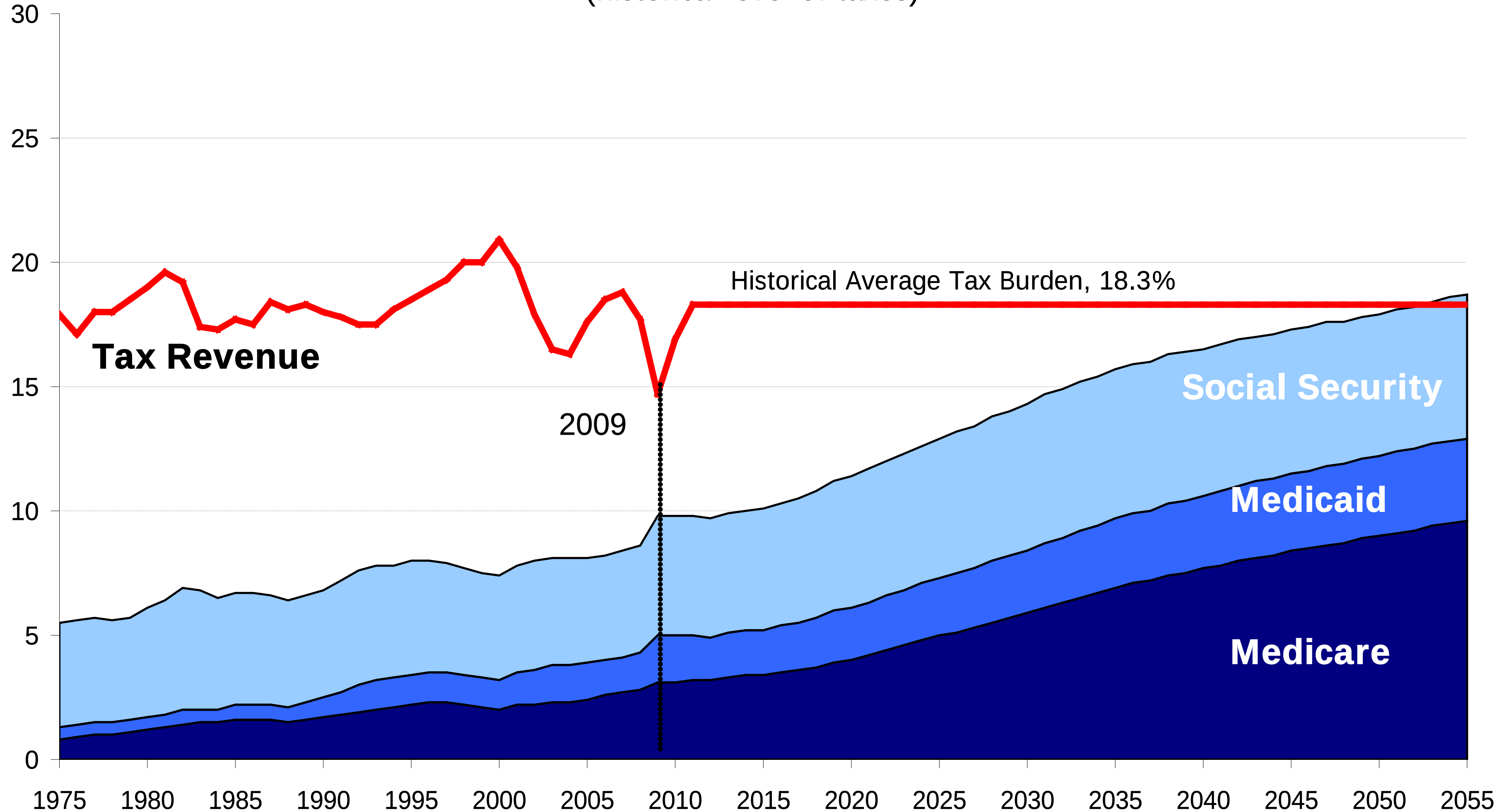
The Federal Deficit and its Effect on Public Policy Options

David C. John
The Heritage Foundation

Entitlements crowd out all other programs

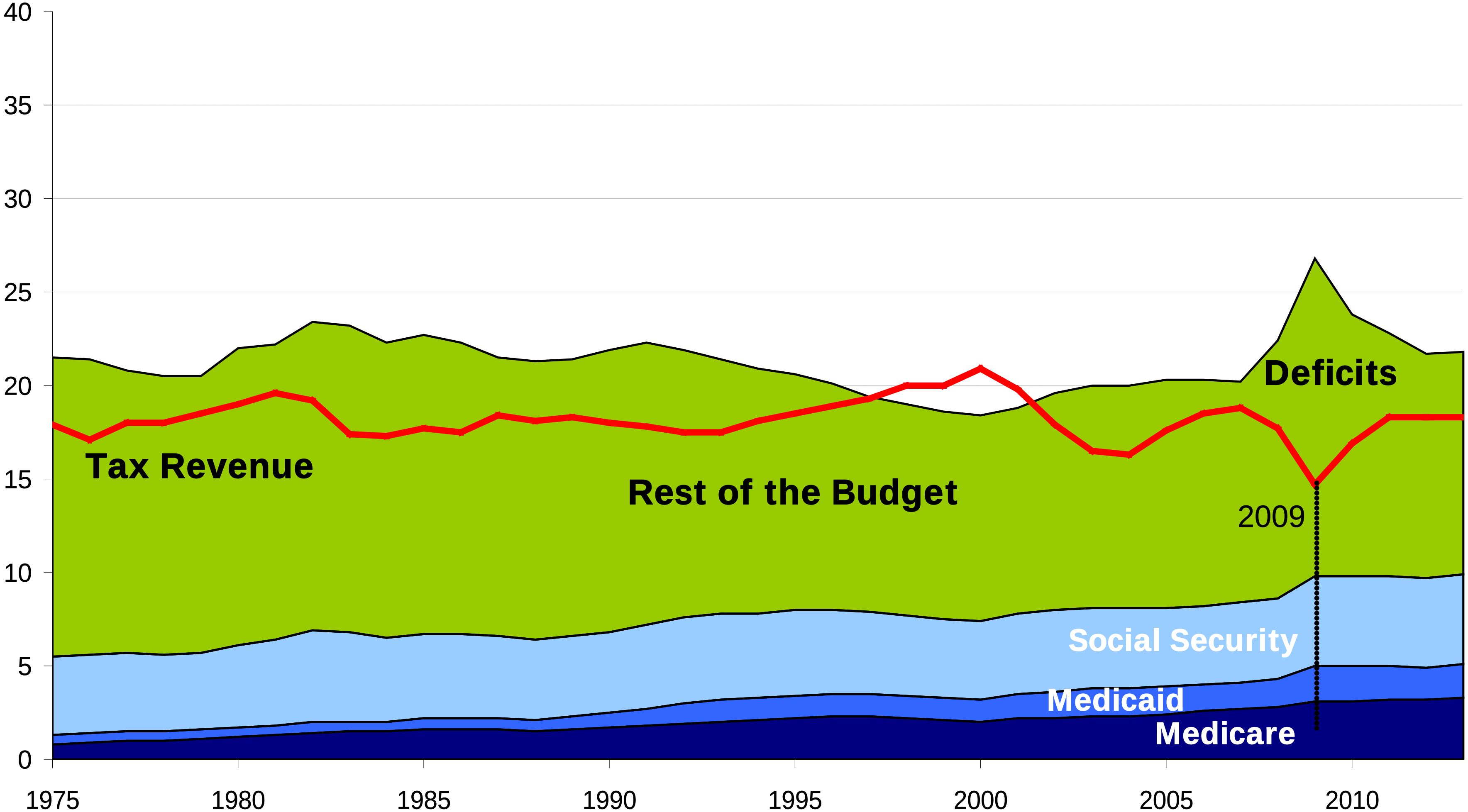
(historical level of taxes)



Federal Spending and Tax Revenue as a Percentage of Gross Domestic Product

Source: Congressional Budget Office and Office of Management and Budget

Budget Yesterday and Today



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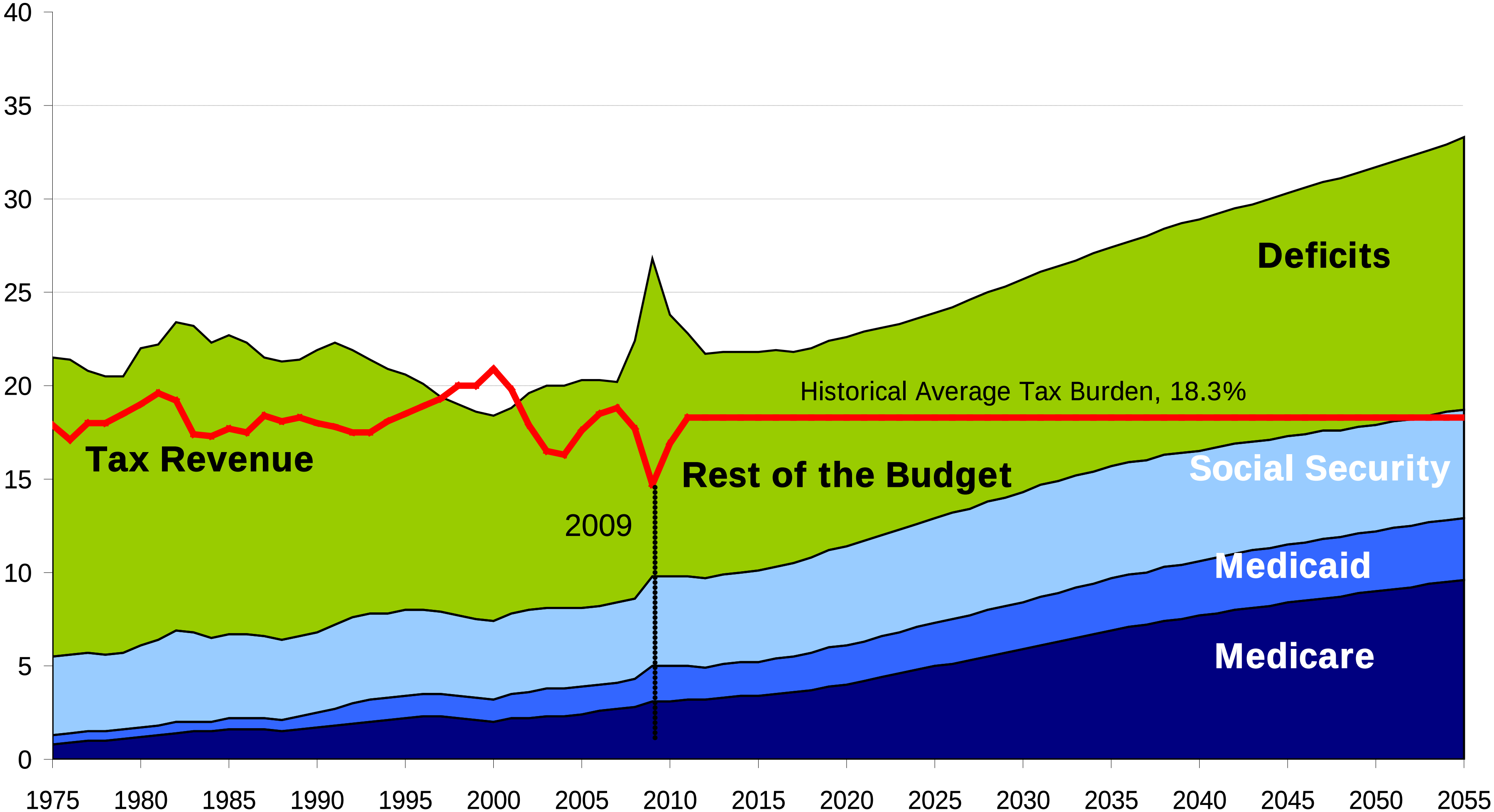
Budget in the Future



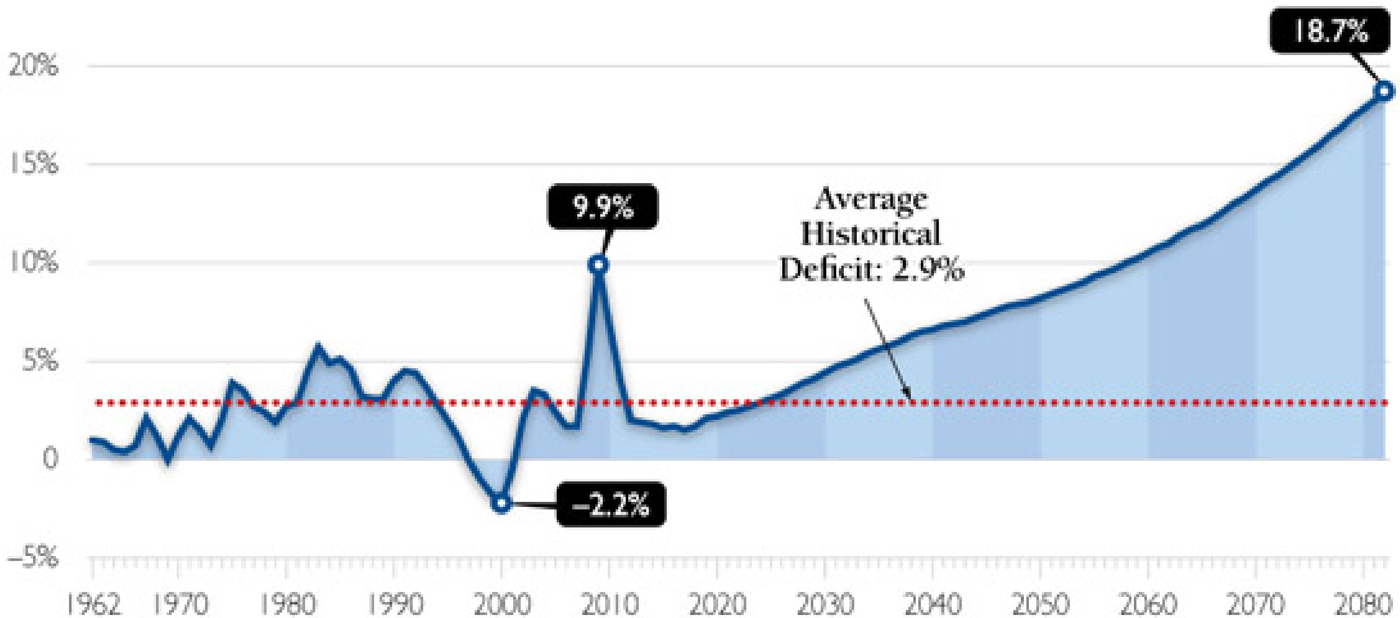
Federal Spending and Tax Revenue as a Percentage of Gross Domestic Product

Source: Congressional Budget Office and Office of Management and Budget

Federal Budget Deficits Will Reach Levels Never Seen Before in the U.S.

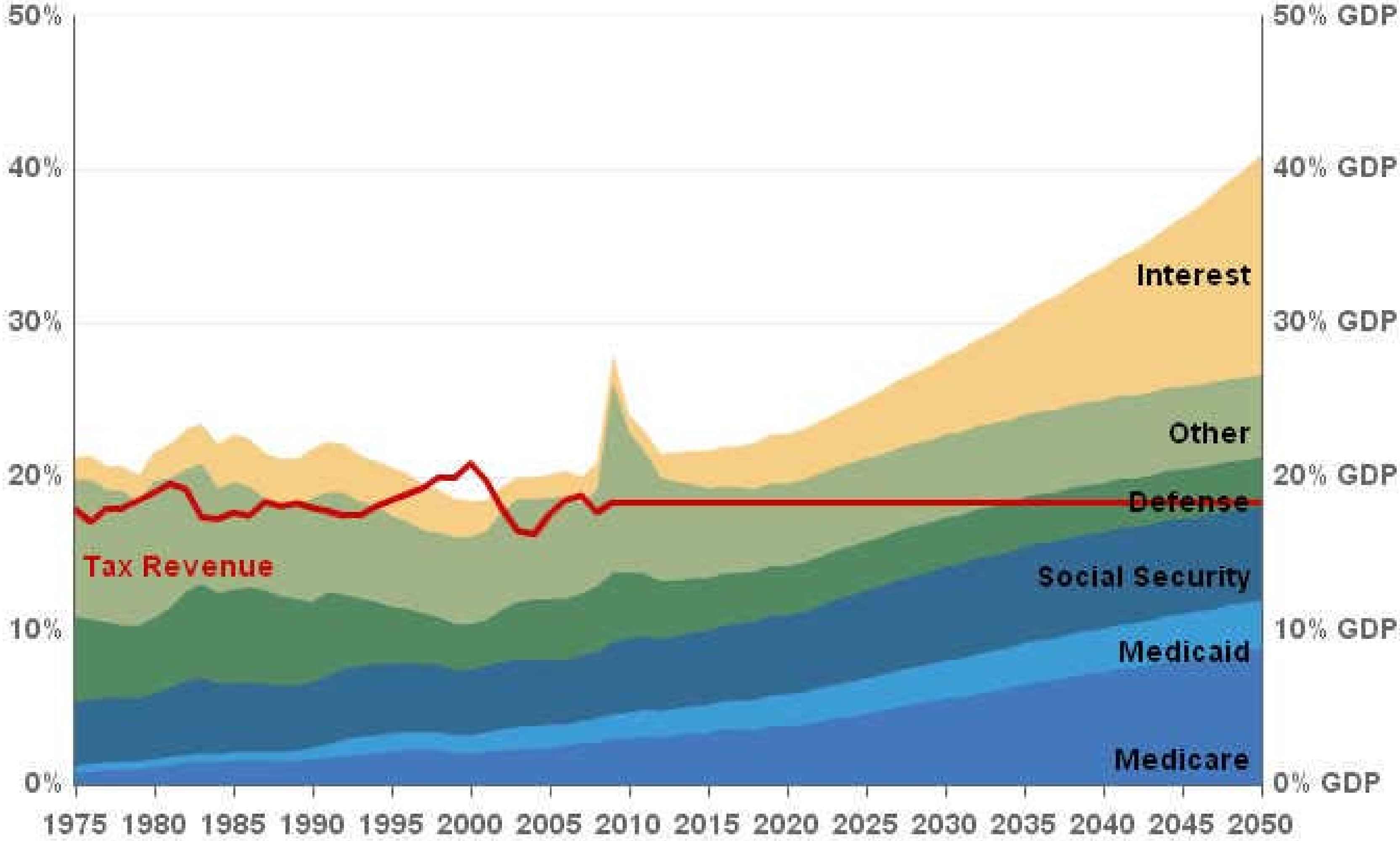
Under current law, the budget deficit is projected to grow to 18.7 percent of GDP by 2082, even if the 2001 and 2003 tax cuts are allowed to expire and the AMT is not fixed. This will be driven by deficits well above the 30-year historical average of 2.9 percent. Deficits of this size have never been seen in the U.S. and illustrate the need to reform these programs.

Federal Budget Deficit as a Percentage of GDP



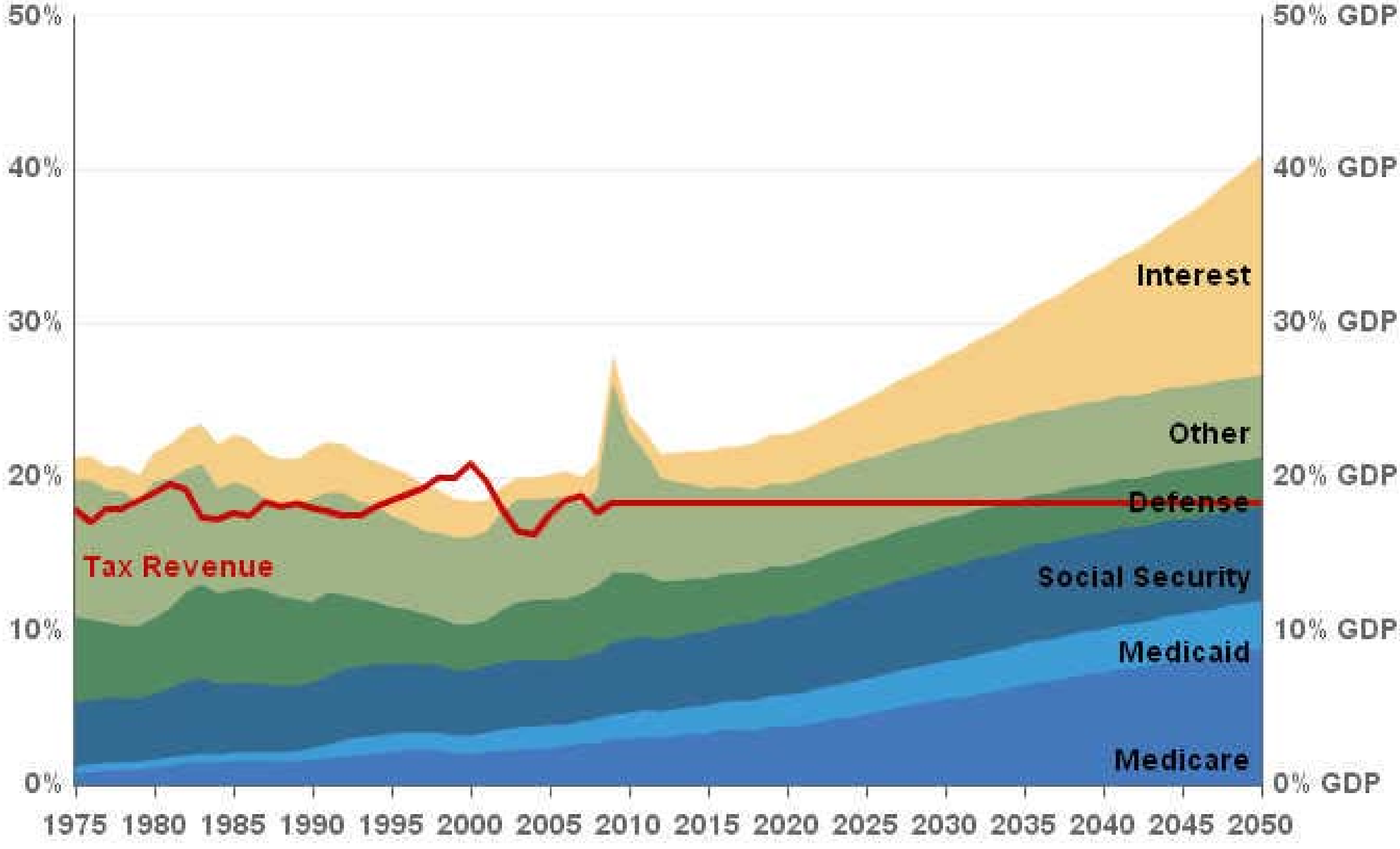
Source: Heritage Foundation calculations based on Congressional Budget Office data.

The Federal Budget, 1975-2050



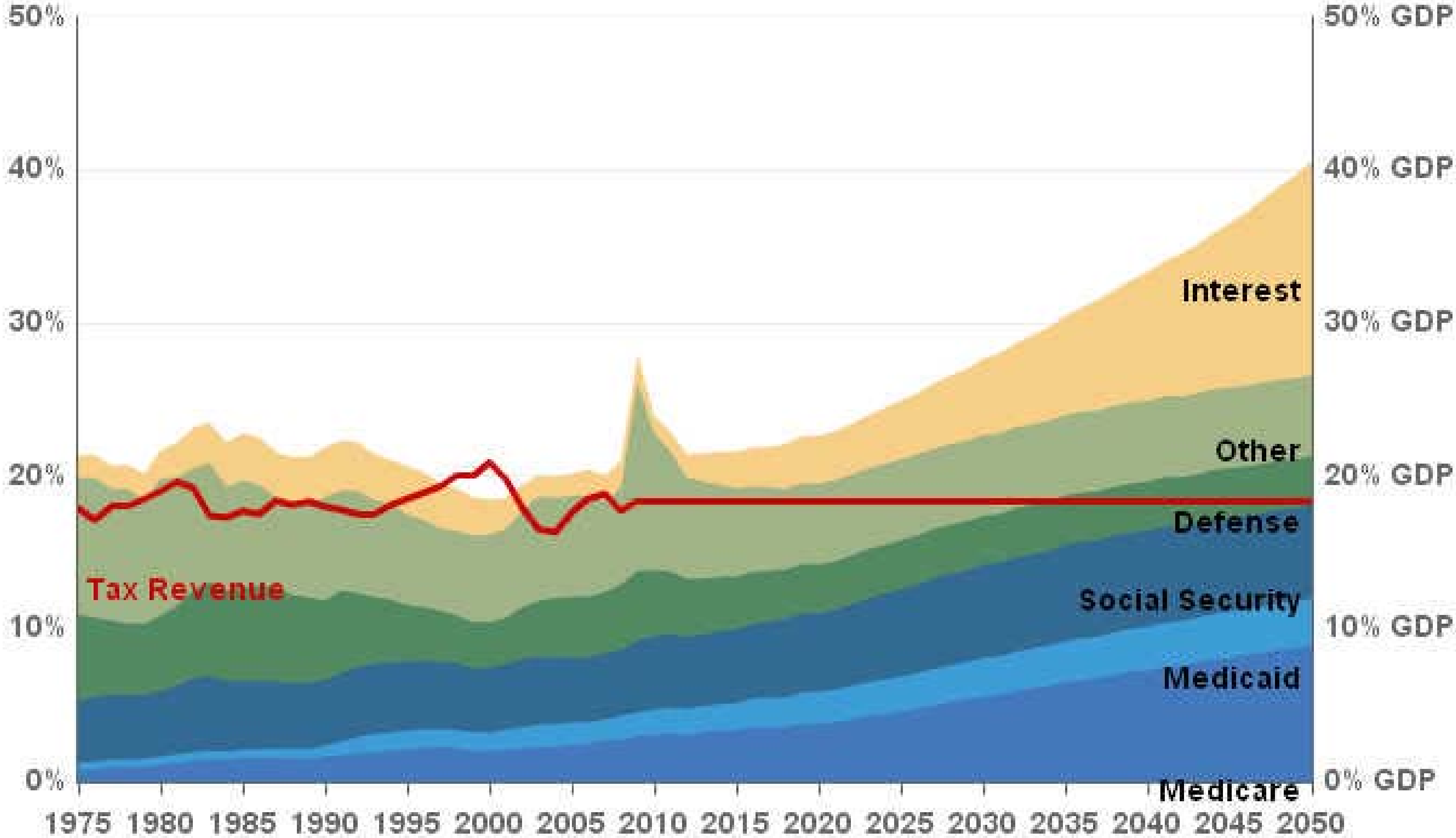
Source: The Heritage Foundation Federal Budget Calculator.

Eliminate NEA



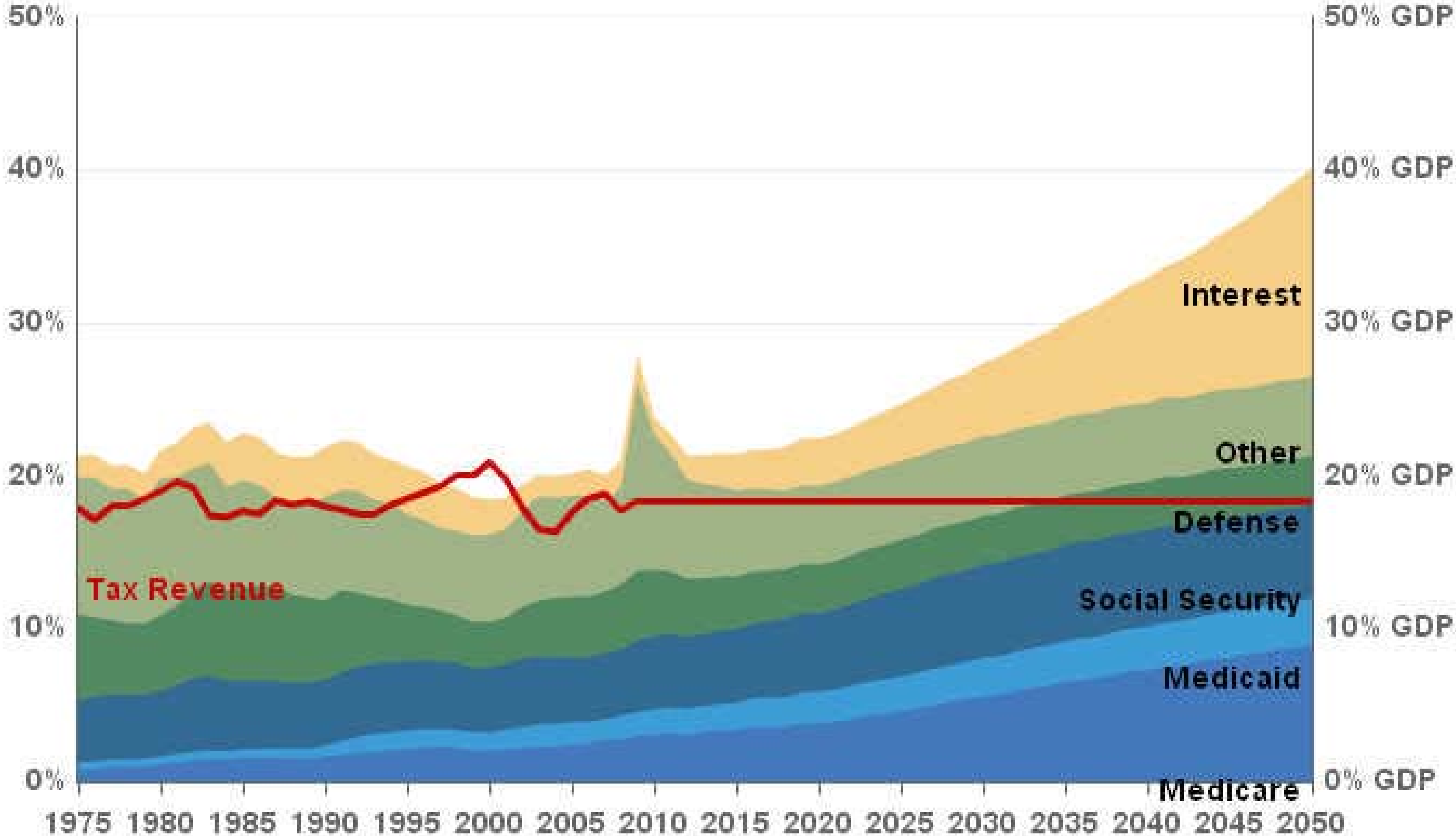
Source: The Heritage Foundation Federal Budget Calculator. Assumes Spending Cuts: Cut NEA

Eliminate NEA + NASA



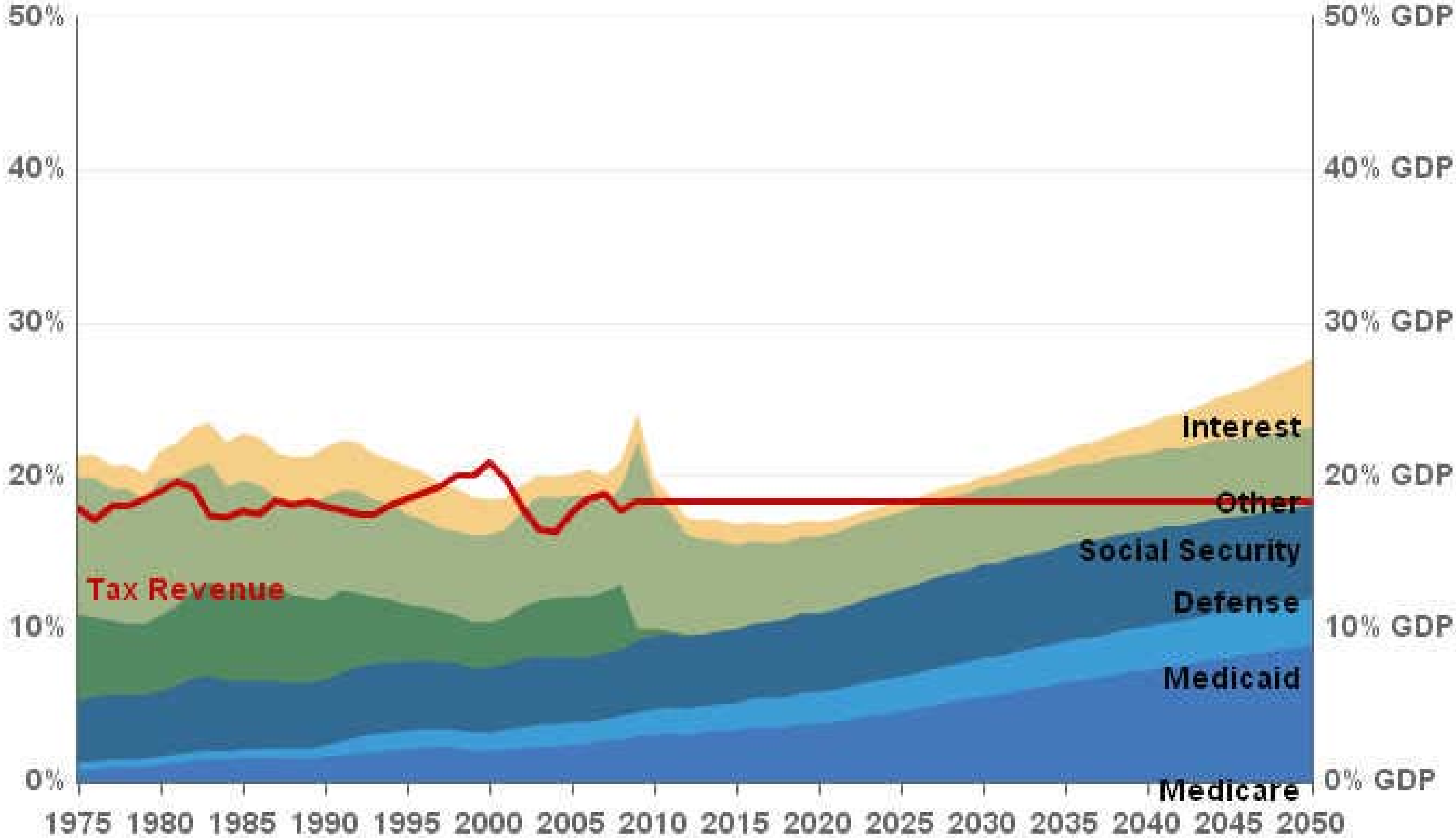
Source: The Heritage Foundation Federal Budget Calculator. Assumes New Category!: Cut Nasa, Spending Cuts: Cut NEA

Eliminate NEA + NASA + Pork



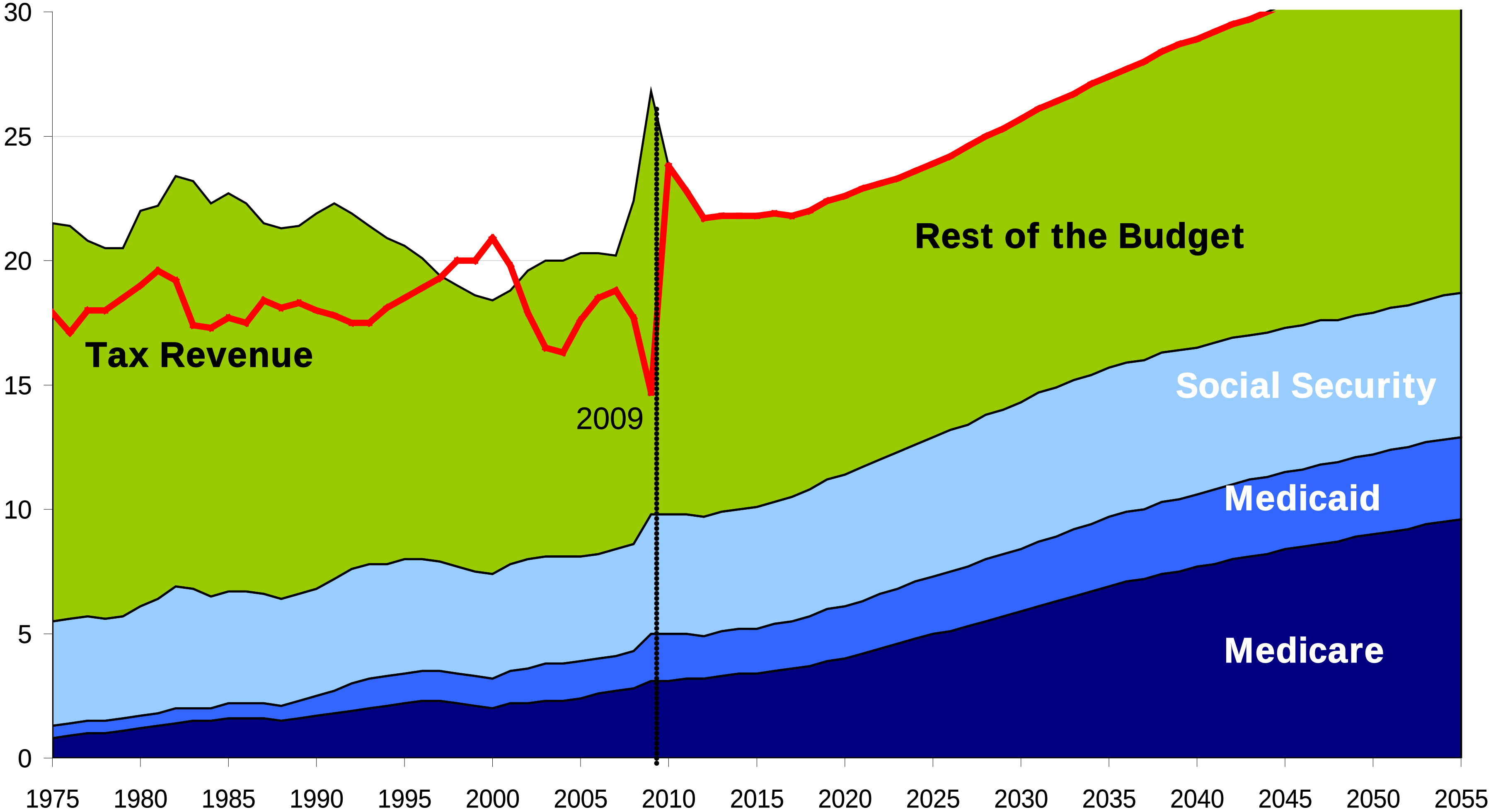
Source: The Heritage Foundation Federal Budget Calculator. Assumes New Category!: Cut Nasa, New Category!: Cut Pork, Spending Cuts: Cut NEA

Even Eliminating Defense Will Not Solve The Problem



Source: The Heritage Foundation Federal Budget Calculator. Assumes New Category!: Cut Nasa, New Category!: Cut Pork, Spending Cuts: Cut NEA, Spending Cuts: Eliminate Defense

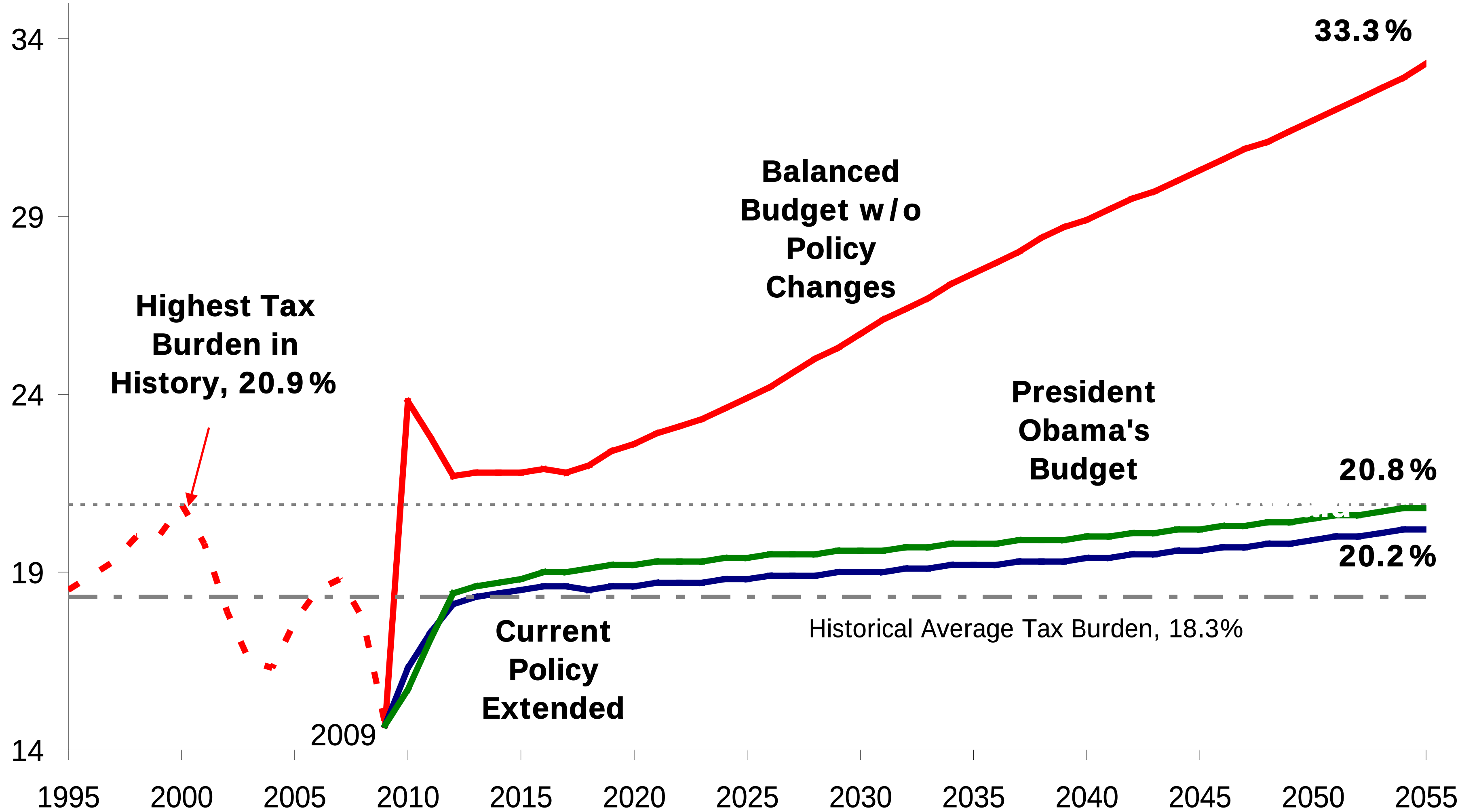
Could raise taxes to balance the budget



Federal Spending and Tax Revenue as a Percentage of Gross Domestic Product

Source: Congressional Budget Office and Office of Management and Budget

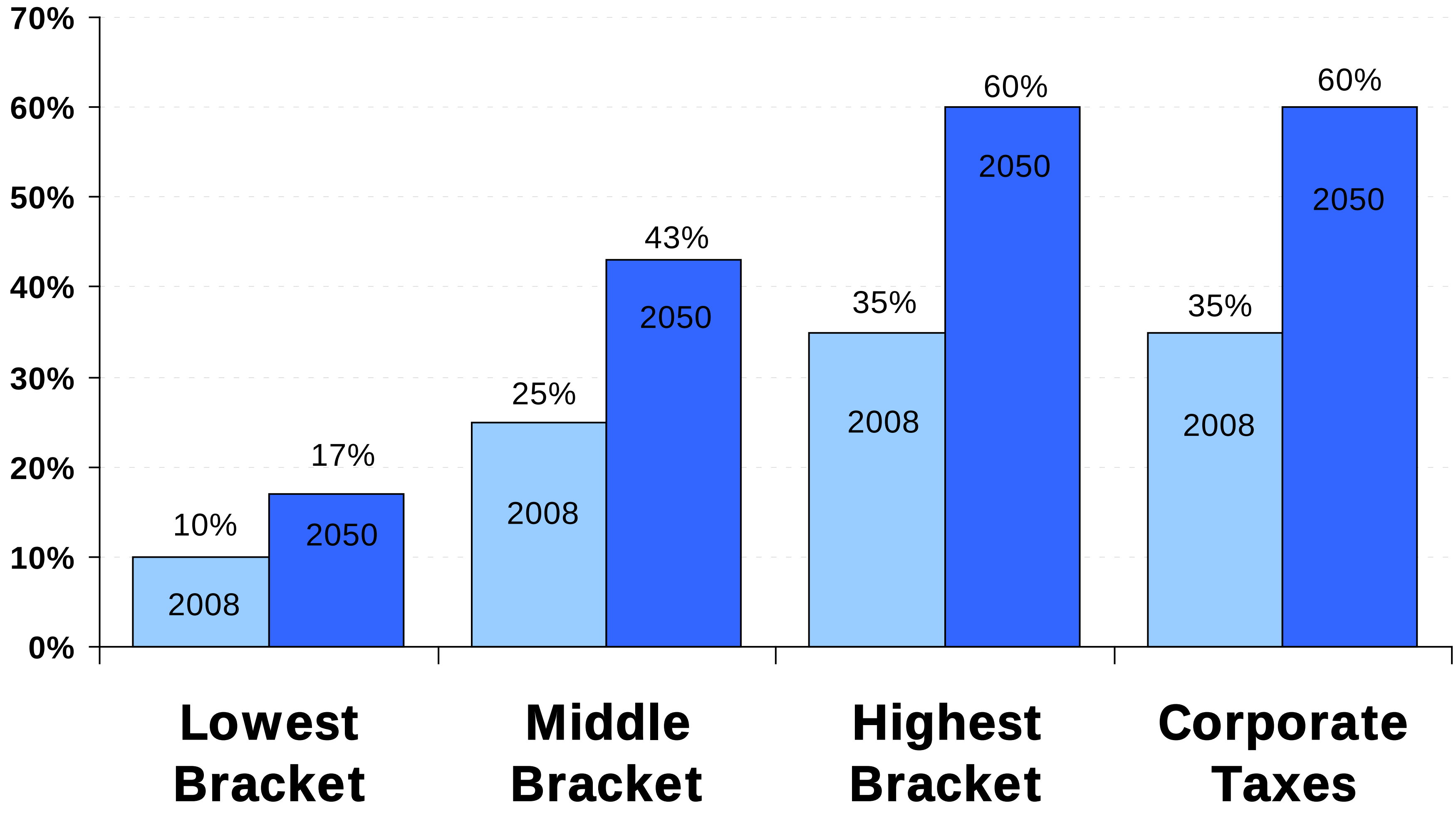
Let's look at the tax-raising choice



Federal Tax Revenue as a Percentage of Gross Domestic Product

Source: Congressional Budget Office and Office of Management and Budget

What would balancing mean for tax rates on our children?



Source: Congressional Budget Office (assumes healthcare grows 1% faster than GDP for 2050 figures)

The Congressional Budget Office Confirms, Raising Taxes to Pay for Entitlements Will Devastate the Economy

"Such tax rates would significantly reduce economic activity and would create serious problems with tax avoidance and tax evasion. Revenues would probably fall significantly short of the amount needed to finance the growth of spending; therefore, tax rates at such levels would probably not be economically feasible"

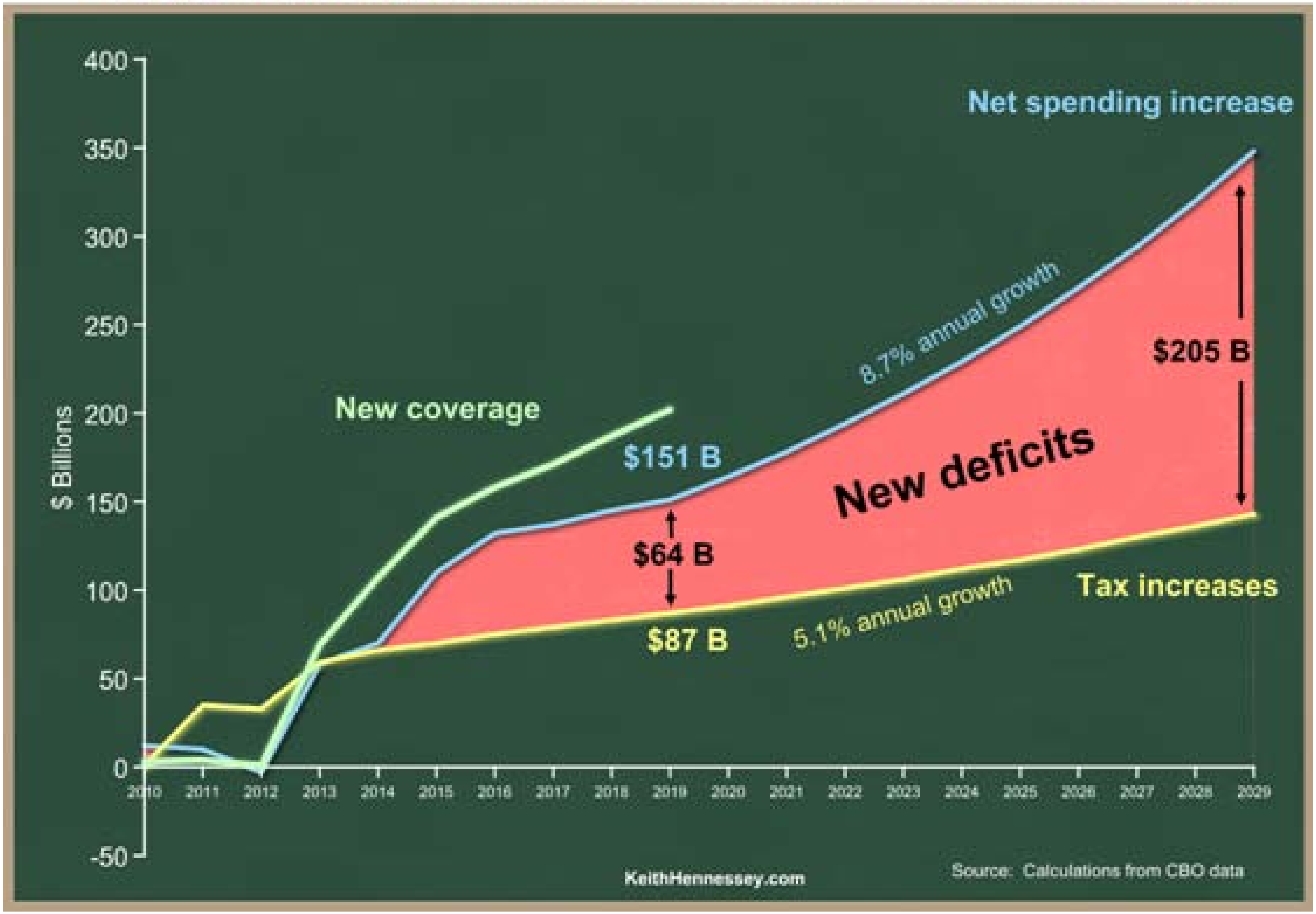
"Beyond 2060, projected deficits would become so large and unsustainable that the model cannot calculate their effects."

Source: Peter R. Orszag, Director, Congressional Budget Office, letter to Representative Paul Ryan (R-WI), May 19, 2008, at *http://www.cbo.gov/ftpdocs/92xx/doc9216/05-19-LongtermBudget_Letter-to-Ryan.pdf* (September 3, 2008).

Health Care Reform

Long-term unfunded impact = $9 trillion

Long run budget effects of the House health care bill



A Brief History of the Retirement Age

- In 1880, 76% of men were employed at age 65, a proportion that declined to 43% in 1940, and 18% in 1990.

- In 1935, state pension systems were split half-and-half between those that used 65 and those that used 70 as the retirement age.

- The Commission on Economic Security was swayed to adopt 65, in part, because the federal Railroad Retirement System which was established in 1934 used 65 and, in part, because analyses at the time showed 65 was actuarially feasible at low levels of taxation.

Life Expectancy Over Time

	Life Expectancy at Age 65		Percent of Life in Retirement NEA		Percent of Life in Retirement EEA		Equivalent normal Eligibility Age	
	Men	Women	Men	Women	Men	Women	Men	Women
1940	77.7	79.7	16%	18%	n/a	n/a	n/a	n/a
2007	82.5	84.8	19%	21%	25%	27%	69	69.1
2040	84.5	86.7	21%	23%	27%	28%	70.6	70.7
2080	86.5	88.6	23%	24%	28%	30%	72.3	72.2

How to Raise the Retirement Age

- **Increase the Normal Eligibility Age**
  - The 1983 reforms set up a process to gradually increase the NEA. This process could simply be continued to increase the eligibility age further.

- **Increase the Early Eligibility Age**
  - The EEA could be increased by a similar mechanism to gradually increase the EEA from 62 to 65.

- **Exempt Workers Above NEA from Payroll Taxes**
  - Since employers would not have to pay the 6.2% match to the payroll taxes withheld from the pay of these workers, such a change would lower the cost of hiring and retaining older workers.

  - Increasing employment for older workers would also slightly offset any negative effects of increasing the retirement ages for healthy workers.

Effects of Increasing the Retirement Ages on Social Security's Finances

- Increasing the NEA is a benefit deduction, such a move will help reduce Social Security's fiscal problems.

- Increasing the retirement age adds about 5 years to the life of the trust fund, but the program in 2080 still faces a deficit of -4.94 percent of taxable payroll instead of the 2005 estimate of a -5.70 percent deficit.

- Indexing the NEA after 2025 would result in additional improvements, but it is unlikely to be anywhere close to enough to close a substantial part of the remaining deficit.

- Other changes to the program will be necessary to make Social Security fiscally healthy.