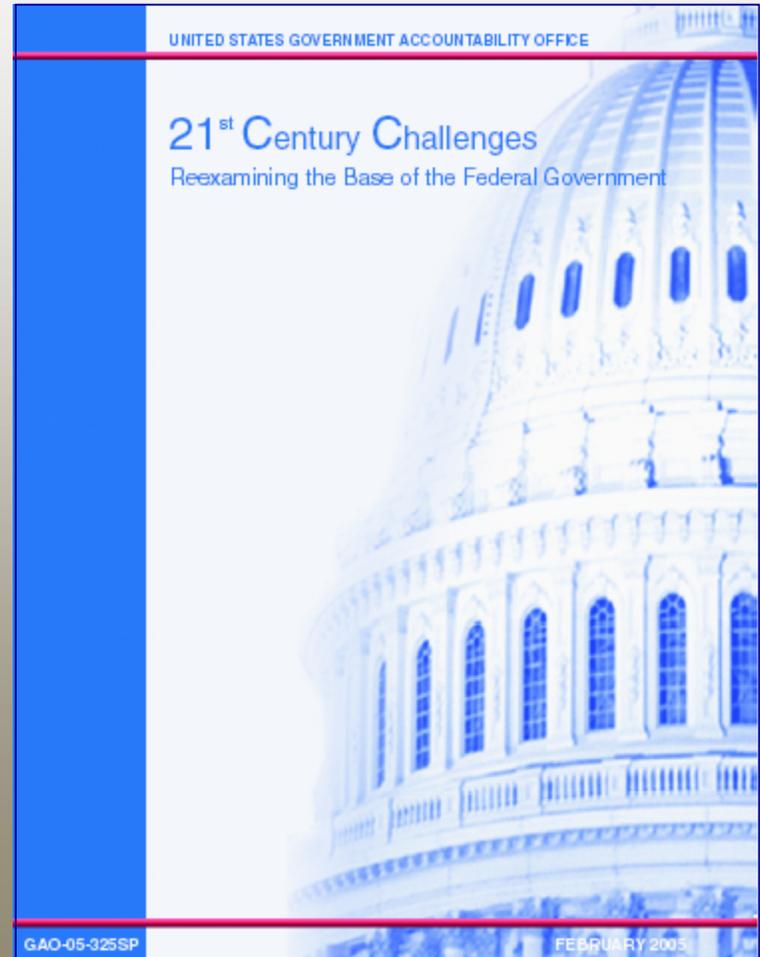
- Reexamine the base of discretionary and other spending
- Restructure existing entitlement programs
- Review and revise our tax policy and enforcement programs

Operations:

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

21st Century Challenges Report

- Provides background, framework, and questions to assist in reexamining the base
- Covers entitlements & other mandatory spending, discretionary spending, and tax policies and programs
- Based on GAO's work for the Congress
- Issued February 16, 2005



Generic Reexamination Criteria and Sample Questions

Relevance of purpose and the federal role

Why did the federal government initiate this program and what was the government trying to accomplish?

Have there been significant changes in the country or the world that relate to the reason for initiating it?

Measuring success

Are there outcome-based measures? If not, why?

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 using the most cost-effective or net beneficial approaches when compared to other tools and program designs?

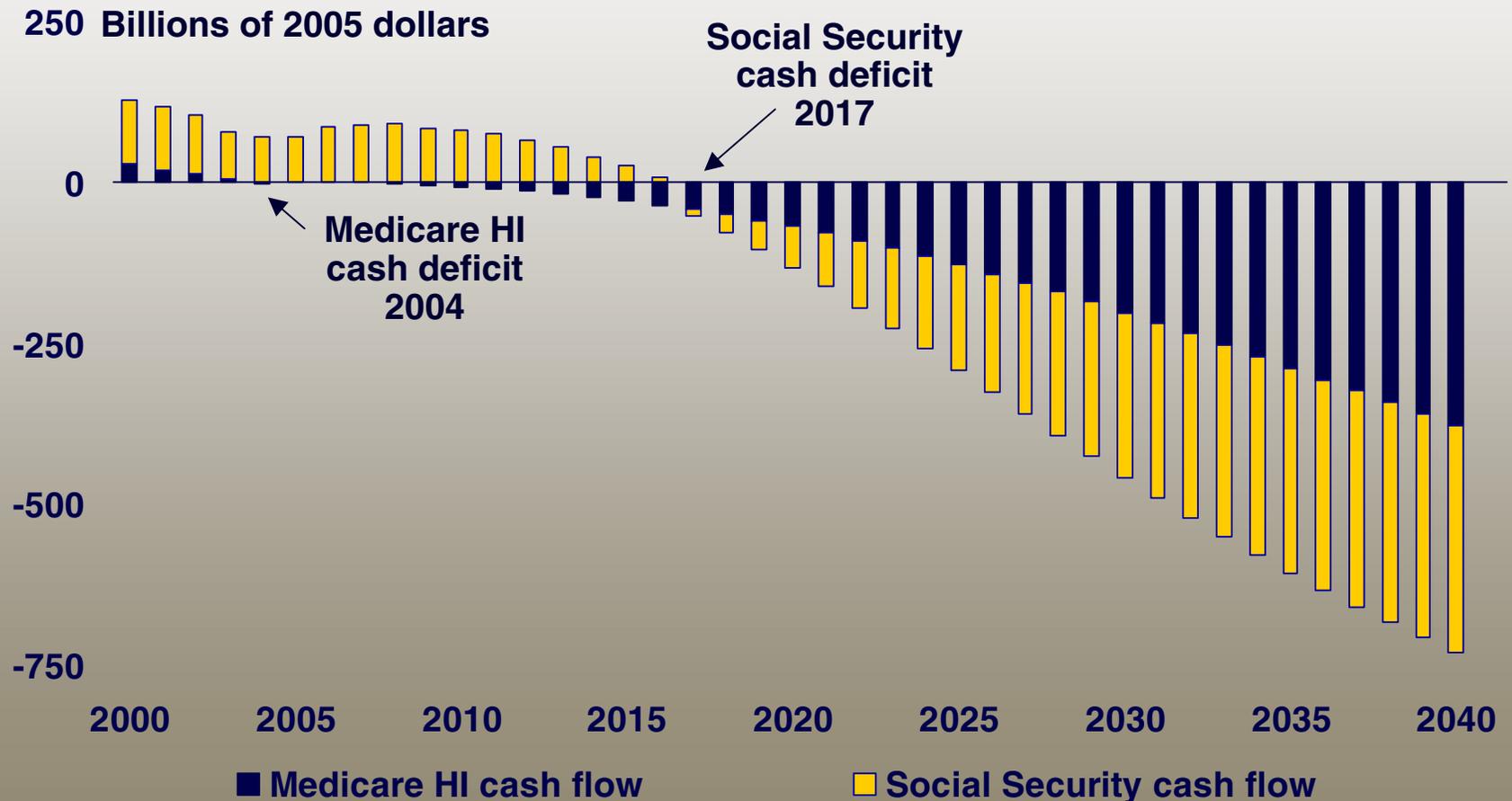
Best practices

Is the responsible entity employing prevailing best practices to discharge its responsibilities and achieve its mission?

Selected 21st Century Questions Social Security and Healthcare

- **How should Social Security be reformed to make it both solvent and sustainable while better aligning it with 21st Century economic, demographic and fiscal realities?**
- **How should our overall health care system be reformed to make it more successful and sustainable over time including,**
 - focusing on certain defined needs versus unlimited wants;
 - addressing the division of responsibilities between levels of government, employers, and individuals; and
 - facilitating individual choice, cost control and quality improvement?

Social Security and Medicare's Hospital Insurance Trust Funds Face Cash Deficits



Note: Projections based on the intermediate assumptions of the 2005 Trustees' Reports.

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

Key Dates Highlight Long Term Challenges of the Social Security System

Date	Event
2009	Social Security cash surplus begins to decline
2017	Annual benefit costs exceed cash revenue from taxes
2027	Trust fund ceases to grow because even taxes plus interest fall short of benefits
2041 (SSA) 2052 (CBO)	Trust fund exhausted, annual revenues sufficient to pay about 74% – 78% of promised benefits

Sources: Social Security Administration, *The 2005 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds*. Washington, DC, March 2005. Congressional Budget Office, *The Outlook for Social Security: Potential Range of Social Security Outlays and Revenues Under Current Law*. Washington, DC, June 2004 (updated April 2005).

GAO Criteria for Evaluating Social Security Reform Proposals

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

Comprehensive proposals can be evaluated against three basic criteria:

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

Key Dates Highlight Long Term Challenges of the Medicare Program

Date	Event
2004	HI outlays exceed cash income
2007	Estimated trigger date for “Medicare funding warning”
2012	Projected date that annual “general revenue funding” will exceed 45 percent of total Medicare outlays
2020	HI (Part A) trust fund exhausted, annual income sufficient to pay about 79% of HI promised benefits

Source: 2005 Annual Report of The Boards of Trustees of The Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds Washington, DC, March 2005

Evaluating Health Care System Reforms

- Cost, access, and quality challenges—together with obstacles to achieving efficiency—argue for fundamental system reform.
- A comprehensive review and reassessment of the overall health care system raises the following questions:
 - **What** are societal needs versus individual wants in our health care system?
 - **Who**—among individuals, employers, and governments—should be responsible for paying for health care?
 - **Where** would we get the largest return for our efforts to control spending?
 - **How** much of health care costs can government, employers, and individuals afford and sustain over time?
 - **When** are we going to get started, as the challenge gets bigger everyday and any delay compounds the problems?

Health Care System Elements: Incentives, Transparency, and Accountability

- **Ideally, health care system reforms will**
 - align incentives for providers and consumers to make prudent choices about health insurance coverage and prudent decisions about the use of medical services,
 - foster transparency with respect to the value and costs of care, and
 - ensure accountability from health plans and providers to meet standards for appropriate use and quality.

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 21st Century
 - which programs and policies should be changed and how
 - how government should be financed



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

Republican Main Street Partnership Forum
May 26, 2005