THE CONCORD COALITION

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Exploring Solutions to Our Long-Term Fiscal Challenges

Senate Budget Committee

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Chairman Conrad, Senator Gregg, and members of the Committee, thank you for inviting me to discuss solutions to the nation's long-term fiscal challenges. It is an important issue for the future health of the economy, generational equity, and the ability of all Americans to enjoy rising standards of living.

I am here representing The Concord Coalition, a nonpartisan organization dedicated to strengthening the nation's long-term economic prospects through sound and sustainable fiscal policy. Concord's co-chairs are former senators, Warren B. Rudman (R-NH) and Bob Kerrey (D-NE). They, along with Concord's President former Commerce Secretary Peter G. Peterson and our nationwide membership, have consistently urged Washington policymakers to produce a credible plan for long-term fiscal sustainability.

In that regard, let me express The Concord Coalition's strong appreciation and support for your recently expressed commitment to work in a bipartisan way to achieve this important goal. We hope it will inspire others.

My testimony today will address key aspects of the long-term challenge and potential strategies for dealing with it. Specifically, I will discuss the importance of:

- Restoring a balanced budget
- Reforming Social Security and Medicare
- Ensuring an adequate revenue stream
- Budget process reform
- Bipartisan cooperation, and
- Public engagement:

I. Overview

All Americans, regardless of political party or ideological perspective, want to leave a more prosperous, secure and compassionate nation to future generations. Yet, we are putting our nation's future at risk with an unsustainable fiscal policy that promises more debt than prosperity, a level of taxation that we would not tolerate for ourselves and diminished prospects for families to enjoy a higher standard of living.

Beyond fiscal imbalance, today's budget policies threaten to place ever-tighter constraints on the ability of future generations to determine their own priorities or to meet challenges that cannot be foreseen. As the share of federal resources pledged to retirement and health care benefits grows, it will leave shrinking amounts for all other purposes. Generational fairness requires a major course correction.

The real choices require scaling back future health care and retirement promises, raising revenues to pay for them or some combination of both. Americans may have very different views about whether it would be better if the federal government were both taxing and spending at 18 percent of GDP or both taxing and spending at 30 percent of GDP. No one, however, would advocate that the government tax at 18 percent of GDP and spend at 30 percent. This would certainly shatter the economy. Yet, this is the future we are now embarked upon.

While there is no quick fix, there are things we can begin doing now that will result in a much brighter picture for future generations. These do not include "slashing" entitlements or "killing the economy with tax increases." They do require that everything be on the table. The Concord Coalition recently published an open letter to the President and Congress recommending that the following steps be taken immediately:

- Negotiate a bipartisan balanced budget plan
- Begin a bipartisan process to address long-term fiscal challenges
- Restore budget caps and pay-as-you-go rules for new spending and tax cuts, and
- Include long-term projections in the budget resolution

The full text of our letter is attached. Let me elaborate on these points and underscore the importance of public engagement in exploring solutions.

II. Balancing the budget is an important first step

As the process gets underway, you will be bombarded with countless proposals for increased spending and demands to preserve and extend many tax cuts. Considered in isolation, many of these proposals will seem worthwhile. Unfortunately we can't have it all. Without the discipline imposed by a balanced budget goal, deficits will be higher and last longer than they would otherwise.

Just as a family anticipating major new expenses, such as a home purchase or college education, must begin to save for these financial obligation, the federal government should be taking steps now to improve its fiscal position in anticipation of the costs associated with the retirement of the baby boom generation.

The most direct action the federal government can take in this regard would be to eliminate the drain on savings caused by the federal budget deficit. Restoring budget balance would lower government borrowing from the financial markets and provide a much needed boost in national savings to help the budget and the economy meet the challenges of an aging population. Working toward the goal of a balanced budget would also provide greater flexibility in the future by reducing interest payments and reducing our reliance on foreign lenders.

Aside from being fiscally responsible, balancing the budget is the goal most likely to be broadly understood, supported and enforced. It is also the most generationally responsible goal. Americans understand that it is wrong to provide ourselves with more government services than we are willing to pay for and then send the bill to our children. The best way to avoid such unjust burden shifting while laying a solid long-term foundation for a strong economy is to adhere as much as possible to the balanced budget goal.

A good first step in improving the budget outlook is to identify savings from eliminating wasteful and unnecessary programs and increasing the efficiency of other government programs as well as eliminating narrowly targeted tax breaks that add to the complexity of the tax code without producing meaningful economic benefit. Such provisions divert resources from more pressing national needs and increase public cynicism about the fairness of the federal budget.

Similarly, as this Committee highlighted in a recent hearing, there is the potential for increased revenues by closing the "tax gap" — the difference between taxes that are owed and the revenues that are actually collected.

While there is the potential for savings in these areas, such relatively painless options will not be enough to get the job done. A serious effort to address the near term deficits will require policymakers to tackle the underlying structural deficit resulting from existing tax and spending policies. Moreover, it will do no good to adopt a balanced budget plan on paper if it is not based on an honest assessment of such items as ongoing military operations, the revenue hole left by reforming the Alternative Minimum Tax (AMT) and all other projections.

There is at least one positive thing to report on the budget front: at $248 billion (1.9 percent of GDP), the deficit in fiscal year 2006 was lower than the $319 billion deficit in 2005 (2.6 percent of GDP). It was the second year in a row that the deficit declined. Another modest decline can be expected in the current year. This does not mean, however, that we are on a smooth and easy road back to balanced budgets.

Budget projections are uncertain, but under plausible assumptions about current trends, deficits would total roughly $5 trillion through 2017. This assumes that funding in Iraq is phased down but not out, that all expiring tax cuts are extended, that regular appropriations grow at the same rate as the economy rather than inflation, and that the Alternative Minimum Tax (AMT) is adjusted for inflation. It also assumes a healthy economy.

Under that scenario, deficits would steadily rise to nearly 4 percent of GDP by 2017. Persistent deficits of that size, while not unprecedented, are nevertheless harmful and would come at a very bad time. They would drain national savings, raise the debt to GDP ratio and increase interest costs at the very time when we should be doing the opposite in preparation for the looming fiscal challenges as the baby boomers retire and entitlement spending balloons.

As government debt increases, interest costs grow as well. These costs add to government spending and are paid for with tax dollars. Interest costs totaled $227 billion in fiscal year 2006. It was the fastest growing major spending category in the federal budget, increasing by 23 percent. We spent more on interest in 2006 than we did on either the federal government's share of Medicaid ($181 billion) or appropriations for military operations in Iraq and Afghanistan ($120 billion). All of this is occurring as we enter our fifth year of economic recovery and with two years of very strong revenue growth.

All of this illustrates the difficulty of achieving your goal, which the President share, of balancing the budget by 2012 while at the same time using realistic cost estimates for current policies. .

A sustainable deficit reduction effort will require all parties to compromise. Starkly partisan budget proposals may appeal to true believers and party loyalists, but a plan to reduce the deficit is unlikely to succeed over the long-term without sufficient political will to enforce it. A successful plan must be capable of resisting pressure to undo the tough choices it contains. The best way to ensure that a plan can stand up over time is to infuse it with broad bipartisan support from the beginning. As the Concord Coalition Board of Directors stated in a December, 2005 statement:

> "If everyone insists on only cutting someone else's priorities, talk about deficit reduction will remain just that. The best way to end this standoff is to agree on the common goal of deficit reduction, put everything on the table—including entitlement cuts and tax increases—and negotiate the necessary trade-offs."

III. Reduce long-term entitlement costs

Getting the short-term deficit under control is only the first step. Even with a near-term balanced budget plan, fiscal policy would remain unsustainable over the long-term. The structural imbalance between future benefit promises for retirement and health care programs and the revenues projected to pay for them must be addressed head-on.

The primary source of the nation's long-range fiscal strains is the rising cost of heath care and retirement programs. Thus, the most effective long-range solutions would be those that constrain the growth of these programs. This will require difficult choices regarding who should receive benefits, what level of benefits can be provided and how those benefits should be delivered.

Any strategy for fiscal sustainability will require reform of our two largest and most popular public programs: Social Security and Medicare. Moreover, the choices that are made in this regard should not be made in a vacuum. Social Security and Medicare tax the same people (mostly workers) to pay benefits to the same people (mostly retirees). What matters fiscally and economically is the combined total cost of these programs. Because controlling health benefit spending will be so difficult, it is all the more urgent to save what we can in Social Security.

a. Social Security reform

There is no good reason why Social Security reform should be kept off the 2007 legislative agenda. The demographic and fiscal challenges facing Social Security in the years ahead are well known. It is understandable that people will disagree on the details of any reform plan. What's needed now, however, is rejection of the "Do Nothing Plan."

It is worth recalling that President Bush is not the first president in recent years to put Social Security on the political agenda. In 1998, President Clinton made Social Security reform one of his top domestic priorities. Here is how President Clinton summarized the problem at a forum hosted by The Concord Coalition and AARP in July 1998:

> We dare not let this disintegrate into a partisan rhetorical battle. Senior citizens are going to be Republicans and Democrats and independents. They're going to come from all walks of life, from all income backgrounds, from every region of this country, and therefore, so will their children and their grandchildren. This is an American challenge and we have to meet it together.

Any Social Security reform plan should be designed to meet three fundamental objectives — ensuring Social Security's long-term fiscal sustainability, raising national savings, and improving the system's generational equity:

- **Reform should ensure Social Security's long-term fiscal sustainability.** The first goal of reform should be to close Social Security's financing gap over the lifetimes of our children and beyond. The only way to do so without burdening tomorrow's workers and taxpayers is to reduce Social Security's long-term cost.

- **Reform should raise national savings.** As America ages, the economy will inevitably have to transfer a rising share of real resources from workers to retirees. This burden can be made more bearable by increasing the size of tomorrow's economy. The surest way to do this is to raise national savings, and hence ultimately productivity growth. Without new savings reform is a zero-sum game.

- **Reform should improve Social Security's generational equity.** As currently structured, Social Security contributions offer each new generation of workers a declining value ("moneysworth"). Reform must not exacerbate--and ideally it should improve--the generational inequity underlying the current system.

Meeting these objectives will require hard choices and trade-offs. There is no free lunch. Policymakers and the public need to ask the following questions to assess whether reforms honestly face up to the Social Security challenge--or merely shift and conceal the cost:

- **Does reform rely on trust-fund accounting?** Trust-fund accounting obscures the magnitude and timing of Social Security's financing gap by assuming that trust-fund surpluses accumulated in prior years can be drawn down to defray deficits incurred in future years. However, the trust funds are bookkeeping devices, not a mechanism for savings. The special issue U.S. Treasury bonds they contain represent a promise from one arm of government (Treasury) to satisfy claims held by another arm of government (Social Security.) They do not indicate how these claims will be satisfied or whether real resources are being set aside to match future obligations. Thus, their existence does not, alone, ease the burden of paying future benefits. The real test of fiscal sustainability is whether reform closes Social Security's long-term annual gap between its outlays and its dedicated tax revenues.

- **Does reform rely on hiking FICA taxes?** Hiking the payroll tax rate to meet benefit obligations is neither an economically sound nor a generationally equitable option. The burden will fall most heavily on lower and middle-income workers and on future generations. A popular alternative to an across-the-board increase is to make more of the earnings of higher income workers taxable by raising the cap on taxable wages. Currently, the Social Security payroll tax (12.4 percent) is capped at $97,500 of wages. This would bring in more money, but as a means of assuring the program's sustainability, raising this cap would be considerably less effective than proponents allege. It would only provide a few more years of positive cash flow to the system and, unless the link between taxable earnings and benefits were to be eliminated, it would add to the system's long-term cost by providing higher benefits to those who need them the least.

- **Does reform rely on new debt?** Paying for promised benefits--or financing the transition to a more funded Social Security system--by issuing new debt defeats a fundamental purpose of reform. To the extent that reform relies on debt financing, it will not boost net savings and may result in a decline. Without new savings, any gain for the Social Security system must come at the expense of the rest of the budget, the economy, and future generations. Resort to borrowing is ultimately a tax increase for our kids.

- **Does reform rely on outside financing?** Ideally, reform should achieve all necessary fiscal savings within the Social Security system itself. Unrelated tax hikes and spending cuts may never be enacted, or if enacted, may easily be neutralized by other measures, now or in the future. Unless the American public sees a direct link between sacrifice and reward, the sacrifice is unlikely to happen.

- **Does reform use prudent assumptions?** There must be no fiscal alchemy. The success of reform should not depend upon rosy projections of future economic growth, presumed budget surpluses or lofty rates of return on privately owned accounts. All projections regarding private accounts should be based on realistic assumptions, a prudent mix of equity and debt, and realistic estimates of new administrative costs.

While fixing Social Security's problems, reform must be careful to preserve what works. Social Security now fulfills a number of vital social objectives. Policymakers and the public need to ask the following questions to assess whether reform plans would continue to fulfill them:

- **Does reform keep Social Security mandatory?** The government has a legitimate interest in seeing that people do not under-save during their working lives and become reliant on the safety net in retirement. Moving toward personal ownership need not and should not mean "privatizing" Social Security. Any new personal accounts should be a mandatory part of the Social Security system. Choice is not important in a compulsory social insurance program whose primary function is to protect people against poor choices.

- **Does reform preserve Social Security's full range of insurance protection?** Social Security does more than write checks to retirees. It also pays benefits to disabled workers, widows, widowers, and surviving children. A reformed system should continue to provide insurance protection that is at least equal to what the current system offers.

- **Does reform maintain Social Security's progressivity?** While individual equity ("moneysworth") is important, so too is social adequacy. Social Security's current benefit formula is designed so that benefits replace a higher share of wages for low-earning workers than for high-earning ones. Under any reform plan, total benefits, including benefits from personal accounts, should remain as progressive as they are today.

- **Does reform protect participants against undue risk?** Under the current system, workers face the risk that future Congresses will default on today's unfunded pay-as-you-go benefit promises. While reducing this "political risk," personal account reforms should be careful to minimize other kinds of risk, such as investment risk, inflation risk, and longevity risk--that is, the risk of outliving ones assets.

Any genuine reform has a fiscal and political price, so it's tempting to pretend that the status quo can continue indefinitely. It can't. Today's Social Security system promises far more in future benefits than it can possibly deliver. Because of this, the proper comparison for any reform plan is between the benefits payable under a reformed system and the benefits payable under the status quo. No realistic reform plan looks good when compared to the false hypothetical of a perfectly solvent system. It is fundamentally unfair to judge any reform plan against a standard that assumes the current system can deliver everything it promises.

Moreover, in assessing the adequacy of benefits under a reformed system that includes personal accounts it must be kept in mind that a person's retirement income would come from *both* sources — a basic level of benefits from the defined benefit portion and the additional benefit financed from the lifetime accumulation of the personally owned account. In comparing benefit levels the entire benefit of a reformed system must be included.

Specific reform options that might do the job

Over the next 75 years, Social Security's revenues are projected to hover in a narrow range around 13 percent of the nation's taxable payrolls. The program's costs, on the other hand, are projected to grow rapidly from 11 percent of the nation's payrolls today to 15.5 percent in 2025 and more gradually thereafter to more than 18.7 percent by 2080.

While the conventional view is that those rising costs will be due to the aging of the population, that view is incomplete. A deliberate policy of paying ever-higher real benefits is also a significant factor. Thus, from a policy perspective, if the aim of reform is to address Social Security's financing problem at its source -- rising costs -- either adjusting the program for increasing longevity or constraining the growing value of its scheduled monthly benefits are the two most logical solutions.

The necessary savings could be achieved using some variation of the following options:

1. Raise the "normal retirement age" for full benefit eligibility

One of the most logical options to consider is raising the age for full benefit eligibility. It makes good sense for two reasons:

- Longevity is increasing steadily, and longer life spans mean longer, and more costly, benefit spans.

- In coming decades, the pool of working-age Americans will virtually stop growing, depriving our nation of this engine of economic growth. Raising the full benefit-eligibility age could help augment the labor force by encouraging older people to remain at work for a few more years.

It's conventional wisdom that our population soon will be growing older because the huge baby boom generation is poised to begin retiring. But that's only part of the picture. The problem posed by an aging population is not just that benefit spans will lengthen. We also expect to be coping with a labor shortage. Instead of increasing our supply of working age people by 2 percent each year as in recent decades, or even the current 1.5 percent rate today, between 2010 and 2050, workforce growth will slow to a crawl: just 0.3 percent per year.[1]

Growing our economy could help finance benefits for a mushrooming retiree population. But, boiled down to essentials, economic growth depends on two factors: increasing the number of workers, and increasing how productive each worker is. Since no one has a sure-fire recipe for boosting worker productivity enough to make up for the slowdown in workforce growth, anything we can do to encourage people to work a few more years and encourage employers to accommodate older workers will help our economy.

2. Index for Longevity

Any reform plan should also index initial benefits to changes in elder life expectancy. Without this provision, Social Security will once again drift out of balance; with it, the system's long-term cost will be stabilized relative to worker payroll.

Social Security retirement benefits are paid in the form of a defined benefit annuity. An annuity purchased with a defined contribution personal account balance would naturally take into account expectations about future longevity. The more years the annuity provider expects to have to pay benefits, the smaller the annual benefit a given account balance would buy. The current Social Security system makes no such adjustment. The benefit annuity it promises is set by a formula that yields the same result no matter how fast and far life expectancy rises. Cutting benefits by a fixed percentage may balance the system for a while. But unless reform also adjusts benefits for ongoing gains in life expectancy, the system will drift out of balance again.

3. Change the formula for determining initial benefits

a. Bend points

The determination of a retiree's initial Social Security benefit check is based on the calculation of Averaged Indexed Monthly Earnings (AIME). The amount of money earned by an individual each year of work is multiplied by the increase in average wages that has occurred up to the year of eligibility for Social Security, and then the average of the highest 35 years (fewer for those receiving disability benefits) of indexed wages is taken and divided by 12 to get the AIME.

Once the AIME is calculated, the Primary Insurance Amount (PIA) is determined by applying the "primary insurance amount formula." This progressive formula is designed to replace a share of annual pre-retirement income based on three "bend points." (90 percent, 32 percent, and 15 percent.) For example, in 2007 the replacement rates are 90

[1] Social Security 2006 Trustees Report, Table V.B2, Additional Economic Factors.

percent of the first $680 of average monthly earnings, 32 percent for earnings up to $4,100, and 15 percent of higher earnings up to the taxable maximum.

One way to reduce Social Security's long-term cost would be to lower the bend points across the board. Or if preferred, reduce the replacement rate within each bend point bracket on a progressive basis that would protect low-income workers. This later approach would work particularly well with a system of personal accounts, which in the absence of some other mechanism such as savings matches paid out of general revenues, would make the overall system less progressive than it is now.

b. Price-indexing

Another option would be to index initial benefits to the growth in prices (CPI) rather than to the growth in wages. Under current law, initial benefit awards are indexed to wages--that is, the wage history on which benefits are based is updated at the time of retirement to reflect the rise in the economy's overall wage level over the course of the beneficiary's working career.

In effect, wage-indexing ensures that the living standard of retirees keeps pace with society's overall living standard. Re-indexing initial benefit awards to prices merely ensures that the absolute purchasing power of retirees keeps up with inflation. Note that this reform effects only initial benefit awards; current benefits are already price indexed.

The reform has two advantages: its simplicity and its large savings. If real wages are growing 1 percent per year faster than inflation, price indexing will result in a roughly 35 percent cut in initial benefits relative to current law for the first cohort to spend a complete career under the new regime. Under this assumption, the savings would be roughly sufficient to close Social Security's long-term cash deficit.

Under current law, it is virtually impossible to close Social Security's deficit through an acceleration in productivity growth. Higher productivity would result in higher wages and this would boost payroll tax revenue. But higher wages would also result in higher benefits, and this would largely cancel out the gain. With price-indexing, however, benefits would shrink indefinitely relative to taxable payroll and GDP — and the faster wages grow, the more benefits would shrink as a share of the economy.

This dynamic, of course, means that the living standards of retirees will diverge from those of the working population. To the extent that we view Social Security as a pure floor of projection, this does not pose a public policy problem. To the extent that we view it as an income replacement program, it does.

For this reason, price-indexing makes most sense as part of an overall reform that also incorporates funded benefits like personal accounts. The price indexed pay-as-you-go benefit would ensure that the purchasing power of benefits would remain the same for each new generation of retirees. The funded benefits would help ensure that the relative living standard of retirees is not eroded. The rate of return to a funded system, after all, is the rate of return to capital and historically, this has been faster than the rate of growth in wages.

4. Treat Social Security Benefits Like Private Pensions for Tax Purposes

Making 85 percent of all benefits taxable is fair, and should be on the table as a means of increasing Social Security's revenues. The 85 percent taxability rule that now applies to beneficiaries with incomes over high thresholds could apply to all beneficiaries. The 15 percent exemption reflects an estimate of the dollar value of most beneficiaries' prior FICA contributions that have already been subject to personal taxation. It would thus bring the tax treatment of Social Security in line with the tax treatment of private pension benefits.

Since this provision would affect only those households with enough income to pay income taxes, it would maintain the progressivity of the program. It's worth noting that because current law does not index the thresholds at which benefit taxation applies, a rising share of total OASDI benefits are now becoming taxable--and eventually 85 percent of all benefits will be taxable. Full benefit taxation is therefore already due to be instituted in the future (and future revenues from it are already included in current projections). What this option would do is to move to full benefit taxation right away.

The new revenue from this provision is not large but it is available immediately and thus generates critical near-term budget savings, which may be needed for the transition costs of any reform plan.

5. Affluence test

An affluence test for upper income beneficiaries could be designed as an alternative to full benefit taxation and generate roughly the same aggregate savings in every future year, which makes the two provisions substitutable. The appeal of full benefit taxation is its simple equity: It would merely subject Social Security beneficiaries to the same tax code as everyone else. The possible drawback is that it reaches deep down into the middle class. The appeal of the affluence test is its greater progressivity. The possible drawback is that it may be regarded as arbitrary.

6. Tax options

Raising future taxes is certainly a substantive option, and one that is more fiscally responsible than unlimited borrowing, but it ignores or dismisses the magnitude of the looming demands that Social Security and other entitlements will place on the income of future workers. Levying higher taxes to meet those costs could hinder an economy that will also have to cope with near stagnant workforce growth.

Yet even assuming that future workers will be able to afford higher taxes, there is another more fundamental reason why this should not be the first option for reform -- it is generationally inequitable.

Ultimately, choosing to raise future taxes to meet current law costs is similar to borrowing in that it places a claim on the expected earnings of today's children -- in effect confiscating their economic progress. If future generations want to sustain these higher costs it should be their choice, not the consequence of the current generation's refusal to plan responsibly for a known problem.

Financing current law benefit promises, for Social Security, Medicare and Medicaid would add about 8 percent of GDP to the federal tax burden by 2040 even under conservative assumptions. Will the American public in the future accept a permanent level of taxation that is 40 to 50 percent higher than it has been over the past 40 years?

Maybe it will, but there is no guarantee. Thus, aside from the dubious generational ethics of deciding today how our children should spend their money, relying on tax increases to fund current law benefit promises risks an intractable political dilemma for future lawmakers -- choosing between unacceptable tax levels or abrupt benefit cuts.

Some advocate getting the wealthy to contribute more by raising, or eliminating, the payroll tax cap on wages, now at $97,500. A modest increase in the wage base would bring in a modest amount of new revenue, but wouldn't do much to reduce the system's long-term cash deficit. Eliminating the cap would have a bigger impact, but would substantially alter Social Security's traditional focus on both fairness to individuals and protection of the needy. It would destroy the whole presumption of a contributory system--that what people get back be at least somewhat proportional to what they pay in.

Payroll tax increases should only be considered within the context of a comprehensive plan that lowers long-term costs. Higher revenues today will do nothing to lessen Social Security’s future burden without a mechanism to ensure that the extra money is translated into higher savings and a larger future economy rather than higher spending on current government programs.

7. Personal account options

One potential mechanism for devoting higher contributions to new savings would be the creation of personally owned accounts within the Social Security system. This reform has could increase savings by providing a more reliable method of pre-funding benefit promises than government trust funds. It would provide a lockbox no politician could pick.

The current system provides a *statutory* right to benefits that Congress can cut at some future date. Personally owned accounts would offer workers ownership of constitutionally protected property. The funds would be put beyond the reach of government. Congress could not double-count personal account assets in the budget.

However, personal accounts are not a free lunch. Money to fund them must come from somewhere. To the extent that the source of funding is additional government borrowing, no new savings for the economy will result because the increase in government borrowing would cancel out the "savings" in personal accounts. Without new savings, any gain for the Social Security system must come at the expense of the rest of the budget, the economy, and future generations.

Moreover, individual accounts alone do nothing to close the existing gap between dedicated revenues and promised benefits. In any true transition to a funded system, workers will have to pay more, retirees will have to receive less, or both. Reform plans that do not face up to this transition cost will not result in new net saving or a larger economy.

Personal account reforms come in two basic types: "carve outs" and "add ons." In a carve out, a portion of the current payroll tax would be diverted to personal accounts. For the carve out to result in genuine funding, the diversion must be paid for by reductions in pay-as-you-go benefits beyond those that would need to be made in any case simply to eliminate Social Security's projected cash deficits. In an add on, the accounts would be funded partly or wholly from additional worker contributions. The contributions would be personally owned savings, and so would not constitute a tax--or at least would not function like one.

A pure carve out necessarily entails cuts in current-law Social Security benefits. Because personal account contributions would earn a higher return than contributions to the existing system, a carve-out plan might be able to pay retirees higher total benefits than today's purely pay-as-you-go system can <u>afford</u>. However, it cannot guarantee that retirees will receive everything that the existing system <u>promises</u>. In practice, most personal account carve outs rely on borrowing to substitute for the lost FICA revenue and mitigate benefit cuts. To be sure, reform plans that rely on debt financing usually promise that the debt will be paid back. But in most plans the borrowing is so large and the payback is so distant that it doubtful the payback will ever occur.

The "add on" approach offers a way to ensure the adequacy of future benefits without recourse to budgetary shell games. In fact, with a 2 percent of payroll add on it may be possible to ensure that every cohort of workers will receive benefits at least as large as what current law now promises but cannot afford. Is it worth paying a bit more to achieve these superior results? In the end, after all the shell games are played out, this is the central choice that the American public must confront.

To be clear, current law must eventually result in either a cut in benefits or a hike in taxes. If the choice is to avoid any hike in the Social Security contribution rate, a personal accounts carve out might generate larger benefits than today's pay-as-you-go system can afford. If the choice is to avoid any reduction in promised benefits, an add on might allow for this at a lower ultimate contribution rate. It is impossible to have it both ways: no cuts in total benefits and no new contributions.

Transitioning out of the current pay-as-you-go system into a partially funded system, with or without personally owned accounts, inevitably requires some group of workers to pay for the pre-funding of the new system while at the same time maintaining funding for those still receiving benefits under the old system. There is no avoiding this cost. Workers will thus have to save more, retirees will have to receive less, or both.

Medicare reform

Medicare is in worse shape than Social Security. We must engage on a bipartisan basis to make Medicare both effective and affordable over the long-term.

As currently structured, Medicare is financially unsustainable. Costs are growing faster than the payroll taxes and premiums that finance the program. Costs are also growing faster than the overall economy, and faster than can be reasonably supported by the federal budget unless spending priorities change dramatically.

Restraining the cost of the health care entitlements poses a greater challenge for policymakers than Social Security because the cost of delivering health care benefits is much more difficult to predict and control than simply providing cash benefits.

Health care costs are rising faster than wages. Consequently, the payroll taxes that fund Medicare are falling short of program costs. At the same time, the number of beneficiaries will climb steeply when the baby boom generation begins receiving benefits in 2011. Moreover, people who reach age 65 are living longer. People aged 85 and older are the fastest growing segment of our population. Medicare spending averages more than twice as much for people over 85 as it does for those age 65.

The addition of Medicare's prescription drug benefit merely compounded the program's shaky financial foundation. According to the Congressional Budget Office, the prescription drug benefit will have a net cost of $42 billion in FY 2008 and $270 billion over the next five years. More importantly, estimates indicate that the future obligations of the Medicare Part D drug benefit are roughly 50 percent more than those of the entire Social Security program. Congress and the President must look for ways to make the benefit more efficient, better targeted and less expensive.

Putting the Medicare program on a financially sustainable path will require some combination of reductions in services, increased cost-sharing by beneficiaries, increasing the eligibility age, bringing more revenues into the system and improving the cost effectiveness of Medicare and the health care system overall. We cannot pretend that there are simple fixes that don't require anyone to give anything up such as clamping down on fraud, or cutting back on excessive paperwork, or eliminating all the unnecessary tests and procedures. Pure "waste" is no easier to pinpoint in the health system than it is in the federal budget. And even if we could identify and eliminate all of it, the underlying cost drivers — from technology to expectations to aging — would soon cause spending to grow again as fast or faster than before.

Health care spending on the elderly will continue to grow faster than the economy so long as we pretend that costs can be controlled without any sacrifice. Costs aren't rising because of the proliferation of useless medical services. They're rising because medical science can do more for more people--and because what it can do is often very expensive.

Ultimately our nation must decide what level of health care we wish to provide, and how much we are willing to pay for it. A distinction must be drawn between wants and needs. Treatments that have little or no promise of achieving any appreciable improvement in a patient's well-being should not be financed with taxpayer dollars.

Setting limits in Medicare will mean moving toward a whole new paradigm--one in which prospective budgets at the program level and capitation at the beneficiary level finally compel us to make tradeoffs between health care and other national priorities.

Before thinking about specific ways to address the Medicare problem, it is important to establish a set of criteria against which various proposals can be evaluated. Listed below are the criteria that the Concord Coalition believes should guide decision makers in reforming Medicare.

- Quality care: Medicare insurance should cover a level of care that is commensurate with the care available to working age people. This does not mean that taxpayers must be expected to finance a "high option" insurance plan for all seniors. If individuals wish to purchase supplementary insurance to augment their Medicare benefits, they should be permitted to do so. However, there must be an affordable insurance plan to provide a reasonable level of medical care available to the elderly, regardless of their ability to pay.

- Fiscally responsible and generationally sustainable: No generation should have an automatic claim on taxpayer resources simply because of its chronological age. People of all ages have problems that the government could address, ranging from prenatal care, to child development and education, to job training, to old age assistance. A fiscally responsible program is one that can reasonably be expected to operate within the resources available to finance it. A program that assumes a perpetually open spigot from the Treasury gushing an ever-increasing flow of spending is not fiscally responsible. If it is decided that program costs should be permitted to increase, (i.e., filling the "donut hole" or adding long-term care) then fiscal responsibility demands that a commensurate stream of revenue be identified to pay for the program.

- Income-related cost sharing: As a group, seniors enjoy a better income and less poverty than other age groups, particularly children. Therefore, Medicare's medical insurance premiums should be geared to income levels.

- Efficient provision of medical care: Whatever new system of medical insurance for the elderly is devised, it should contain incentives for both providers and patients to use resources in a cost-effective manner. Treatments that have little or no promise of achieving any appreciable improvement in a patient's well-being should not be financed with taxpayer dollars. A distinction must be drawn between wants and needs.

- Prompt action: Changes in Medicare should be enacted promptly. Entitlement programs for the elderly are long-term commitments between the government and the citizenry. People base their behavior and make their plans based on current provisions. Therefore changes in the Medicare health insurance commitment should be undertaken in time to permit gradual changes and give people time to plan and adjust.

- Medicare changes should not be made in a vacuum: Medicare is only one of the long-term commitments citizens have made to support seniors, along with Social Security and, in the case of long-term care, Medicaid. When program reforms are considered one at a time, it is possible to ignore the ripple effect of changes in the cost or financing for other programs serving the elderly. And once a stream of revenues has been committed to pay for one of the programs on which elderly people rely, it can no longer be used to shore up other programs.

IV. Ensure an adequate revenue stream

Lower taxes are generally thought to encourage work, savings and investment, however, the economic effect of rising deficits must also be considered in assessing tax policy. Debt is not a painless alternative to taxation. In the final analysis, revenues must be sufficient to pay for the cost of government.

While reforms should be enacted that would substantially reduce the long-term growth in federal spending, it is unlikely that any realistic array of reforms will allow an aging society to hold spending to today's level. Economic efficiency requires that taxes be held relatively stable at a level sufficient to pay for public spending in all future years, regardless of whether this leads to surpluses or deficits in any given year. It makes no sense to cut taxes today if that cut will only necessitate raising taxes tomorrow.

In that regard, The Concord Coalition believes that tax cuts scheduled to expire should not be permanently extended absent a plan for long-term fiscal sustainability.

Circumstances have changed dramatically since the bulk of the tax cuts were enacted in 2001. The surplus era in which the tax cuts were enacted has been replaced by deficits and the budget faces new demands for the war on terrorism and homeland security. Moreover, no action has been taken to prepare for the costs of the baby boomers' retirement and health care needs that will begin to place a growing strain on the budget in the years ahead. In fact, the burden has been dramatically increased with the addition of a Medicare prescription drug benefit. In light of all of this, it makes sense to reassess whether we should continue all of the tax cuts enacted in the surplus era.

It has been suggested that the recent high increase in the growth rate of federal taxes proves that tax cuts have not increased the deficit because they "pay for themselves" through greater economic growth. This is a tempting theory but it is not supported by evidence. Economists from the left and right generally agree that tax cuts do not fully pay for themselves through greater economic growth. A July 2006 analysis by the U.S. Treasury Department suggested that the economic feedback from extending the 2001 and 2003 tax cuts would offset less than ten percent of the revenue loss, and would only do so if the tax cuts were offset by spending cuts, something that has neither happened nor been proposed.

Revenue growth has indeed been very impressive over the past two years, however we should not leap to the conclusion that tax cuts lead to "higher" revenue. Keep in mind:

- While 2006 revenues ($2.4 trillion) set a record in dollar terms, it represents a much lower percentage of the economy (GDP) than in 2000 — 18.4 percent of GDP as opposed to 20.9 percent.

- Revenues in 2006 were almost identical to 2000 revenues adjusted for inflation. In 2000, revenues were 2.025 trillion. In 2006, revenues were $2.4 trillion, which translates to $2.029 trillion in 2000 dollars adjusted by CPI. Done in reverse, 2000 revenues would be $2.397 trillion adjusted for inflation.

- Individual income taxes are still below 2000 levels, adjusted for inflation. In 2006 individual income taxes totaled $1.04 trillion, which translates to $894 billion in 2000 dollars, well below the $1.004 billion in individual income taxes collected in 2000. If individual income taxes had kept pace with inflation since 2000, they would be $1.189 trillion. As a percentage of GDP individual income taxes have declined from 10.3 percent in 2000 to 8 percent in 2006.

- The $2.65 trillion of spending in 2006 is also a record in dollar terms, although as a percentage of the economy spending is actually a bit lower than its average over the past 40 year (20.3% in 2006 vs. the average of 20.6%)

Setting a record for revenues in nominal dollars is not remarkable. Revenues almost always set a record in nominal dollars every year as revenues naturally increase with inflation, economic growth and other factors. What is remarkable is that the revenue record set in 2000 ($2 trillion) was not broken until 2005. Between 2001 and 2003 revenues actually declined for three years in a row for the first time since the 1920's.

Moreover, there is not an inevitable connection between tax cuts, economic growth and higher revenues. For example, in the five years following the tax increases of 1993, annual real economic growth averaged 3.8 percent. In the five years since the tax cut policies began in 2001, annual real economic growth has averaged 3.1 percent. Certainly, this does not establish that tax increases are better for the economy than tax cuts, but it does establish that tax cuts enacted over the past few years are not necessarily needed beyond their expiration date to ensure economic growth.

If the decision is made to continue the expiring tax cuts, in part or in whole, Congress should look for opportunities to fill the gap. To that end, there are other areas of tax policy that warrant consideration:

- **Raise excise taxes.** A higher gas tax increase would reduce U.S. dependence on foreign oil and encourage faster adoption of alternative fuel technology. Higher alcohol and tobacco taxes would discourage use especially among price-sensitive teenagers and young adults when these habits are most likely to form.

- **Tax excess employer-paid health insurance**. The current tax code treats the purchase of health insurance among individuals differently, favoring employer-sponsored insurance at the expense of policies purchased by individuals or the self-employed. This inequity can be addressed by removing the preference for employer-sponsored plans.

- **Limit the home mortgage deduction**. The tax-favored status of home ownership distorts investment decisions by encouraging Americans to place a disproportionate share of their savings into a home rather than other higher-yield, more productive assets like plant, equipment, education, and training. Moreover, the current high limit on mortgage interest deduction subsidizes expensive homes and provides a loophole through which taxpayers with substantial home equity can circumvent the limits on consumer or investment interest.

- **Impose a Consumption tax.** By removing the disincentives to save, a consumption tax would increase the nation's pool of savings so that funds will be available for investment and economic growth.

Spending restraint is, of course, the key to maintaining a sustainable fiscal policy and allowing future generations more of a choice in setting their own priorities. But experience has demonstrated that attempting to reduce spending simply by cutting taxes, or "starving the beast," is a failed strategy.

The tax burden is ultimately determined by the government's spending commitments and not the other way around. Whatever government spends, it must eventually pay for. Deficits merely shift the tax burden toward the future, while surpluses shift it toward the present. Unless we reduce spending over the long-term we are not really cutting taxes over the long-term but merely shifting the tax burden from ourselves to our children. The best fiscal policy is one that aims to preventing total spending, taxes or debt from reaching levels that could reduce economic growth and future standards of living.

V. Improve the budget process

Budget rules alone will never be able to solve the nation's fiscal problems, however, enforcement mechanisms can bring greater accountability to the budget process and help provide Members of Congress with the political cover to make the tough choices necessary to reduce the deficit. Pay-as-you-go rules (PAYGO) for all tax and entitlement legislation and spending caps for appropriations are proven tools for fiscal discipline. These enforcement rules, enacted in 1990 and extended in 1997 with bipartisan support, were an important part of getting a handle on the deficits in the early 1990s and getting the budget back into balance. The lesson to be learned from the overall success of the BEA is that budget process can be an important tool in achieving strategic long-term goals. Unfortunately, Congress allowed these rules to expire in 2002.

The Concord Coalition strongly supports a pay-as-you-go (paygo) rule in the House and Senate requiring entitlement expansions and tax cuts to be offset by corresponding spending cuts or revenue increases. We believe that reinstating paygo in this form, as it was originally designed, is a crucial step toward restoring fiscal discipline and preventing the daunting long-term outlook from getting any worse. We also hope that it will encourage a discussion of the tough choices that must be made, regardless of procedural mechanisms, to restore fiscal responsibility.

No budget rules will be effective, however, if they are not accompanied by a commitment to enforce them. Thus, it is critical that Congress resist the pressure to weaken them by exempting politically popular items, assuming additional costs in the baseline or routinely circumventing them when they become inconvenient. This will require policymakers to set priorities and make compromises among competing needs. Many tax and spending initiatives will need to be scaled back to fit within the amount of available offsets.

Some have argued that paygo should only apply to spending increases and not tax cuts. This would be a mistake. Fiscal discipline is a concept that applies to the budget as a whole. Any legislation that would increase the deficit should be part of the enforcement mechanisms. Since spending and tax decisions both impact the bottom line, there is no good reason to exempt either from enforcement rules. Moreover, exempting tax cuts from paygo would encourage an expansion of so-called "tax entitlements" where benefits are funneled through the tax code rather than by direct spending. Finally, exempting tax cuts from paygo encourages the false notion that debt is a painless alternative to taxes.

Adoption of a paygo rules in the House a and Senate should be followed by enactment of legislation reinstating the Budget Enforcement Act in its original and successful form, including statutory paygo and limits on discretionary spending enforced by sequestration. Reinstating statutory paygo will put additional teeth into the paygo rule by establishing a mechanism that cannot be easily waived or repealed by a future Congress. Budget enforcement rules should apply to all parts of the budget — taxes, entitlements and discretionary appropriations. Excluding any part of the budget from discipline will inevitably lead to that part of the budget becoming the escape valve for budget busting proposals.

Ideally, a new bipartisan balanced budget plan should be agreed upon and enacted along with strong enforcement mechanisms. But the fact that more needs to be done is not an excuse for doing nothing. The choice for policymakers is whether to reclaim a measure of fiscal discipline through the budget process while a more substantive plan is negotiated, or to sit by while deficits drift higher in the absence of any procedural hurdles designed to rein them in.

In Concord's view the choice is clear. We believe that reinstating strong budget enforcement rules, such as paygo, is the best step that can be taken immediately to stop digging the fiscal hole deeper.

While this would be a positive step, it falls short of addressing the central long-term budget challenge, which is constraining the cost of existing entitlement programs. Paygo requires Congress to offset the cost of new programs or expansions of existing programs. It does not apply to current-law benefits...

In fact, there is nothing in the budget process that requires Congress to review the current-law budget outlook beyond the next ten years, much less take corrective action. Every corporation in America must account for and defray the cost of its long-term commitments. But the federal government does not, even though its commitments are thousands of times larger than those of any corporation.

The current budget process encourages short-term thinking by focusing on a 5 or 10-year window. Yet, as analysts from all sides generally agree, our truly unsustainable fiscal problem stems from commitments that extend far into the future. You could take a major step in improving the transparency of our future obligations and encourage actions to deal with them by including in the budget resolution targets and estimates of your policy proposals stretching out for at least 40 years.

A five or ten year budget window may have been adequate back when most federal spending was appropriated annually. It is insufficient when most of the budget consists of entitlement programs set on a rising autopilot. It's time to include the long term in the budget process.

Congress should establish long-term targets for revenues and outlays by major spending category as part of the annual budget resolution. It should note how major legislative proposals assumed in the resolution would affect these targets and how the targets differ, if at all, from current law as projected by the CBO. Separate targets could be established, as a share of GDP at five-year intervals through 2040, for total revenues, defense spending, domestic discretionary spending, Social Security, Medicare, Medicaid, other entitlements, and net interest. If the targets differ from current-law projections, CBO could be required to issue a report with an illustrative menu of reform options capable of generating the proposed savings. [2]

By compelling both parties to go on record about their long-term budget priorities, it would focus Congress and the public on the nature of the choices before us—and so might pave the way for lasting reform.

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[2] See, Concord Coalition Facing Facts Quarterly, December 2006, "Beyond Paygo: How to Encourage Long-Term Fiscal Discipline," by Richard Jackson.

To be sure, this proposed reform would not actually compel Congress to raise a dime in taxes or cut a dime in spending. But then again, neither would the other reforms. Automatic triggers usually lead to fiscal shenanigans, not fiscal discipline. What's worse, they send the wrong signal. What we need is strategic vision, not arbitrary mechanisms. No Congress will ever enact an entitlement cut that it has not debated and for which the public is not prepared.

This proposal would inject strategic vision into the budget process by requiring each party to go on record about the long-term choices it would make. Those who want to leave taxes alone would have to propose large entitlement cuts. Likewise, those who want to leave entitlements alone would have to propose large tax hikes. Without some mechanism is put such choices on the record everyone can continue to ignore the long-term consequences of current policy. With it, they must begin to talk concretely about the size and shape of the government they want. Meanwhile, the CBO reform options would educate the public about the practical steps needed to get there.

VI. Establish a bipartisan process

Since the regular legislative process has been incapable of dealing with the impending fiscal crisis, some have suggested that a new bipartisan commission be appointed. This could be a useful mechanism to break the gridlock, but only if it recognizes fiscal and political realities. As Concord Co-Chairs former Senators Warren Rudman (R-NH) and Bob Kerrey (D-NE) wrote in a *Washington Post* op-ed, the commission would need five elements to succeed:

- First, it must be truly bipartisan. Any perception that the commission's purpose is to facilitate swift enactment of a partisan agenda would doom it to failure. It must have bipartisan co-chairs and equal representation. Doing otherwise in the current partisan environment would be a waste of time and money.

- Second, it must have a broad mandate. While it is critical to control the growth of entitlements, particularly Medicare and Social Security, the commission should examine all aspects of fiscal policy.

- Third, all options must be on the table. If either side sets preconditions, the other side will not participate. This means that Republicans cannot take tax increases off the table and Democrats cannot take benefit reductions off the table.

- Fourth, the commission must engage the public in a genuine dialogue about the trade-offs inherent in realistic solutions. When people are armed with the facts and given the opportunity for honest dialogue, they are willing to set priorities and make hard choices.

- Fifth, the commission's recommendations should be given an up or down vote in Congress, allowing for amendments that would not reduce the total savings. Absent that, the report would likely join many others on a shelf.

In the ideal world, we would not need another commission to tell us things most people in Washington already know. Moreover, elected leaders — not an appointed commission — must make the ultimate decisions. However, a commission with a broad mandate and no preconditions could develop a credible marker for Congress and the President.

VII. The importance of public engagement

Political realities explain why nothing has been done. Changing course will require substantial spending reductions from projected levels, equivalent increases in revenues, or — most likely — a combination of both. Neither party wants to be the first to propose such tough choices out of fear that the other side will attack them. Similarly, neither side wants to discuss possible compromises of their own priorities out of fear that the other side will take the concessions and run. Unfortunately, these fears are justified.

Because these choices are politically difficult, the active involvement of the American people is critical. Without greater understanding of the problem among the public, community leaders, business leaders and home state media, elected leaders are unlikely to break out of their comfortable partisan talking points — and unlikely to find solutions.

The Fiscal Wake-Up Tour is a joint public awareness initiative by The Concord Coalition, the Budgeting for National Priorities Project at The Brookings Institution, and The Heritage Foundation. U. S. Comptroller General David Walker is an advisor and has participated in each of the Tour's public events.

For the past year we have visited many cities including Atlanta, Richmond, Minneapolis, Portland (OR), Kansas City, Durham, Omaha, Philadelphia, Wilmington, San Diego, Austin, Chicago, Denver, Seattle and Columbus. We have also spoken to various organizations such as the National Conference of State Legislatures and the National Conference of Editorial Writers. Many other events are being planned for the fall and into next year. In fact, later today some of my Fiscal Wake-Up Tour colleagues and I will be headed to Iowa for a series of forums.

The purpose of this Tour is to explain in plain terms why budget analysts of diverse perspectives are increasingly alarmed by the nation's long-term fiscal outlook. Our emphasis is on the key areas in which we have found consensus, such as:

- The overall dimensions of the problem
- The nature of the realistic trade-offs that must be confronted in finding solutions
- The adverse and inequitable consequences for future generations if we fail to make serious changes, sooner rather than later.

Our mission is to cut through the usual partisan rhetoric and stimulate a more realistic public dialogue on what we want our nation's future to look like, along with the required trade-offs. We believe that elected leaders in Washington know there is a problem, but they are unlikely to act unless their constituents better understand the need for action, and indeed, demand it.

Members of the Fiscal Wake-Up Tour do not necessarily agree on the ideal levels of spending, taxes and debt, but we do agree on the following key points:

- Current fiscal policy is unsustainable
- There are no free lunch solutions, such as cutting waste fraud and abuse or growing our way out of the problem.
- The best way to make the hard choices is through a bipartisan process with all options on the table.
- Public engagement and understanding is vital in finding solutions.
- This is not about numbers. It is a moral issue.

A typical stop on the Fiscal Wake-Up Tour will include a public forum, a breakfast meeting with community/business leaders and an editorial board meeting with the local newspaper. In most cases, the venue for the public forum is a college or university.

The program generally consists of presentations by four or five panelists and an extended Q&A session with the audience. Panelists use PowerPoint presentations to show:

- The current budget numbers in historic context as a percentage of GDP
- Where the budget is headed on autopilot
- The driving forces behind the long-term projections
- The magnitude of the changes in either spending or tax policies that are needed to bring about a more sustainable and generationally equitable outcome
- Potential consequences of failure to change course

We do not recommend specific policy solutions. Indeed, we are upfront about the fact that we do not necessarily agree on solutions. However, we remind audiences that each of the realistic options comes with economic and political consequences that must be carefully weighed, and that there must be tradeoffs. Those who want to raise taxes are asked to explain what level of taxation they are willing to support and the manner in which the new revenue should be raised. Those who argue that spending must come down from projected levels are asked which programs they would target and how the savings would be achieved. Those who are unwilling to do either are asked how much debt they are willing to impose on future generations.

Our experience is that when audiences are told the facts, and shown that if they demand their "rights" to programs or policies it will have damaging economic effects to other groups or generations represented in the audience, they begin to accept the need for tradeoffs.

The Fiscal Wake-Up Tour does not presume to know the "correct" answers, but we are trying to make sure that the American people and their elected leaders are asking the correct questions.

In addition to the Fiscal Wake-Up Tour, the same group of analysts from Concord, Heritage and Brookings have been working with Public Agenda and ViewPoint Learning, (both chaired by Dan Yankelovich) on a project designed to provide insight into how attitudes evolve as people discuss difficult trade-offs with regard to long-term fiscal policy.

Three intensive day-long "Choice Dialogues" were conducted earlier this year in San Diego, Kansas City and Philadelphia. Public Agenda and ViewPoint Learning are in the process of reviewing the results. A report issued in December 2006 made the following observations:

- The public is strongly averse to big increases in the size of the national debt and, with the right kind of leadership, is prepared to accept sacrifices to avoid it.
- For most people, the overriding concern is not resistance to taxes but a profound lack of trust in government. People are willing to pay for what they want so long as they can be satisfied that government will spend the money wisely and for the purposes intended.
- Americans are willing to make changes in entitlements, but again on condition that trust and accountability exist.
- While there is continued strong support for defense spending, it is accompanied by the widespread perception that funds are misallocated and often wasted.
- Americans want to be engaged in addressing these issues and are frustrated by the lack of engagement that contributes to their mistrust of government

Daunting as the long-term projections are, there is nothing inevitable about a fiscal crisis. The problems we face - essentially a structural imbalance between what government promises and what it collects in taxes to pay for those promises - is one that can be cured in a timely way if we begin to address it now. In other words, the solution is in our own hands. As Concord Coalition President and former Commerce Secretary Peter G. Peterson has written:

> If America chooses the right future, it will be because we learn again to cooperate politically and embrace a positive vision of what our nation can become. Yes, we have to make some tough choices. But instead of obsessing over the tax hike that outrages us, or the benefit cut that shocks us, we need to focus on everything our nation can achieve if we all made an effort to come to terms with our future [8]

There is no better time to begin such an effort than now. The lessons of Hurricane Katrina have important implications for our long-term fiscal challenge. Known dangers should be acknowledged in advance of a crisis and dealt with in a straightforward manner. By all means, we should debate the options and trade-offs. But we must act. Economic growth alone will not be enough to close the gap. Moreover, the sooner action is taken, the more gradual the remedies can be. The political system can adjust to unexpected good news. More problematic are the potentially harsh adjustments of deferring action on bad news projections that prove correct.

Concord's founding Co-Chair former Senator Paul Tsongas (D-MA) said, "The bond between parent and child is nature's strongest. Providing for the well-being of the young is how every generation of Americans undertook their stewardship."

Our time to act as generational stewards is now.