Time To Take Federal Budget Off Autopilot

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Hamlet's lament of the "calamity of so long life" wasn't about the federal budget. But if major entitlements aren't reformed, the budget is headed for a true calamity as the population ages and health costs soar.

Social Security, Medicare and Medicaid will absorb 6% to 9% more of the GDP in 2030 than they do today. That's roughly equivalent to increasing the Social Security tax rate from 15% to 30% of earnings or wiping out every other federal expenditure program.

What is largely ignored from Washington to Wall Street is that this fiscal calamity is happening by default. Entitlement spending grows dramatically even when Congress does nothing. Even most Social Security reforms now being debated would do little to curb growth for decades.

Empty Promises

Social Security is in trouble because for decades it has been set up to grow faster than the economy. More and more years of benefits are provided as people live longer, and each new generation's annual benefits grows along with their wages. The goal was to increase forever benefits for each new retiring generation.

The mistakes? Trying to achieve the goal automatically regardless of cost. Forcing other legitimate claims to compete for the budget leftovers. One consequence has been an ever-dwindling share of the budget pie for discretionary budget items serving children and working families.

To top it off, these growing promises were made without regard for the revenue decline implied when a lower birth rate meant fewer workers paying taxes.

Medicare and Medicaid, which entitle eligible populations to an almost open-ended array of medical services, were also designed to grow continuously faster than the economy. Had a voucher system been adopted instead, government would have provided a fixed amount of money to citizens to buy insurance policies meeting certain minimum standards. Or had we gone the way of the United Kingdom and Canada, we would have had a fixed budget for these programs. Either way, someone somewhere would have had to decide how to live within a budget by limiting payment rates or rationing expensive services.

We suggest a simple approach to fixing Social Security. Whenever the system's trustees report a long-term imbalance, retirement ages would be increased modestly; or benefits above some minimum would be indexed to prices instead of wages.

Slowing cost growth either way or through some combination of both would be gradual and wouldn't blindside near-retirees. If the projected imbalance goes away, so does the adjustment.

Health insurance programs can't be handled quite so straightforwardly. For now, the better part of valor is to address first the Medicare budget rather than that portion of Medicaid serving the poor. We propose to cut the Gordian knot by ratcheting back all provider payments in Medicare whenever other reforms are insufficient to keep its cost growth below GDP growth.

This is not an ideal solution, but it would provoke Congress into designing more efficient and equitable reforms.

Heed The Warning

Under our proposal, automatic cuts would be initiated whenever the Medicare trustees sounded a "funding warning." The Medicare prescription drug bill requires such an alarm bell when the subsidy required from general revenues exceeds a specified amount. Currently, the warning does not demand much response from the president or Congress. Our proposal gives the warning real meaning.

These simple but powerful mechanisms would make the budget ever more responsible instead of ever less. They are not intended to specify a particular, everlasting design for Social Security or Medicare -- the very mistake we are trying to correct. Existing and new anomalies still would need to be corrected periodically by Congress.

Congress is even free to be somewhat reckless each year, but not to box in future Congresses by making promises that can't be kept.

Meanwhile, spending on health and retirement, though still favored, would be forced to compete more evenly with programs for children, education, community development, and other worthy priorities.

Our proposal sounds radical. But it merely restores U.S. budget standards to the level of responsibility met throughout most of our nation's history.

It is a direction some other nations, such as Sweden and Japan, are already turning, as demographics and economics give them, too, no other choice. In these ways, we can duly recognize recognize long life as good fortune, not budget calamity.

Other Publications by the Authors

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