A CHOICE OF TWO FUTURES

The trends described in the previous section – especially those concerning the health care marketplace and Federal entitlement spending – translate into one of two possible fiscal futures for the U.S. The status quo leads to a level of government spending, financed by taxes or debt, that will cripple the U.S. economy and, as a result, deprive future working families of their potential prosperity, and future retirees of the very benefits government promises.

The other path entails a transformation of health care, Federal entitlements, and Federal taxes; restrains the growth of Federal Government spending to sustainable levels; and fulfills America's promises from one generation to another.

AN UNSUSTAINABLE PATH

According to estimates by the Congressional Budget Office [CBO], current Federal spending trends are leading toward an unprecedented level of taxes or debt. Because entitlement spending is governed by permanent law and runs automatically, unless Congress enacts new laws to address the problem, the country marches down this path of unsustainable debt or sharply higher tax levels.

In its December 2007 report, *The Long-Term Budget Outlook*, CBO presented estimates of Federal spending, revenue, and deficits shown in Table 5 on the next page. The table is developed from two assumptions: 1) that Congress increases spending only for specific policies approved in the past, such as adjustments to physician payments under Medicare; and 2) that current tax polices are extended, including provisions of the 2001 and 2003 tax laws, and the alternative minimum tax [AMT] is indexed for inflation.

As Table 5 shows, the rate of "primary" Federal spending – excluding interest – rapidly outpaces the revenue path. But because all Federal spending must be financed somehow, the spending excess (reflected in the table as the budget "deficit") causes increased amounts of borrowing and interest payments. When these interest costs are included, Federal spending exceeds an alarming 40 percent of GDP by mid-century, and consumes three-fourths of economic resources by 2082.

The substantial borrowing demanded by this trend would rapidly increase to unprecedented levels. By 2031, Federal debt – which was 37 percent of GDP at the end of 2007 – would reach 109 percent of GDP, more than double the level of debt reached during the Civil War. But unlike those war years, when debt temporarily jumped to this escalated level and then quickly declined, the debt under the current fiscal outlook keeps rising, and at an accelerating rate.

The effect on economic performance and standards of living will be devastating, and it will be felt as those born today are completing college and beginning their careers.

Workers and families will begin to see the growth in their wages and incomes erode. Another decade after that, standards of living begin to stagnate, and then decline in real terms. By 2060, the economy enters a free-fall, and CBO cannot model the economic impact later in that decade because debt rises to levels the economy cannot support.

Table 5: Projected Federal Spending and Revenue, as Percentages of Gross Domestic Product

	2007	2030	2050	2082
Primary Spending[a]				
Social Security	4.3	6.1	6.1	6.4
Medicare	2.7	5.9	9.4	15.6
Medicaid	1.4	2.5	3.1	3.7
Other Noninterest	9.9	9.8	9.7	9.6
Subtotal: Primary Spending	18.2	24.2	28.3	35.3
Interest	1.7	4.8	13.6	40.1
Total Spending	**20.0**	**29.0**	**41.8**	**75.4**
Revenue	18.8	18.9	19.4	20.9
Deficit (-)	-1.2	-10.1	-22.5	-54.5

[a] Assumes spending increases that Congress typically has approved, such as adjustments in physician payments under Medicare.
[b] Assumes continuation of current tax law – including the provisions enacted in 2001 and 2003 – and adjustment of the alternative minimum tax for inflation.
Source: Based on figures in *The Long-Term Budget Outlook*, Congressional Budget Office, December 2007.

The other alternative would be to raise taxes to finance growing entitlement spending. Notably, even large and unprecedented tax increases – from the scheduled expiration of the 2001 and 2003 tax provisions, and expansion of the AMT – could not keep pace with the rate of spending growth driving this scenario. As summarized recently by the Brookings-Heritage Fiscal Seminar:

> [R]estoring tax rates to pre-2001 levels will not close the gap between spending and revenues. . . . Even raising revenues as a percent of GDP to European levels – levels that are unprecedented in the United States – will not be sufficient. If the wedge between spending and revenues attributable to social insurance programs continues to grow, taxes would have to be raised continuously and would eventually cripple the economy. (The Brookings-Heritage Fiscal Seminar, *Taking Back Our Fiscal Future*, April 2008)

CBO also concluded that financing this unrestrained rate of Federal spending with higher marginal tax rates yielded results similar to those from financing it with debt: over the long run, the economy cannot sustain the tax rates needed to finance this spending. CBO focused on three points in time: 2030, 2050, and 2080. CBO found that by 2050, income tax rates (individual and corporate rates) would have to rise by 90 percent to fund the projected spending path. In other words, the current 10-percent income tax bracket would rise to 19 percent, and the current top rate of 35 percent would rise to 66 percent.

Translating such a tax trend to its impact on families produces the following result: today, a family of four with a median income of roughly $66,000 pays slightly more than $3,100 in individual income taxes; applying the high-tax scenario to today's dollars, this family's income tax bill would jump to $5,900 – an increase of $2,800 (and this figure does not include payroll taxes). By the end of the period (just past 2080), the top individual and corporate tax rates would have to increase by 150 percent – a tax burden that the economy simply could not sustain, CBO concluded.

THE PATH OF SUSTAINABLE GROWTH

By contrast, *A Roadmap for America's Future* charts a path of fiscal sustainability by keeping revenues as a percent of GDP at their historical average, and restraining spending to hold deficits within their historical levels. The result, shown in Table 6 below, is that interest and debt accumulate at much slower rates than projected under current fiscal policy, and actually begin to decrease after peaking in mid-century.

Table 6: *A Roadmap for America's Future* – Projected Federal Spending and Revenue, as Percentages of Gross Domestic Product

	2007	2030	2050	2082
Primary Spending[a]				
Social Security	4.3	6.5	6.4	4.1
Medicare	2.7	5.3	5.1	5.0
Medicaid	1.4	1.3	1.2	1.0
Other Noninterest	9.8	7.3	6.1	3.1
Subtotal: Primary Spending	18.2	20.3	18.7	13.1
Interest	1.7	2.9	5.3	2.9
Total Spending	**19.9**	**23.2**	**24.0**	**16.0**
Revenue	18.7	18.5	18.5	18.5
Deficit (-)	-1.2	-4.7	-5.5	2.5

Source: Committee on the Budget.

Under this plan, Federal spending peaks in 2041 at 24.7 percent of GDP. With revenue projections held to 18.5 percent of GDP, this means the largest deficit faced under this plan is 6.2 percent of GDP. Although this number is large, recent history shows it is sustainable for a short period. (In 1983, the Federal Government ran a deficit of 6 percent of GDP.) What is important about this plan, however, is not how it compares with the past, but how it compares with the trajectory under current policy – and whether the economy can sustain these deficit levels. Absent policy reforms, the Federal Government will face a deficit of 6.2 percent of GDP in 2022, which will then swell to nearly 20 percent of GDP in 2041, and continue growing to more than 50 percent of GDP in 2082. In contrast, deficits in *A Roadmap for America's Future* peak in 2041 and then begin a rapid decline, until the budget reaches surplus.

Similarly, *A Roadmap for America's Future* keeps debt held by the public from spiraling to unsustainable levels. Under current policy, debt held by the public soars to the improbable level of more than 800 percent of GDP (though the economy would crash well before this level were reached). As CBO notes in *The Long-Term Budget Outlook*, countries that carry debt of more than 100 percent of GDP must change their fiscal policies because those levels are not sustainable over the long run.

The *Roadmap* also slows the accumulation of debt held by the public, and eventually reduces debt year over year beginning just after the middle of the century. Although deficit and debt levels rise in the *Roadmap*, CBO concluded the economy could sustain them, and would be "considerably stronger" than under current policy (see Appendix II).

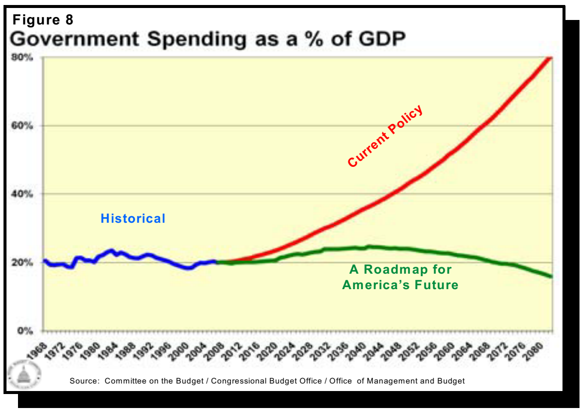

Figure 8
Government Spending as a % of GDP

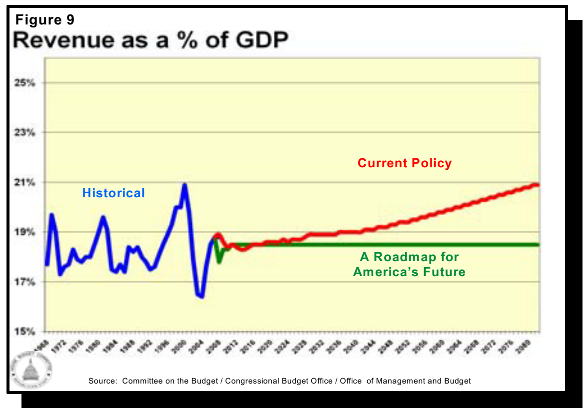

Figure 9
Revenue as a % of GDP

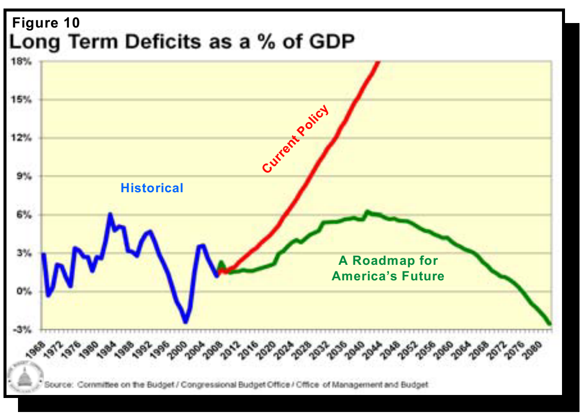

Figure 10
Long Term Deficits as a % of GDP

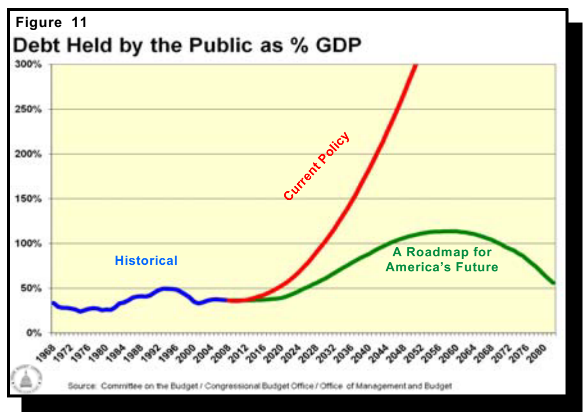

Figure 11
Debt Held by the Public as % GDP

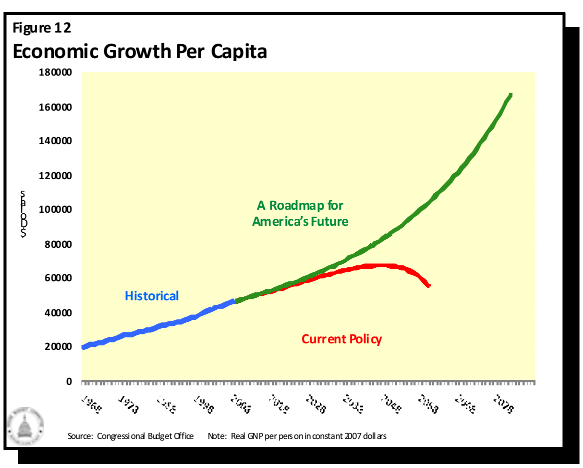

Figure 12
Economic Growth Per Capita

Most important, real living standards continue to increase under this budget path. Data from CBO show that, under this scenario, the standard of living for a child born today would double (i.e. per-capita output would rise from $45,000 to more than $90,000) by the time he or she reached middle age, just after the middle of the century (see Figure 12). In this way, the sustainable budget path continues the American legacy of leaving the next generation better off. *This is in sharp contrast with current fiscal policy, which would lead to stagnant, and eventually declining, standards of living.*