



# Fiscal, Social Security, and Health Care Challenges

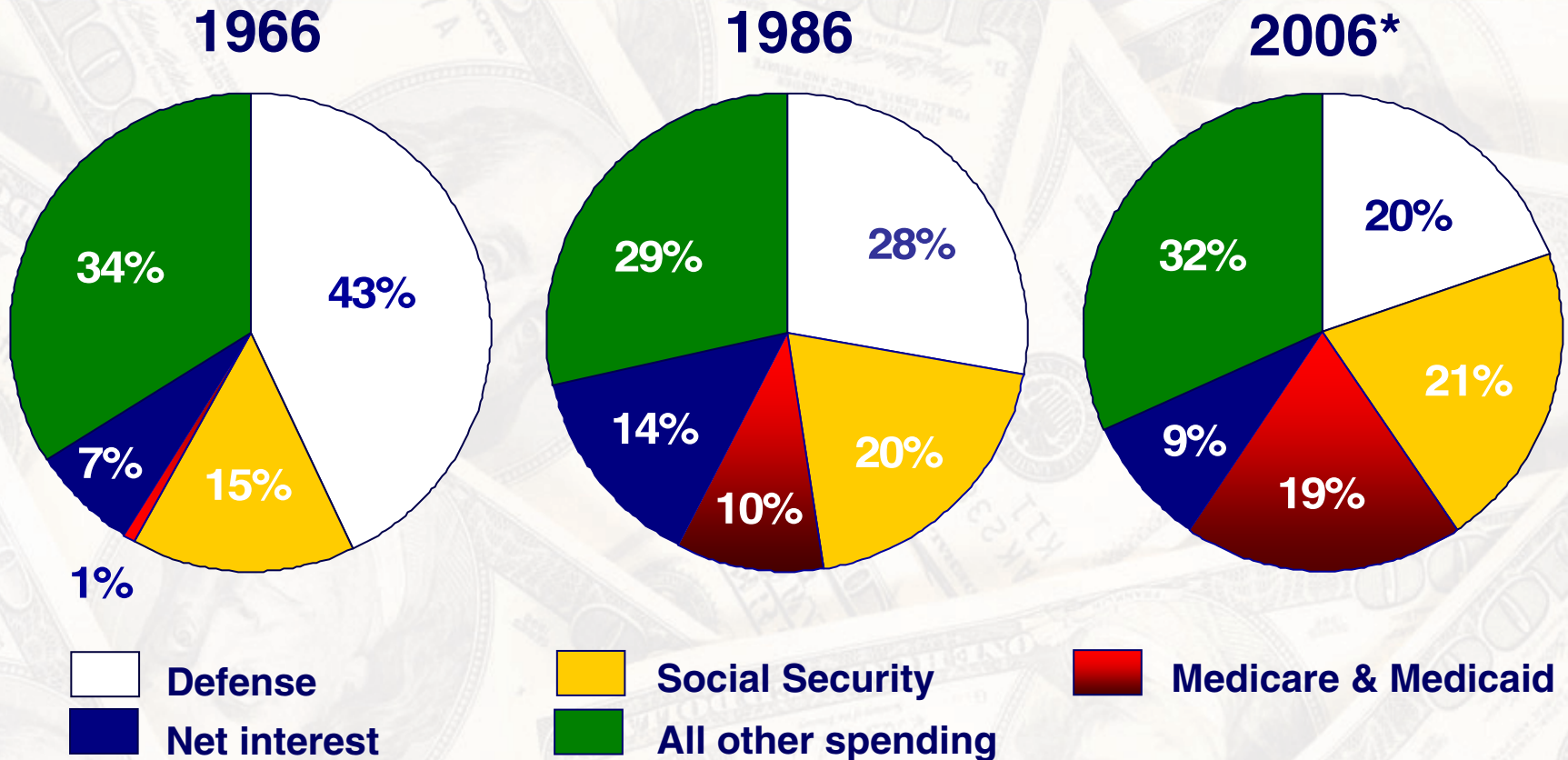
The Honorable David M. Walker  
Comptroller General of the United States  
Awakening Conference  
Sea Island, GA  
January 7, 2007

# The Case for Change

**The federal government is on a “burning platform,” and the status quo way of doing business is unacceptable for a variety of reasons, including:**

- Past fiscal trends and significant long-range challenges
- Rising public expectations for demonstrable results and enhanced responsiveness
- Selected trends and challenges having no boundaries
- Additional resource demands due to Iraq, Afghanistan, incremental homeland security needs, and recent natural disasters in the United States
- Numerous government performance/accountability and high risk challenges
- Outdated federal organizational structures, policies, and practices

# Composition of Federal Spending



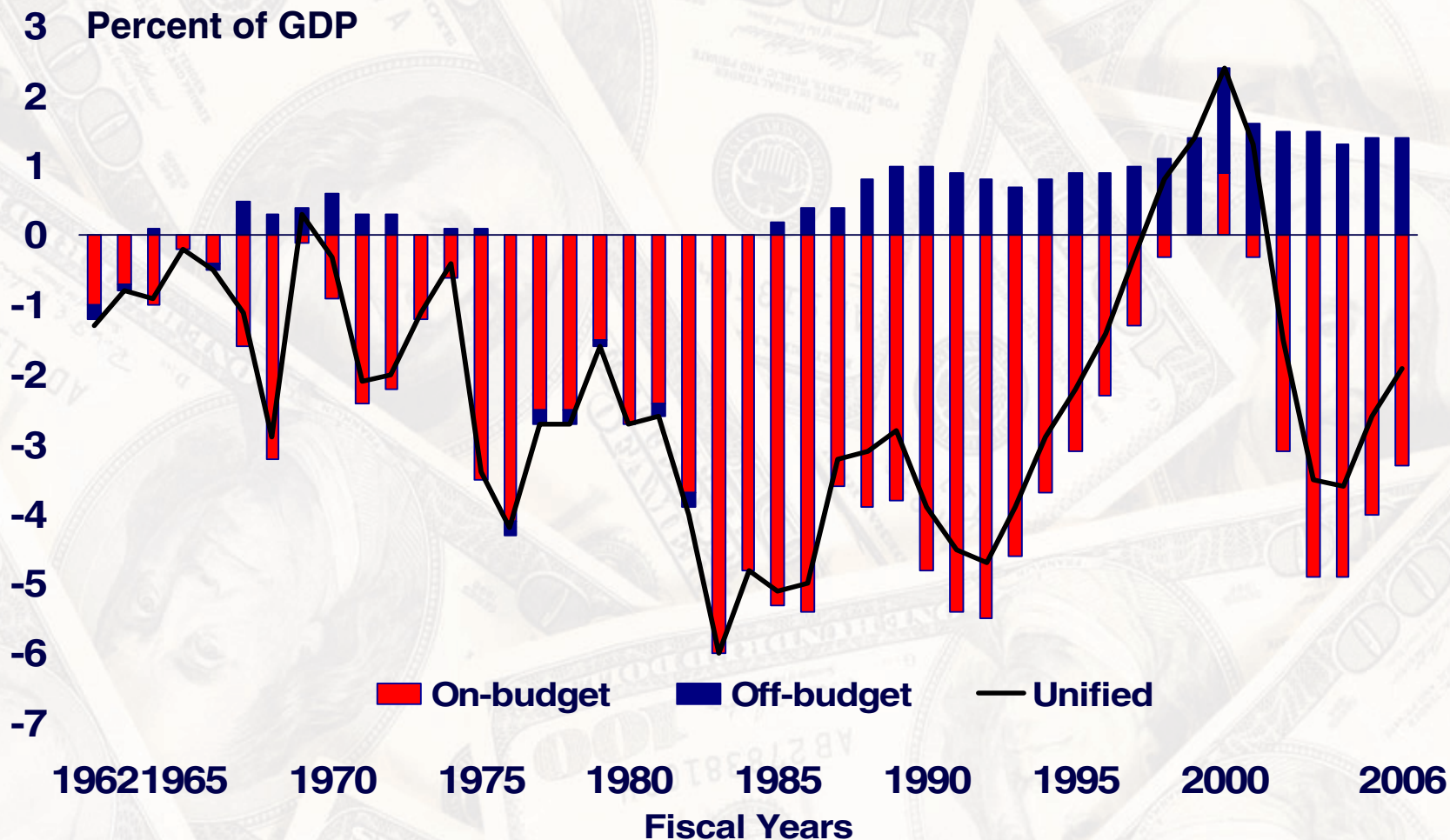
\*Preliminary.

Source: Office of Management and Budget and the Department of the Treasury.

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

# Surplus or Deficit as a Share of GDP

## Fiscal Years 1962-2006



Source: Office of Management and Budget, Department of the Treasury and the Congressional Budget Office.

# Fiscal Year 2005 and 2006 Deficits and Net Operating Costs

	Fiscal Year 2005	Fiscal Year 2006
	(\$ Billion)	
On-Budget Deficit	(494)	(434)
Off-Budget Surplus <sup>a</sup>	175	186
Unified Deficit	(318)	(248)
Net Operating Cost	(760)	(450)

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

<sup>a</sup>Includes \$173 billion in Social Security surpluses for fiscal year 2005 and \$185 billion for fiscal year 2006; \$2 billion in Postal Service surpluses for fiscal year 2005 and \$1 billion for fiscal year 2006.

# Major Fiscal Exposures

(\$ trillions)

	2000	2006	% Increase
<b>• Explicit liabilities</b>	<b>\$6.9</b>	<b>\$10.4</b>	<b>52</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>1.3</b>	<b>140</b>
<ul style="list-style-type: none"> <li>• E.g., PBGC, undelivered orders</li> </ul>			
<b>• Implicit exposures</b>	<b>13.0</b>	<b>38.8</b>	<b>197</b>
<ul style="list-style-type: none"> <li>• Future Social Security benefits</li> </ul>	3.8	6.4	
<ul style="list-style-type: none"> <li>• Future Medicare Part A benefits</li> </ul>	2.7	11.3	
<ul style="list-style-type: none"> <li>• Future Medicare Part B benefits</li> </ul>	6.5	13.1	
<ul style="list-style-type: none"> <li>• Future Medicare Part D benefits</li> </ul>	--	7.9	
<b>Total</b>	<b>\$20.4</b>	<b>\$50.5</b>	<b>147</b>

Source: 2000 and 2006 Financial Report of the United States Government.

Note: Totals and percent increases may not add due to rounding. Estimates for Social Security and Medicare are at present value as of January 1 of each year and all other data are as of September 30.

# How Big is Our Growing Fiscal Burden?

This fiscal burden can be translated and compared as follows:

<b>Total –major fiscal exposures</b>	<b>\$50.5 trillion</b>
<b>Total household net worth<sup>1</sup></b>	<b>\$53.3 trillion</b>
<b>Burden/Net worth ratio</b>	<b>95 percent</b>
<b>Burden<sup>2</sup></b>	
<b>Per person</b>	<b>\$170,000</b>
<b>Per full-time worker</b>	<b>\$400,000</b>
<b>Per household</b>	<b>\$440,000</b>
<b>Income</b>	
<b>Median household income<sup>3</sup></b>	<b>\$46,326</b>
<b>Disposable personal income per capita<sup>4</sup></b>	<b>\$31,519</b>

Source: GAO analysis.

Notes: (1) Federal Reserve Board, Flow of Funds Accounts, Table B.100, 2006:Q2 (Sept. 19, 2006); (2) Burdens are calculated using estimated total U.S. population as of 9/30/06, from the U.S. Census Bureau; full-time workers reported by the Bureau of Economic Analysis, in NIPA table 6.5D (Aug. 2, 2006); and households reported by the U.S. Census Bureau, in *Income, Poverty, and Health Insurance Coverage in the United States: 2005* (Aug. 2006); (3) U.S. Census Bureau, *Income, Poverty, and Health Insurance Coverage in the United States: 2005* (Aug. 2006); and (4) Bureau of Economic Analysis, *Personal Income and Outlays: October 2006*, table 2, (Nov. 30, 2006).

# Composition of Spending as a Share of GDP

## Under Baseline Extended (January 2001)

Percent of GDP

50  
40  
30  
20  
10  
0

Revenue



2005

2015\*

2030\*

2040\*

Fiscal year

■ Net interest

■ Social Security

■ Medicare & Medicaid

■ All other spending

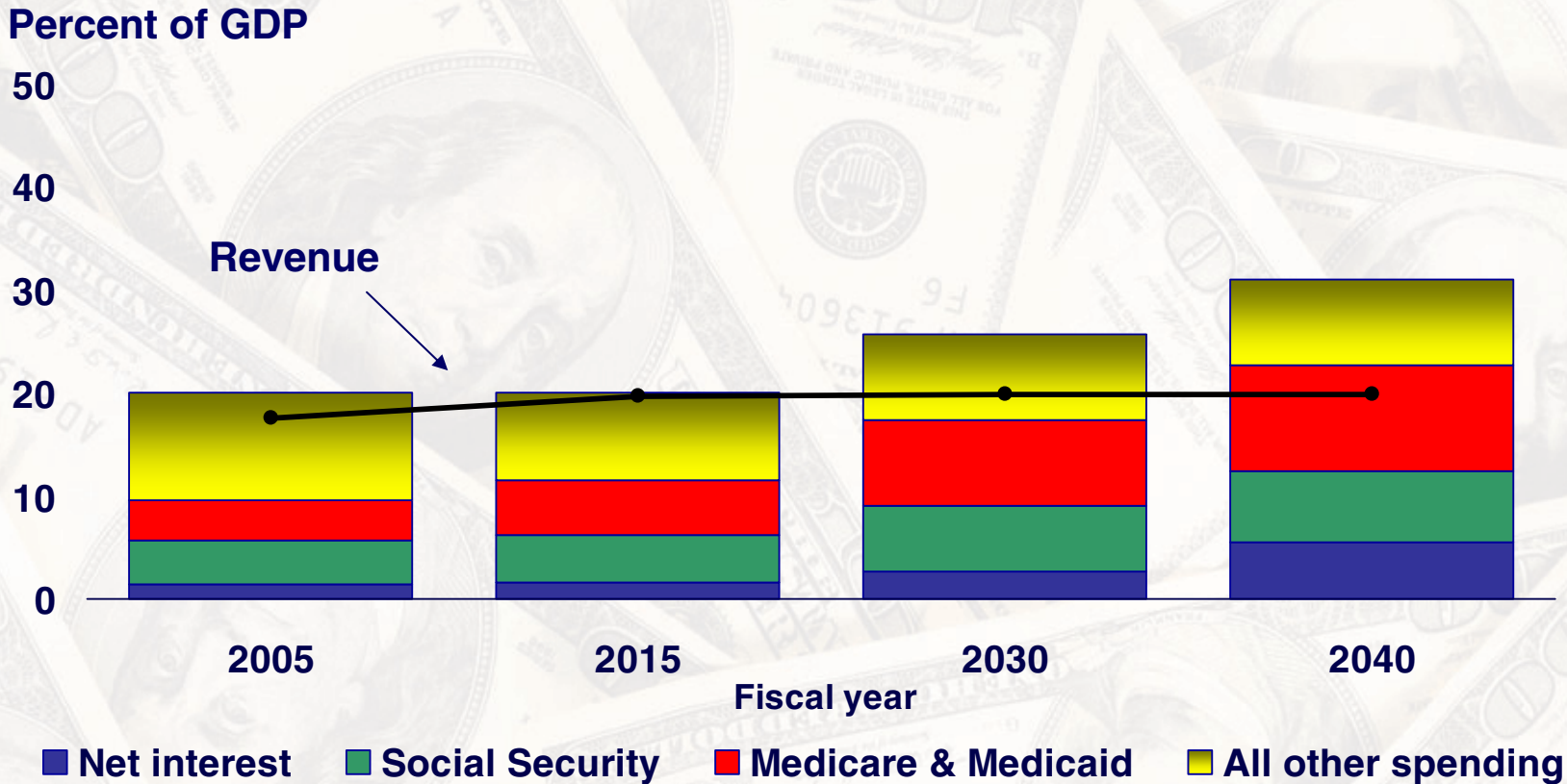
Source: GAO's January 2001 analysis.

\*All other spending is net of offsetting interest receipts.



# Composition of Spending as a Share of GDP

## Under Baseline Extended (August 2006)



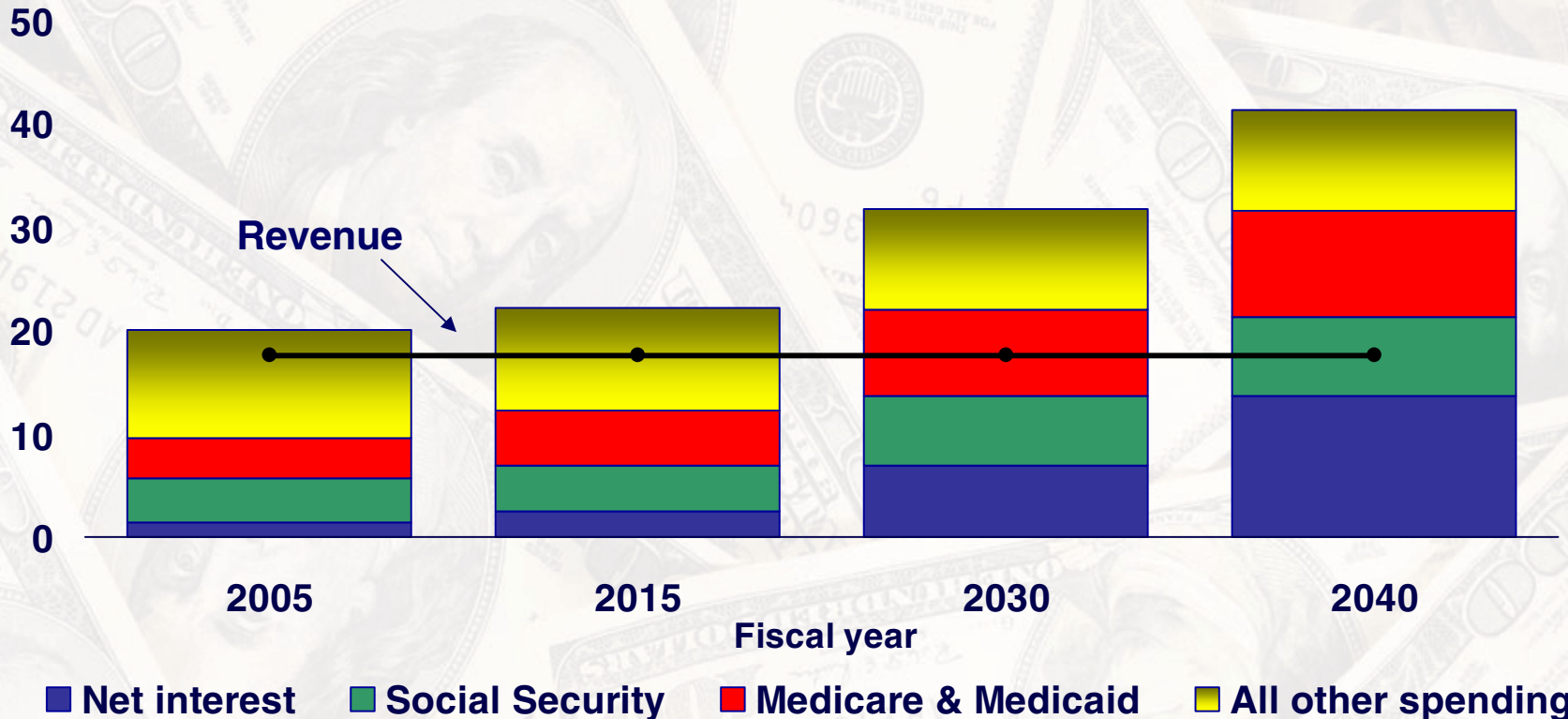
Source: GAO's August 2006 analysis.

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.

# Composition of Spending as a Share of GDP

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

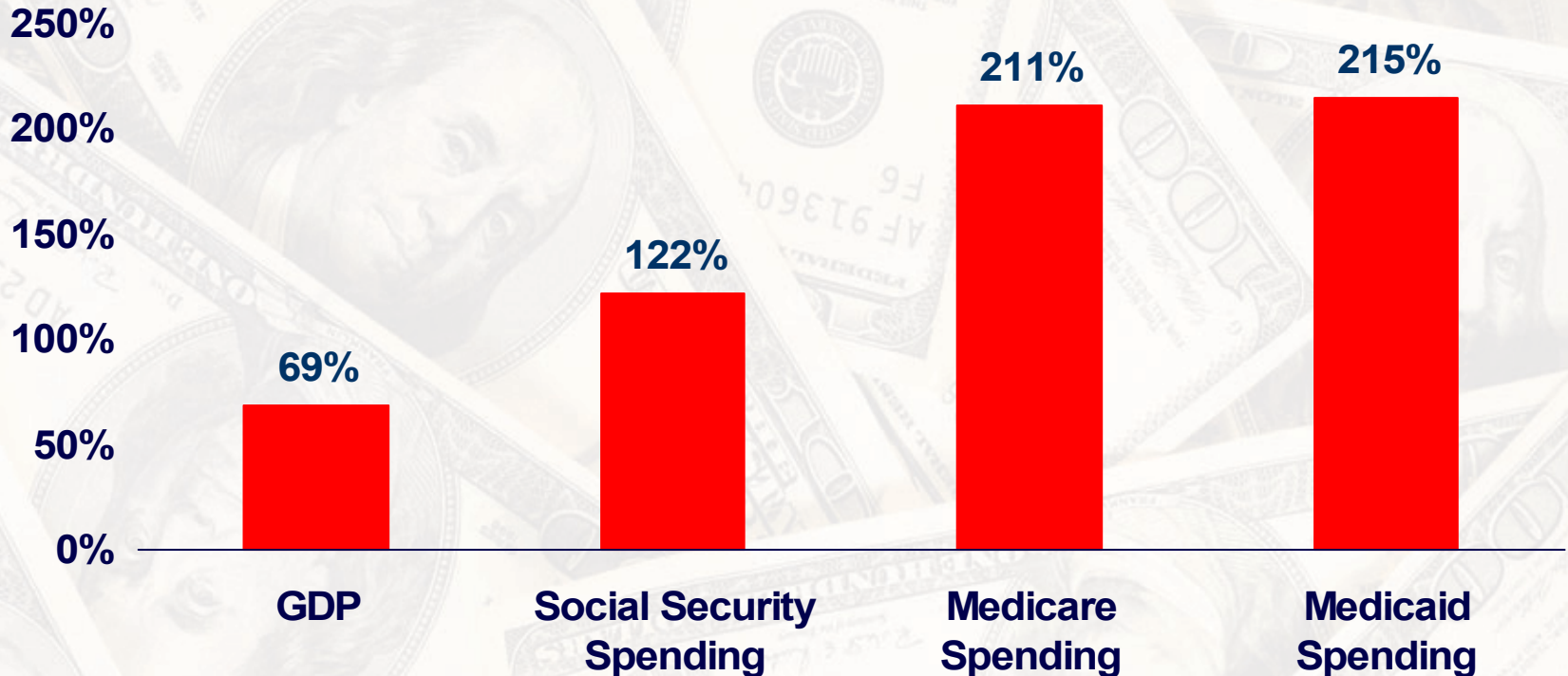
Percent of GDP



Source: GAO's August 2006 analysis.

# Growth in Spending for Social Security, Medicare, and Medicaid Expected to Outpace Economic Growth

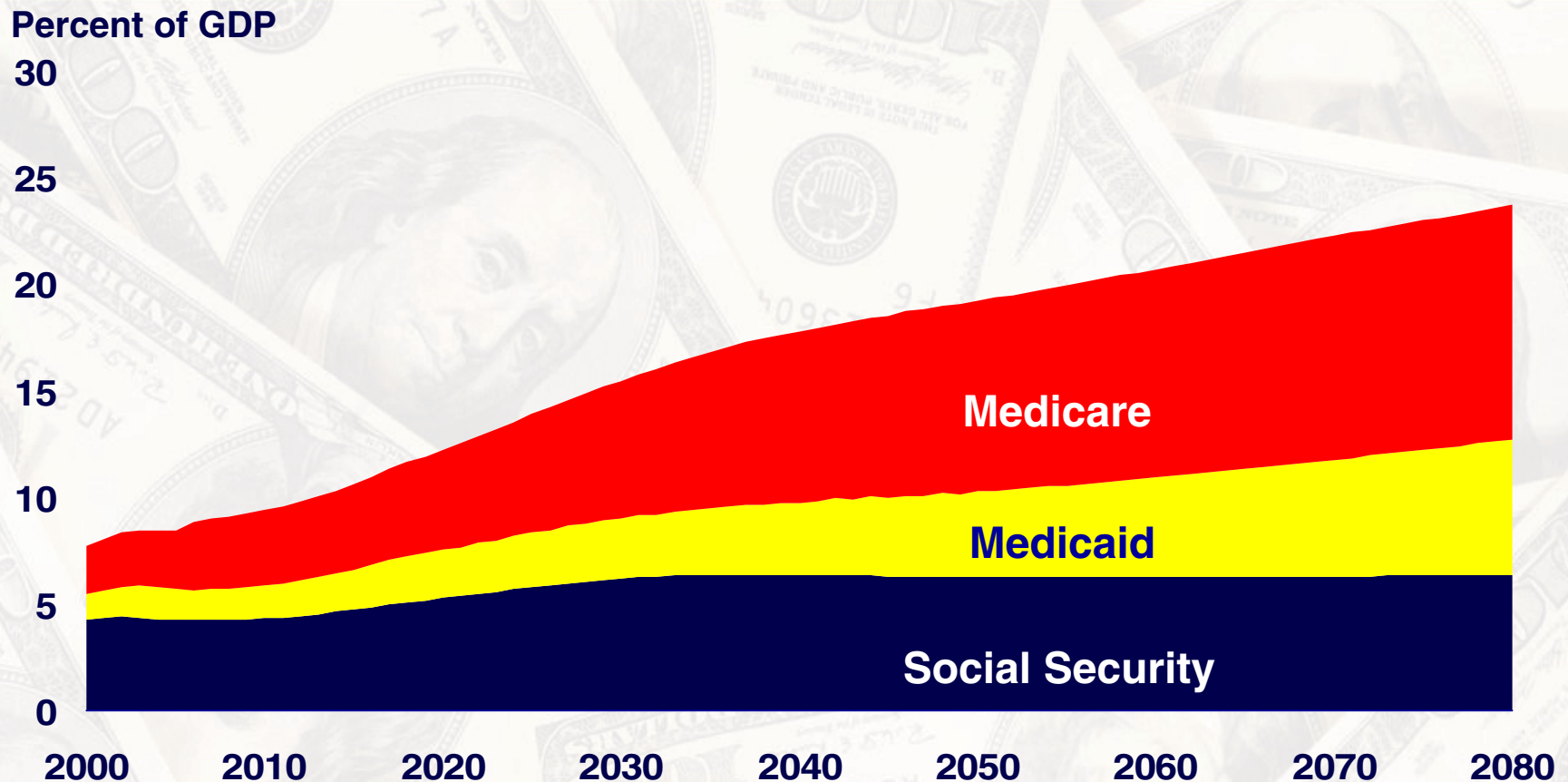
Growth in constant dollars 2006-2030



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.

Notes: Social Security and Medicare projections based on the intermediate assumptions of the 2006 Trustees' Reports. Medicaid projections based on CBO's August 2006 short-term Medicaid estimates and CBO's December 2005 long-term Medicaid projections under mid-range assumptions.

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



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.

Notes: Social Security and Medicare projections based on the intermediate assumptions of the 2006 Trustees' Reports. Medicaid projections based on CBO's August 2006 short-term Medicaid estimates and CBO's December 2005 long-term Medicaid projections under mid-range assumptions.

# Debt per Capita Could Exceed GDP Per Capita Before 2030

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

Per capita 2005 dollars

200,000  
175,000  
150,000  
125,000  
100,000  
75,000  
50,000  
25,000  
0

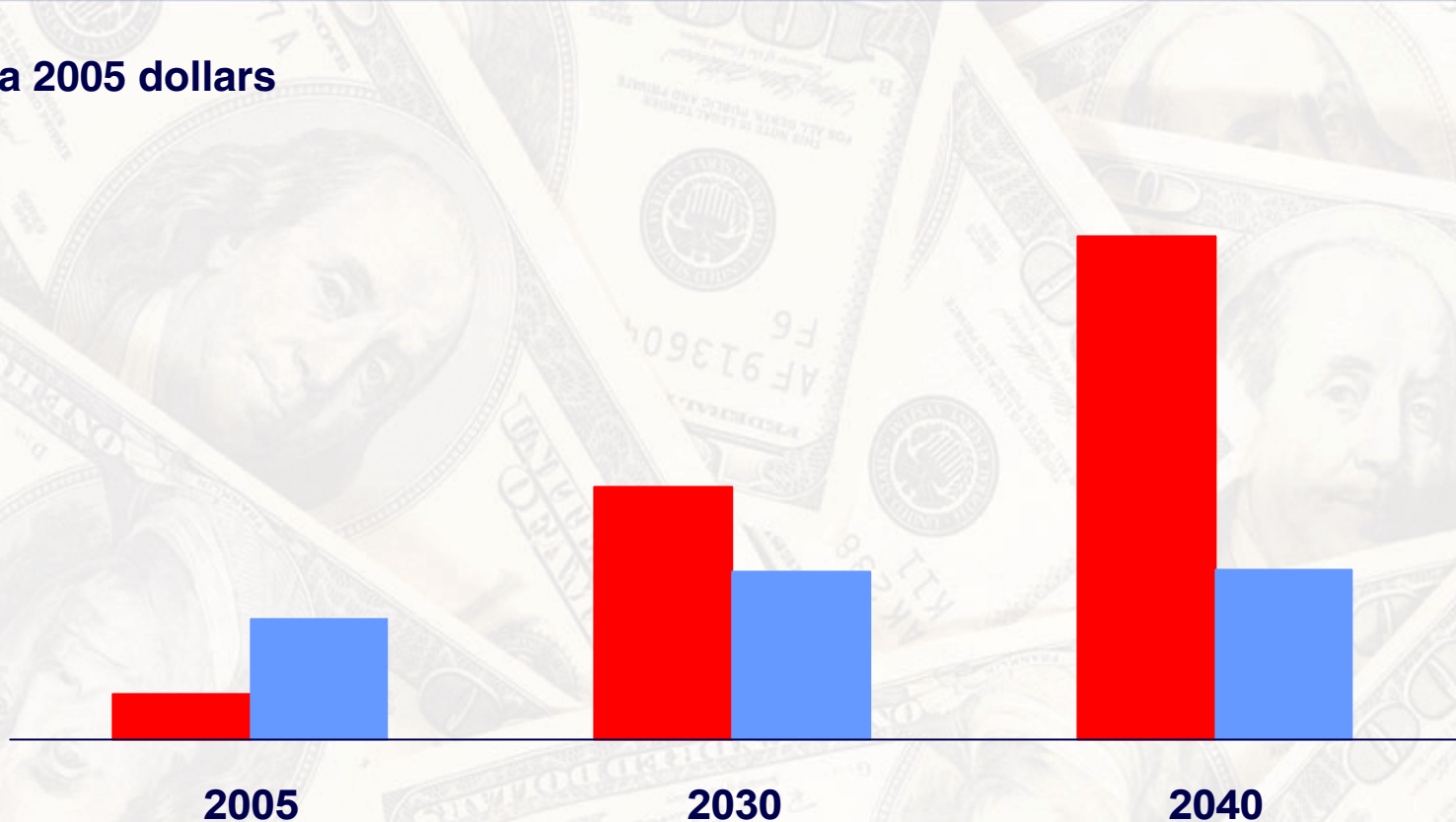
2005

2030

2040

■ Debt per Capita

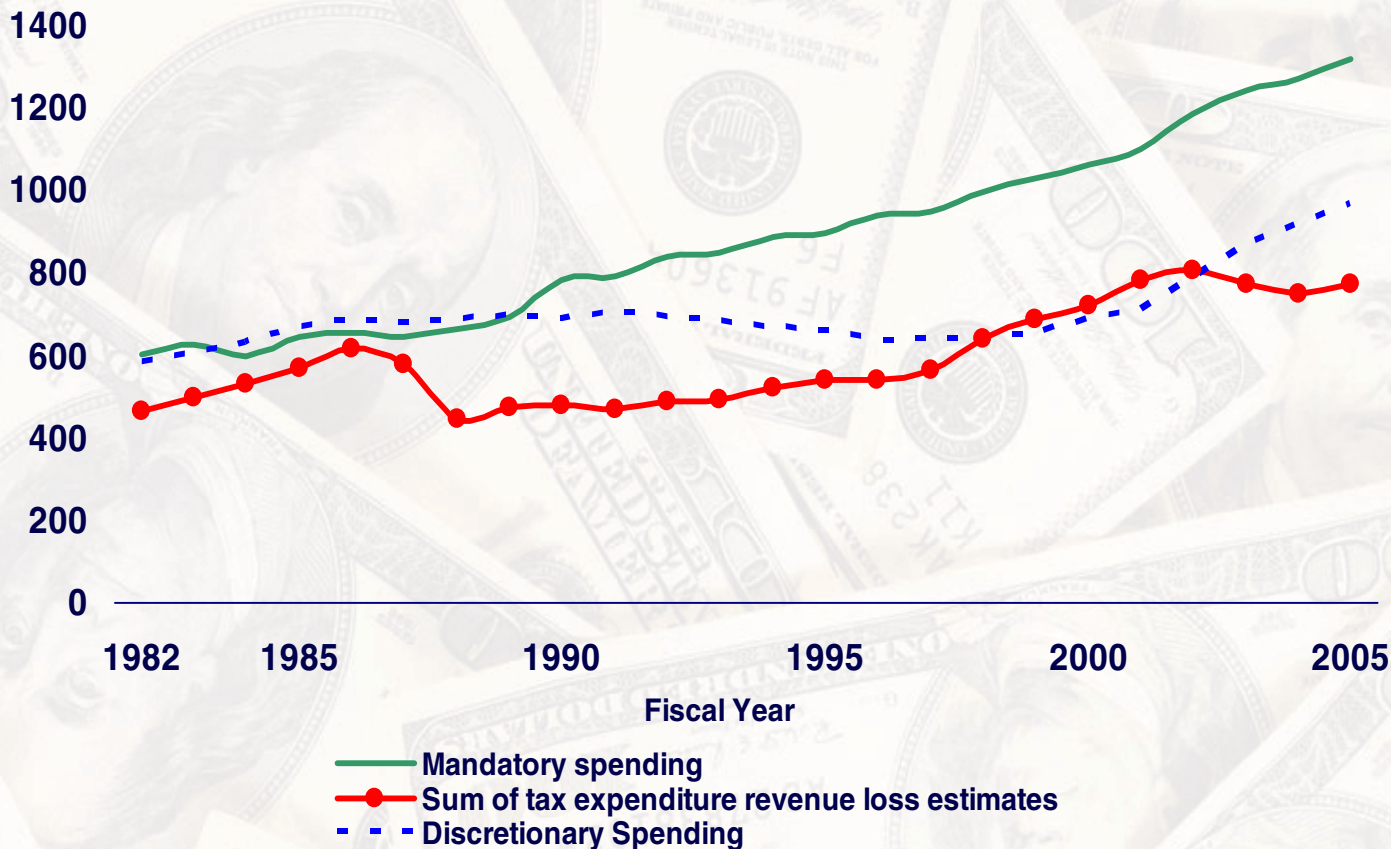
■ GDP per Capita



Source: GAO's August 2006 analysis.

# Federal Tax Expenditures Exceeded Discretionary Spending for Half of the Last Decade

Dollars in billions (in real 2005 dollars)



Source: GAO analysis of OMB budget reports on tax expenditures, fiscal years 1976-2007.

Note: Summing tax expenditure estimates does not take into account interactions between individual provisions. Outlays associated with refundable tax credits are included in mandatory spending.

# 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.

# The Way Forward: A Three-Pronged Approach

1. Improve Financial Reporting, Public Education, and Performance Metrics
2. Strengthen Budget and Legislative Processes and Controls
3. Fundamental Reexamination & Transformation for the 21<sup>st</sup> Century (i.e., entitlement programs, other spending, and tax policy)

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



# The Way Forward

## Improve Financial Reporting, Public Education, 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 & explain a fiscal goal and a path to that goal within 10-year window--or justify 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
- Increase information on long-range fiscal sustainability issues in Congressional Budget Resolution & Budget Process.
- Develop key national (outcome-based) indicators (e.g. economic, security, social, environmental) to chart the nation's posture, progress, and position relative to the other major industrial countries

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

- Restore discretionary spending caps & PAYGO rules on both spending and tax 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 long-term cost estimates (e.g. present value) for any legislative debate on all major tax and spending bills, including entitlement programs. Cost estimates should usually assume no sunset
- Extend accrual budgeting to insurance & federal employee pensions; develop techniques for extending to retiree health & environmental liabilities
- Consider biennial budgeting
- Consider expedited line item rescissions from the President that would only require a majority vote to override the proposed rescission(s)

# 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 and enforcement programs
- Expand scrutiny of all proposed new programs, policies, or activities
- Reengineer internal agency structures and processes, including more emphasis on long-term planning, integrating federal activities, and partnering with others both domestically and internationally
- Strengthen and systematize Congressional oversight processes
- Increase transparency associated with government contracts and other selected items
- Consider a capable, credible, bi-partisan entitlement and tax reform commission along the lines proposed by Sen. Voinovich and Cong. Wolf

# 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

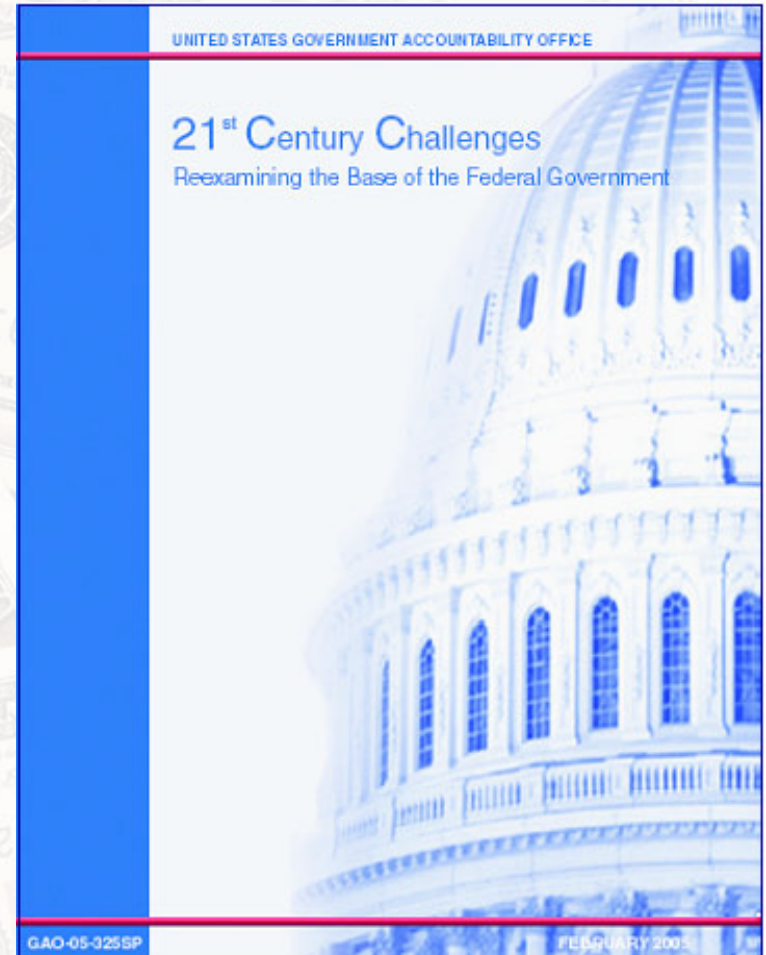
# 16 OUT OF 28

## 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	

# 21<sup>st</sup> 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



Source: GAO.

# Twelve Reexamination Areas

## MISSION AREAS

- Defense
- Education & Employment
- Financial Regulation & Housing
- Health Care
- Homeland Security
- International Affairs
- Natural Resources, Energy & Environment
- Retirement & Disability
- Science & Technology
- Transportation

## CROSSCUTTING AREAS

- Improving Governance
- Reexamining the Tax System

# Illustrative 21<sup>st</sup> Century Questions: Retirement and Disability Policy

- 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)?
- 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)?
- 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)?



# Illustrative 21<sup>st</sup> Century Questions: Health Care

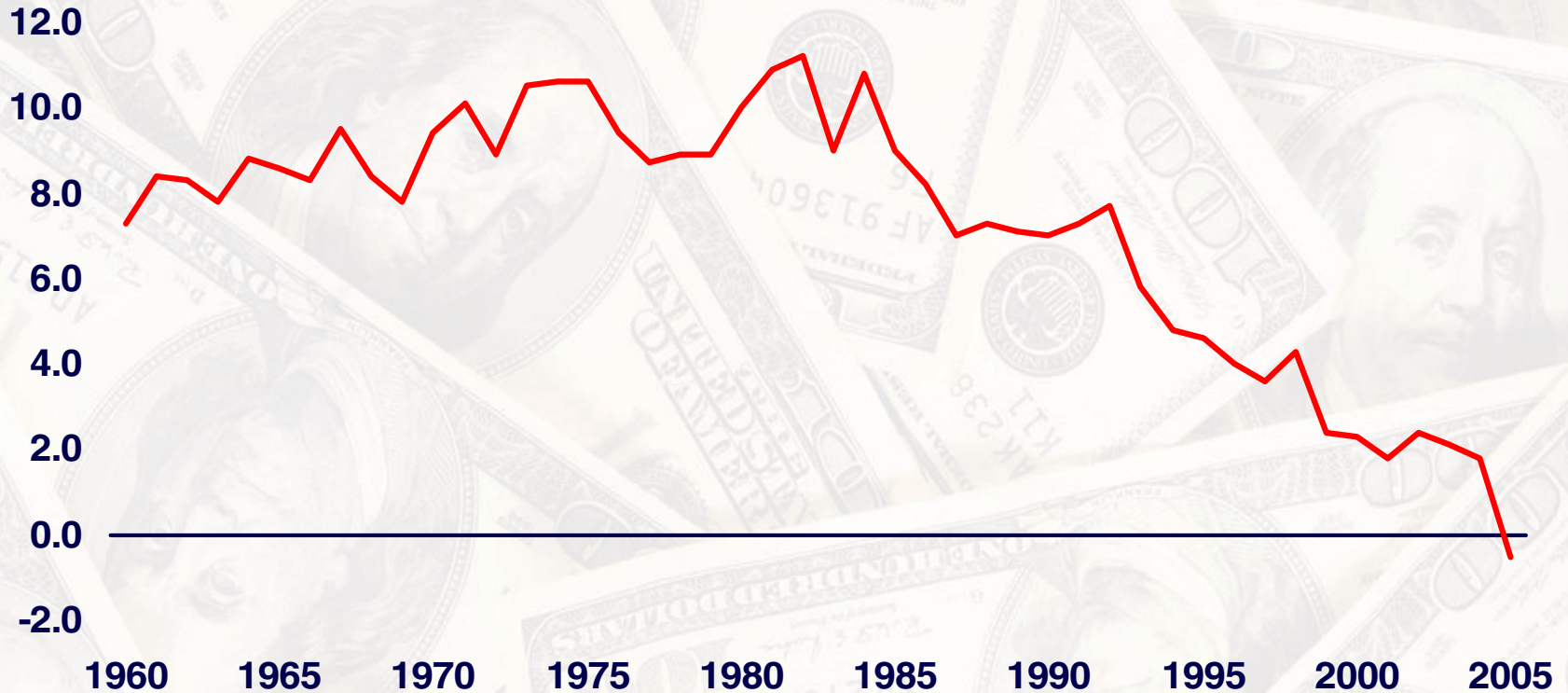
- How can we make our current **Medicare and Medicaid** programs sustainable? For example, should the eligibility requirements (e.g., age, income requirements) for these programs be modified?
- How can we perform a **systematic reexamination of our current health care system**? For example, could public 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?

# Key Elements for Economic Security in Retirement

- **Adequate retirement income**
  - Savings
  - Social Security
  - Pensions
  - Earnings from continued employment (e.g., part-time)
- **Affordable health care**
  - Medicare
  - Retiree health care
- **Long-term care (a hybrid)**
- **Major Players**
  - Employers
  - Government
  - Individuals
  - Family
  - Community

# Personal Saving Rate Has Declined

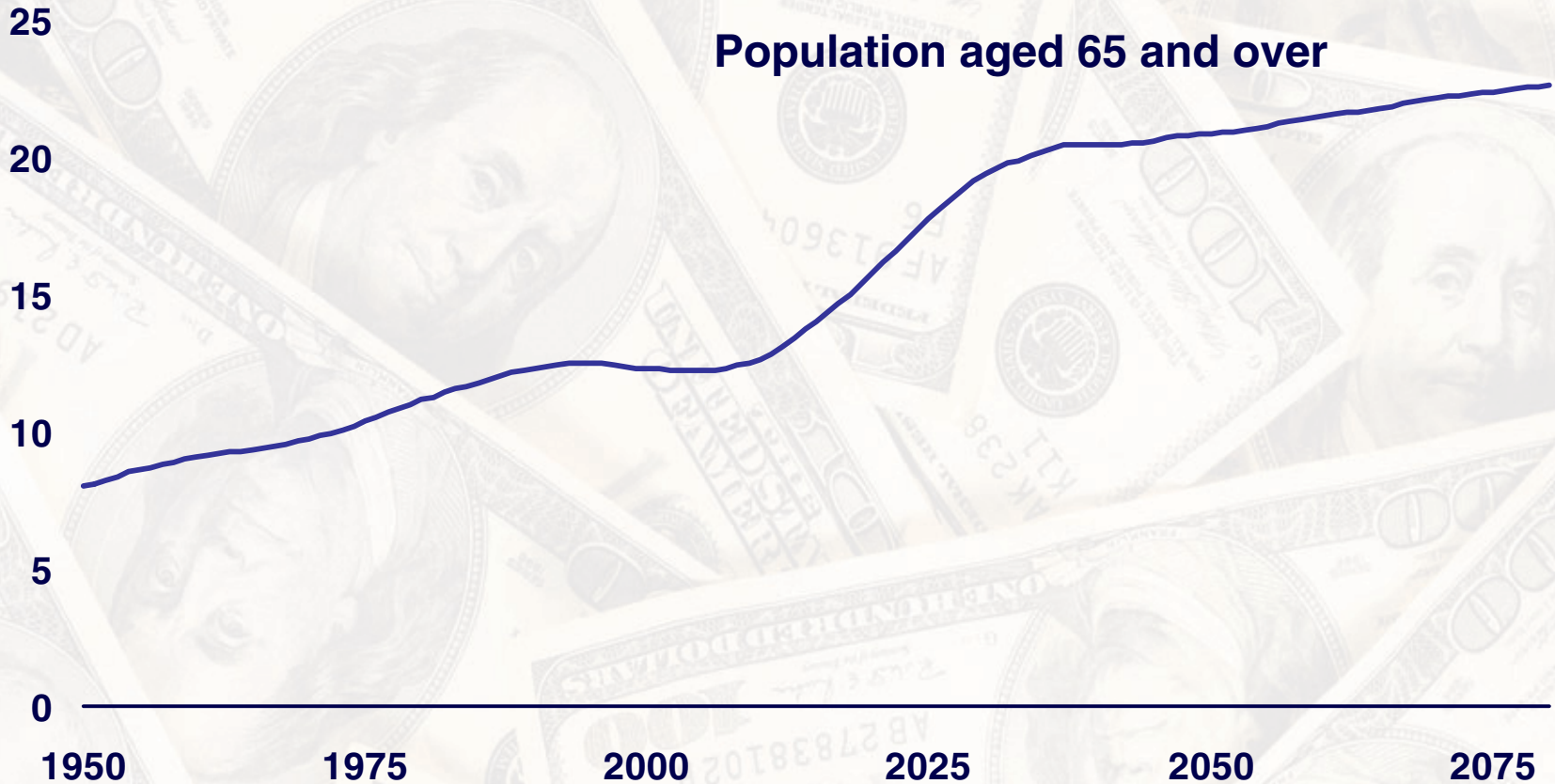
Percent of disposable personal income



Source: Bureau of Economic Analysis, Department of Commerce.

# Aged Population as a Share of Total U.S. Population

Percent of total population

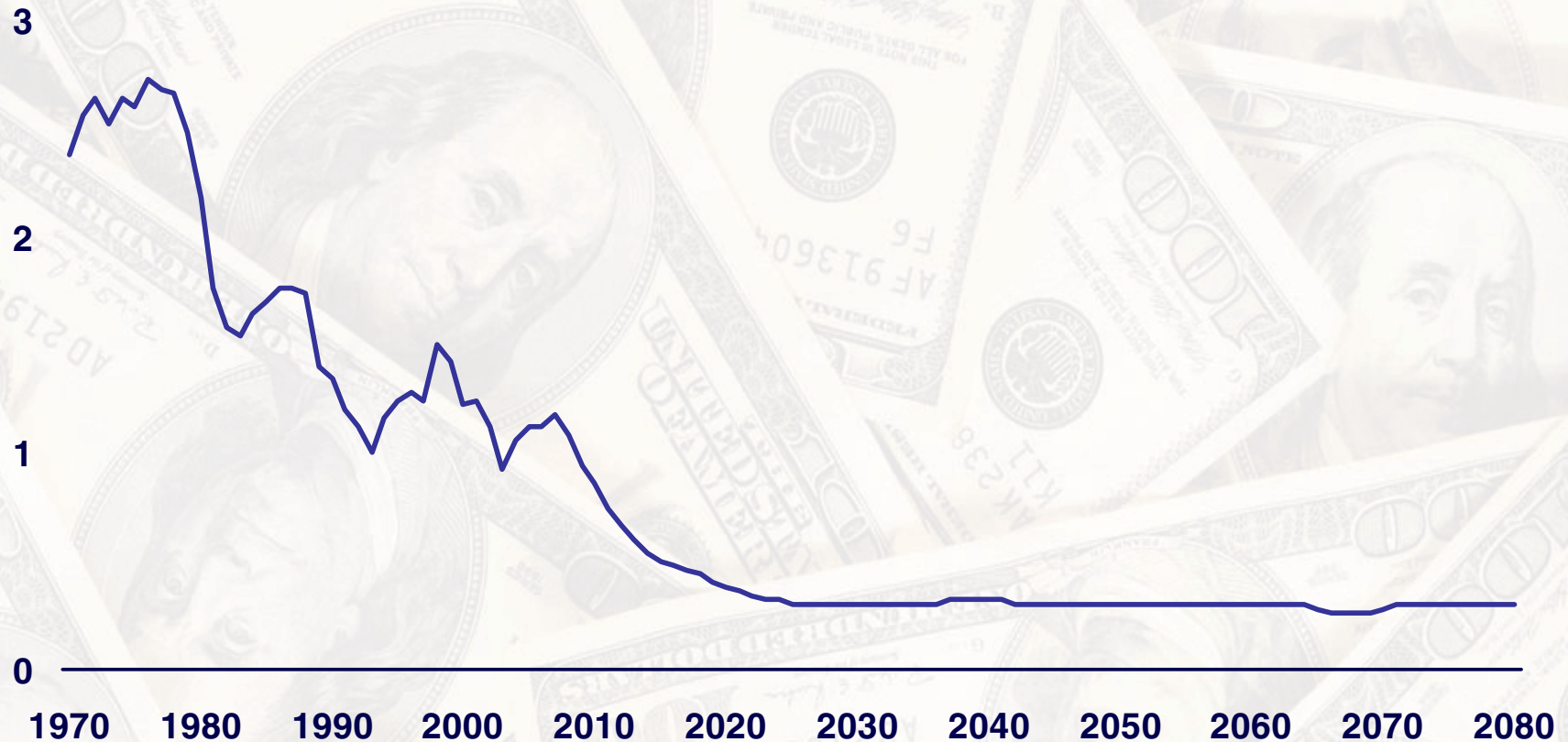


Source: Office of the Chief Actuary, Social Security Administration.

Note: Projections based on the intermediate assumptions of the 2006 Trustees' Reports.

# U.S. Labor Force Growth Will Continue to Decline

Percentage change (5-yr moving average)

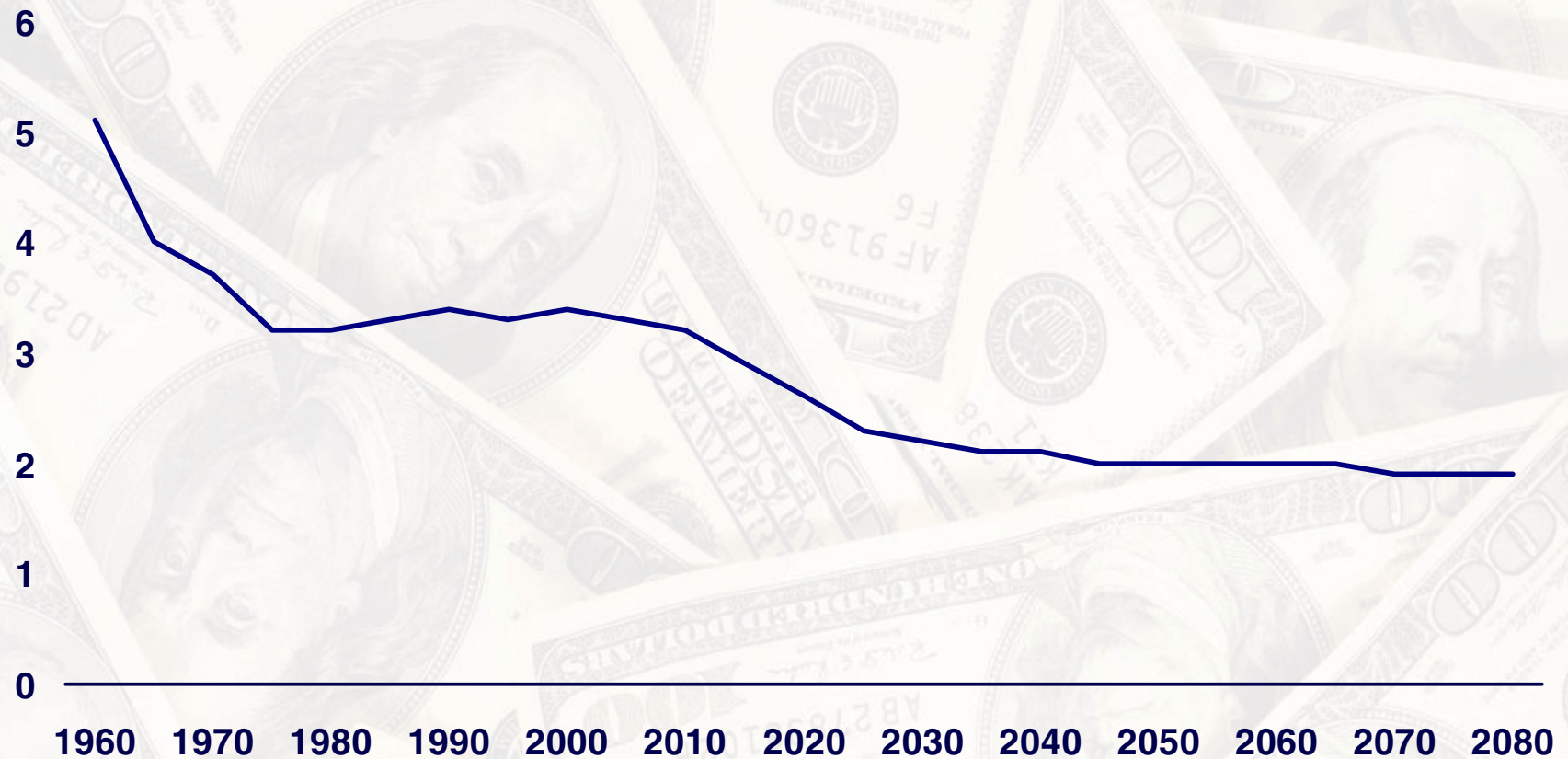


Source: GAO analysis of data from the Office of the Chief Actuary, Social Security Administration.

Note: Percentage change is calculated as a centered 5-yr moving average of projections based on the intermediate assumptions of the 2006 Trustees Reports.

# Social Security Workers Per Beneficiary

Covered workers per OASDI beneficiary



Source: Office of the Chief Actuary, Social Security Administration.

Note: Projections based on the intermediate assumptions of the 2006 Trustees' Reports.

# Working Longer May Help Address the Challenges of an Aging Population

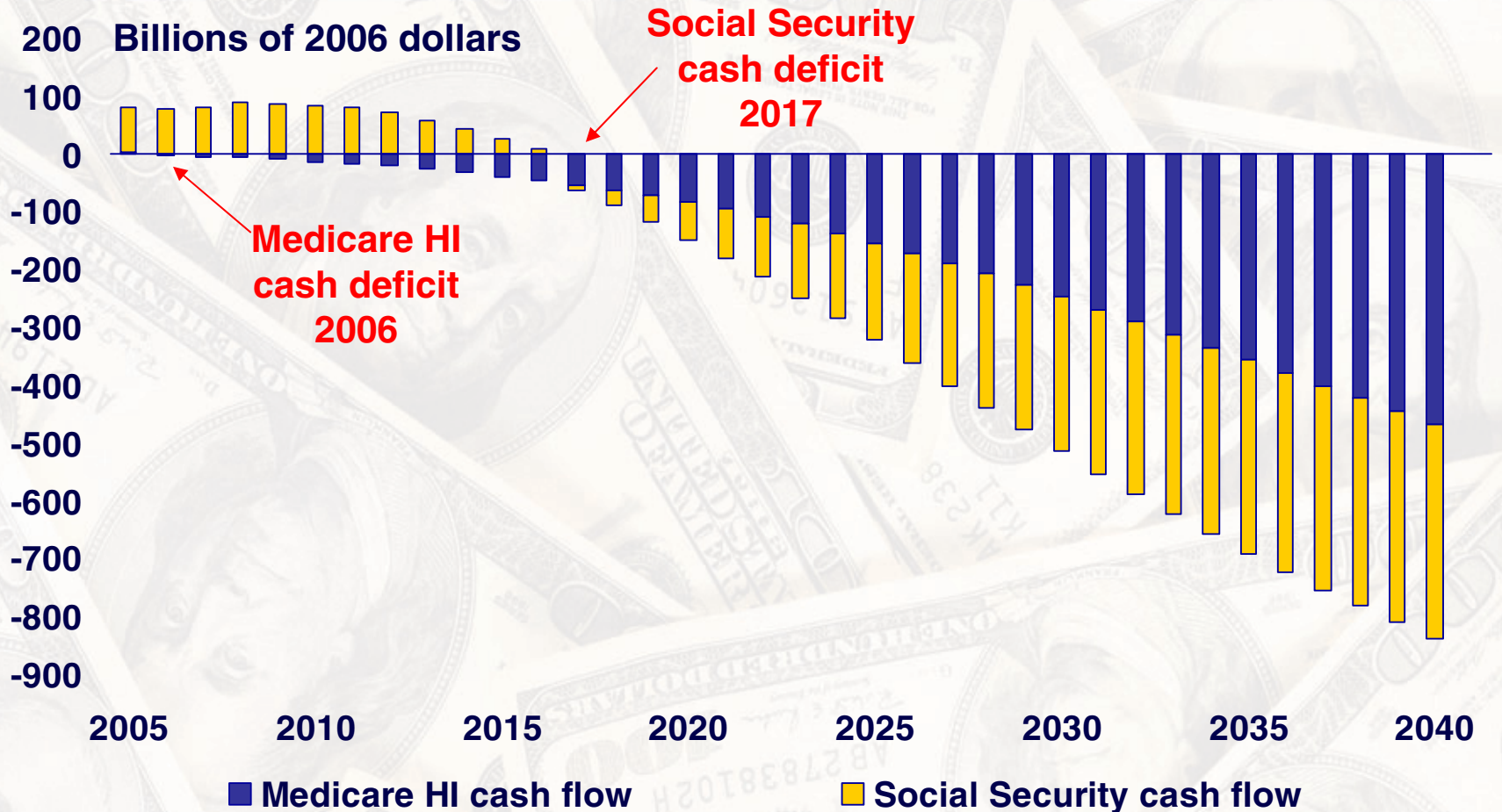
- **Impact on the Economy**
  - Larger labor force
  - Additional economic growth
- **Impact on the Federal Budget**
  - Additional tax revenue
  - Reduced expenditures: Social Security & Medicare
- **Impact on Individuals**
  - Enhanced retirement security and quality of life

# Why Older Americans Don't Work Longer

- **Cultural Expectation to Retire in Mid-60s**
  - Social Security early retirement age is 62
  - Many private pensions have similar or lower eligibility ages
- **Older Americans Perceive Few Opportunities**
  - Few older workers felt they had opportunities for partial retirement
  - Most older workers and retirees saw low wage, low skilled jobs as their primary employment opportunities
- **Most Employers Do Not Make a Special Effort to Hire and Retain Older Workers**
  - Many employers say they are willing to implement policies to recruit and retain older workers, but few have actually done so
  - Employers cite barriers, such as federal pension regulations, to flexible employment options for older workers



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



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.

Note: Projections based on the intermediate assumptions of the 2006 Trustees' Reports. The CPI is used to adjust from current to constant dollars.

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

Date			Event
OASI	DI	OASDI	
2009	--	2009	Cash surplus begins to decline
2018	2005	2017	Annual benefit costs exceed cash revenue from taxes
2028	2013	2027	Trust fund ceases to grow because even taxes plus interest fall short of benefits
2042	2025	2040	Trust fund exhausted

Sources: Social Security Administration, *The 2006 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds* (Washington, DC: May 2006).

# 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

# Possible Way Forward on Social Security Reform

Hold harmless those who are near retirement or already retired and make a number of adjustments that would affect younger workers

- Phase-in an increase in the retirement age and index it to life expectancy
- Modify income replacement and/or indexing formulas for middle and upper income earners
- Strengthen the minimum benefit
- Increase the taxable wage base, if necessary
- Consider supplemental individual accounts and mandatory individual savings on a payroll deduction basis (e.g., a minimum 2 percent payroll contribution and a program designed much like the Federal Thrift Savings Plan with a real trust fund and real investments)

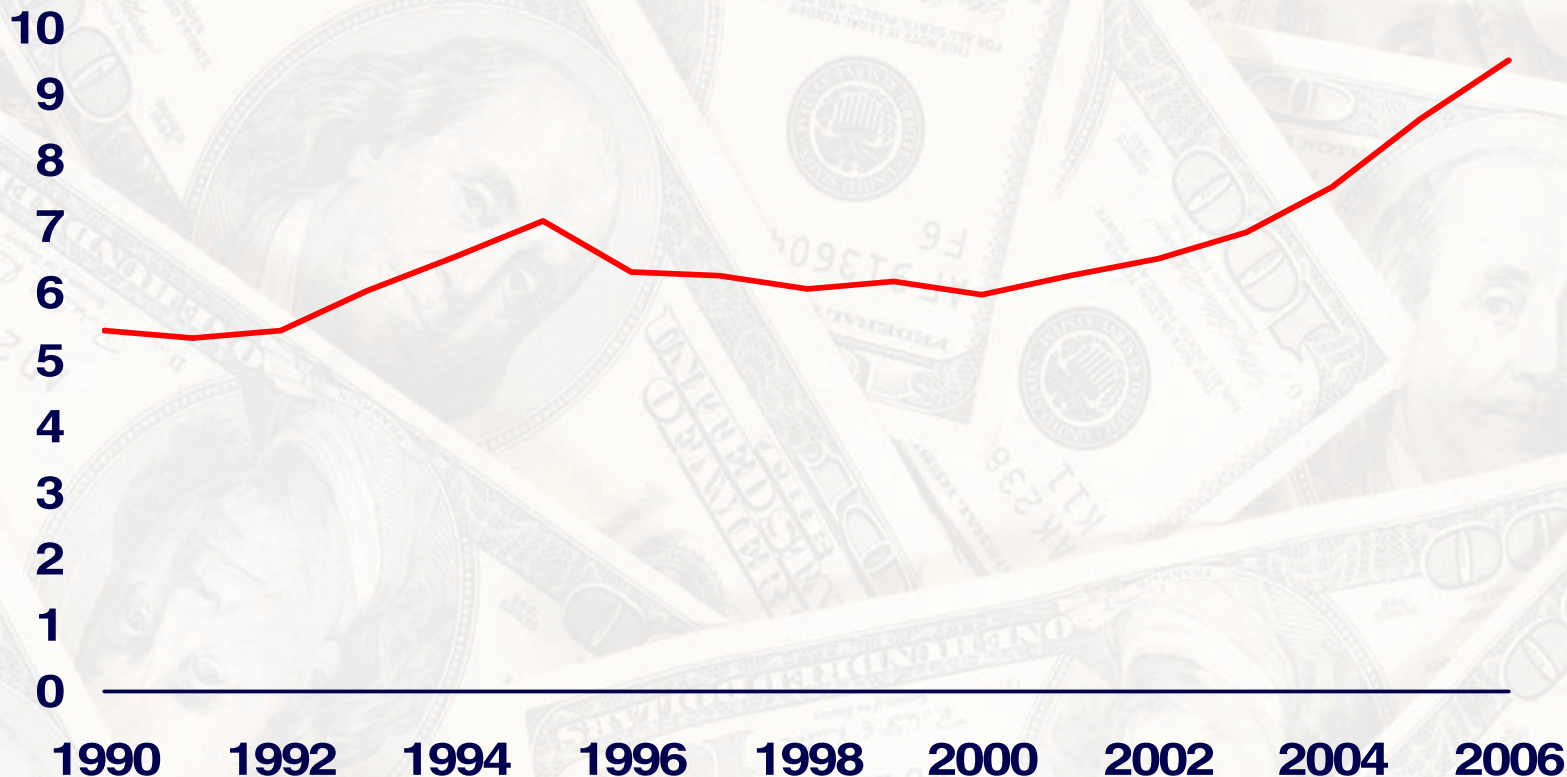
# Key Dates Highlight Long Term Challenges of the Medicare Program

Date	Event
2006	Medicare Part A outlays exceed cash income
2007	Estimated trigger date for “Medicare funding warning”
2012	Projected date that annual “general revenue funding” for Part B will exceed 45 percent of total Medicare outlays
2018	Part A trust fund exhausted, annual income sufficient to pay about 80% of promised Part A benefits

Source: 2006 Annual Report of The Boards of Trustees of The Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds (Washington, DC, May 2006).

# SMI Premium as Share of Average Social Security (OASI) Benefit

Percent of average OASI benefit

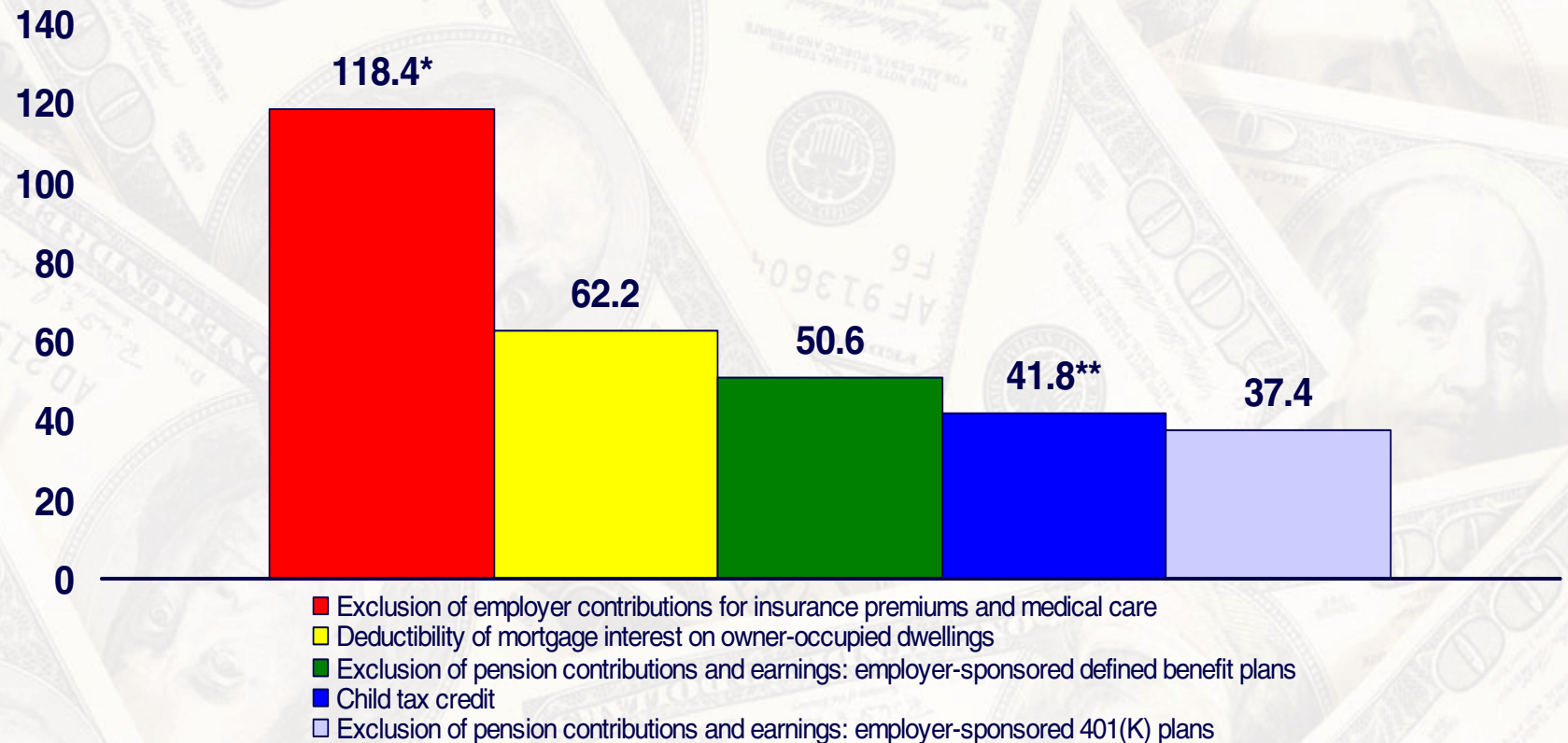


Source: CMS, Office of the Actuary.

Note: Data for 2006 are based on the announced SMI monthly premium of \$88.50 and do not include the Medicare Prescription Drug premium. In August, the Centers for Medicare & Medicaid Services estimated that the national average monthly premium for prescription drug coverage equivalent to the Medicare standard coverage would be \$32.20.

# Health Care Is the Nation's Top Tax Expenditure in Fiscal Year 2005

Estimated dollars in billions



Source: Office of Management and Budget (OMB), *Analytical Perspectives, Budget of the United States Government, Fiscal Year 2007*.

Note: "Tax expenditures" refers to the special tax provisions that are contained in the federal income taxes on individuals and corporations. OMB does not include forgone revenue from other federal taxes such as Social Security and Medicare payroll taxes.

\*If the payroll tax exclusion were also counted here, the total tax expenditure for employer contributions for health insurance premiums would be about 50 percent higher or \$177.6 billion.

\*\*This is the revenue loss and does not include associated outlays of \$14.6 billion.

# Issues to Consider in Examining Access, Cost, Quality, and Personal Responsibility Challenges

- In reforming our health care system, the public needs to be educated about the differences between **wants**, **needs**, **affordability**, and **sustainability** at both the individual and aggregate level.
- Ideally, health care reform proposals 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.



# Possible Objectives of Health Care Reform

## Access

- Develop a core set of basic and essential services with universal access that can be provided by employers, unions, and professional organizations at group rates — supplemental coverage could be available as an option but at a cost. Use the Federal Employees Health Benefits Program (FEHBP) as a possible model

## Cost

- Limit the percentage of the federal budget that can be dedicated to health care

## Quality

- Take steps to achieve above average outcomes on key indicators of well being (e.g., infant mortality, life expectancy, and medical error rates)

## Personal Responsibility

- Encourage individuals to assume more personal responsibility for healthy lifestyles

# Selected Potential Health Care Reform Approaches

- Reexamine the scope, timing, and structure of Medicare Prescription Drug Benefit
- Consider re-imposing some limits on direct advertising on prescription drugs
- Consider some limited importation of prescription drugs from selected countries
- Leverage the government's purchasing authority to foster value-based purchasing for health care products and services
- Foster more transparency in connection with health care costs and outcomes, including leveraging of technology while protecting privacy
- Encourage case management approaches for people with expensive acute and chronic conditions to improve the quality and efficiency of care delivered and avoid inappropriate care

# Selected Potential Health Care Reform Approaches

- Foster more preventative care and wellness services and capabilities, including fighting obesity and encouraging better nutrition
- Develop a set of national practice standards to help avoid unnecessary care, improve outcomes, and reduce litigation
- Revise certain federal tax preferences for health care to encourage the efficient use of appropriate care
- The federal government should seek to lead by example in connection with reforming the health care programs for which it is responsible (e.g., VA, DOD, FEHBP)
- Limit spending growth for government-sponsored health care programs (e.g., percentage of the budget and/or the economy)
- Pursue multinational approaches to investing in health care R&D
- Promote broad-based access to basic and essential health care services and efficient health care delivery models
- Provide additional cost sharing mechanisms for individuals; create insurance pools for alternative levels of coverage, as necessary
- Weigh the reform options for accessing and financing long-term care (e.g., assess the potential role of social insurance and recognize the benefits, burdens, and costs of informal care-giving)

# Four National Deficits

- ***Budget***
- ***Balance of Payments***
- ***Savings***
- ***Leadership***

# Key Leadership Attributes Needed for These Challenging and Changing Times

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



# Fiscal, Social Security, and Health Care Challenges

The Honorable David M. Walker  
Comptroller General of the United States  
Awakening Conference  
Sea Island, GA  
January 7, 2007

---

## On the Web

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

---

## Contact

Paul Anderson, Managing Director, Public Affairs  
[AndersonP1@gao.gov](mailto:AndersonP1@gao.gov) (202) 512-4800  
U.S. Government Accountability Office  
441 G Street NW, Room 7149  
Washington, D.C. 20548

---

## Copyright

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.