

# A Fiscal 'Tsunami'

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The government's top watchdog warns of a coming catastrophe.

By Jeffrey Bartholet

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David Walker can sound like a modern-day prophet of doom, warning about the gross irresponsibility of his countrymen and the disaster that awaits them if nothing is done. Put a scraggly beard on him, replace the neatly pressed suit with a tattered frock, and you could drop a coin in his cup and walk on by. But Walker is frighteningly sane. A former partner at Arthur Anderson LLP, he has been the comptroller general of the United States and head of the Government Accountability Office since he was appointed to a 15-year term in 1998. The GAO is a nonpartisan agency that investigates, on behalf of Congress, how the government is performing. It then issues thoroughly researched and often critical reviews. If the federal government is not spending taxpayers' money effectively, it's Walker's job to holler. He's hollering now—mainly about a severe fiscal crisis that will strike the United States as baby boomers reach retirement age. His fears are supported by economists from the left-leaning Brookings Institution and the conservative Heritage Foundation. NEWSWEEK's Jeffrey Bartholet spoke to Walker at his office in downtown Washington. Excerpts:

**NEWSWEEK: You have likened the situation here in the United States to the fall of the Roman Republic. Do you foresee the decline and fall of the United States?**

**David Walker:** I don't believe that the United States will decline and fall, but I think it's important that we wake up and recognize that we are seeing some of the same warning signs that existed with the Roman Republic. There are many people who think the United States is the longest-standing republic in the history of mankind, and that's not true. Rome lasted over double the period of time that we have existed so far, and it is important that we make tough choices to make sure that we are the first republic to stand the test of time.

**So what are the changes [that are needed], in a nutshell?**

To a great extent, we have a situation where people are too focused on today and not taking enough steps to prepare for a better tomorrow. In the fiscal realm, people have a false sense of security, because our deficits have come down for three years in a row, and they think we are on the right path, when in reality the structural imbalance between our long-range commitments and our projected revenues has continued to grow every year. As a result, we don't have the sense of urgency that is needed in order to make prudent changes, sooner rather than later, and that is one of the reasons that I have been speaking out.

**Let me ask you specifically about Social Security. Tax-paying Americans receive statements from the government telling them how much they should expect to receive in Social Security when they retire. Are those statements a fiction?**

No, they're not a fiction, but there is also a footnote in those statements that says that starting in about 2041, absent reform, Social Security only has enough revenues to pay about 73 cents of every dollar of promised benefits. So, no, they are not a fiction, but footnotes are an integral part of statements, and one needs to read the footnotes. The ultimate irony is that Social Security is the easiest problem that we have to fix.

**Sum up for me the fiscal situation with Medicare and Medicaid. How long will those programs be sustainable?**

Well, they're not sustainable right now. Let me just give you some statistics to put it in perspective. Social Security is underfunded [meaning there's a gap between dedicated funding and benefits] by \$6 trillion in current-dollar terms. Medicare is underfunded by over \$32 trillion in current-dollar terms, of which the Medicare prescription-drug benefit is underfunded by \$8 trillion.

**When people see these statistics, eyes tend to glaze over. There is not a sense of urgency**

**out there in the land. So why should people feel a sense of urgency? Politicians aren't expressing a sense of urgency. No one feels that the crunch is coming tomorrow.**

We have a failure of leadership in America, and it is a bipartisan problem.

**When does this become a crisis?**

First, Medicare is already in a negative cash-flow position. The Social Security surplus will start to decline in 2009. It is estimated to have negative cash flow in 2017. So those are some interim dates, but the most likely fiscal crisis that we would see is a reluctance on behalf of foreign investors to continue to buy our debt at the rates that they have in the past, for the interest rates that we are providing.

**That is happening already. The Chinese are talking about moving [more] of their money into euros.**

And OPEC nations are doing the same. The OPEC nations started before the Chinese did ... It is really frustrating when the numbers are clear and compelling and when you know that you have a tsunami of spending that is heading for your shores, and yet you still have people partying on the beach. That is analogous to the situation that we face. At the same time, elected officials don't like to have to make tough choices, unless and until it is necessary, because they are afraid they might lose their job. My view is there are only two ways that you can achieve dramatic and fundamental reforms, one of which is if you have a crisis. The second is if you have committed, inspired, and determined leadership, and I personally think the second is preferable to the first.

**Does the current social contract, whereby Americans at a certain age are entitled to Social Security payments and medical coverage, need to be scrapped or rewritten?**

I think there is no question that we are going to have to review the current social contract. There will have to be modifications to both Social Security and Medicare; much greater modifications to Medicare than Social Security because the financing gap is multiple times greater. And I think we also have to recognize that our Medicare challenge is really a subset of the broader health-care challenge. Ultimately, we are going to have to reform our entire health-care system in installments over a number of years because if there is one thing that could bankrupt America, it is health-care costs.

**To your mind, are any of the candidates out there in the '08 campaign offering sensible ideas to address these issues?**

Once the nominees have effectively been determined, which I think will be in February or March of 2008, then I plan to focus more attention on what their specific proposals are, and I also propose to offer them a briefing on fiscal and other issues based upon GAO's good work. I have already had several candidates ask me to provide them a briefing, and I have done that.

**Which candidates?**

Well, I would rather not say which ones. I will tell you that it has been on both sides of the aisle, and I am only doing it right now on a request basis because there are so many candidates.

**Fred Thompson declared last week that he aimed to reform Social Security by reducing benefits and also by creating voluntary investment accounts. Without commenting on the specifics of his plan, do you support some form of privatization for Social Security?**

You have to keep in mind that Social Security is one of several elements of our retirement-income security system. Only 50 percent of workers in this country have a private pension plan. [And] we have the lowest personal savings rate of any industrialized nation. So, when you look at those two facts, you recognize that Social Security is very, very important, and that is why I think serious consideration has to be given to maintaining the basic Social Security program as a defined-benefit program that provides a strong safety net for people at or near the poverty level and encourages people to work longer because we need that for economic growth and other reasons. Now, I also think that in addition to [that], we need to consider a mandatory supplementary personal savings account that would be achieved through payroll deduction, that would go into a real trust fund, that could serve to provide an enhanced retirement benefit, and also would be transferable to one's heirs if you passed away before those funds were exhausted.

**On the other side of the aisle, Barack Obama and John Edwards have proposed to raise the ceiling on payroll taxes as a way of getting more money into Social Security. And they've accused Hillary Clinton of ducking the issue. How much would raising the ceiling help?**

Well, it depends how much you raise the ceiling. If additional revenues are going to be part of a Social Security reform package, then the most likely form that will take is an increase in the taxable wage base in order to have that burden be borne by those who are better off.

**Elderly people represented by the AARP vote in larger numbers than young people and that has made it politically difficult for anybody in office to make these tough choices that you're talking about. How do you get around that?**

I think most seniors care about their kids and their grandkids. And I think that once they are told the truth--that the federal government is spending more money than it makes, that it is charging the national credit card, and it is expecting their kids and grandkids to pay it off with compound interest--[they will see that] that is fiscally irresponsible and morally wrong.

**What about the notion that we can grow our way out of this, that if you lower taxes and get more growth and more taxable revenue, that somehow we will find a way out?**

There is no way we can grow our way out of these problems. We would have to grow at double-digit, real GDP growth for decades in order to close the gap that we currently face, absent reforms. We haven't grown at that rate in modern times, and we are not going to grow at that rate.

**There are a couple of proposals out there now to establish a bipartisan commission that would suggest changes, very specific changes, which the Congress would then have to vote on as a package without amendments. This would sort of end-run the political process, and give people a bit of political cover. Do you think that is a good idea?**

I do believe it is a good idea to form some type of capable, credible and bipartisan commission or task force. And in my view, at a minimum, any such commission or task force would have to address the need to reimpose tough budget controls, to engage in comprehensive Social Security reform, to engage in round one of comprehensive tax reform, and to engage in round one of comprehensive health-care reform. If Congress were able to act and the president was willing to sign a package that included those four elements, it would likely result in a significant down payment in our large growing fiscal imbalance.

**It seems like an awful lot to take on all at once.**

In some ways, you are better off to have more to deal with than less because you have more of an opportunity for tradeoffs.

**But health-care reform, for instance?**

Well, round one. You know, in my view, one of the things we are going to have to do in this country is something we have never done before. We have never had a national discussion and debate over what type of health care is in our broad-based national and societal interest to [provide for] every American. We actually have very perverse incentives in our system right now.

**What are the perverse incentives right now?**

Well, right now, no matter how much you smoke, no matter how much you drink, no matter how much you eat, you get the same taxpayer subsidy.

**Right. So what would be the alternative?**

There could be a risk-based premium. See, one of the things we have to debate ... there is a difference between whether or not you ought to be eligible for a program and how much the taxpayers ought to subsidize you. Those are fundamentally different things.

**How would you know, for instance, how much somebody drinks?**

Well, there are lab tests you could take.

**But does the government want to get into the business of conducting blood tests on people to see what kind of lifestyle they are leading?**

You know, we are kind of drilling down into the weeds here. My view is there are certain types of services that I think we are going to need to make sure that everybody has. Let me give you possible examples: inoculations against infectious diseases; certain wellness and preventative-care services that are clearly cost-beneficial; protection against financial ruin due to unexpected catastrophic illness or accident (while avoiding heroic measures), and guaranteed ability to purchase additional insurance at group rates should you desire to do so. That is the basic and essential package. Then you have to say, "Well, how are you going to price it?" That gets to a whole range of other issues. Does it make sense for everybody to be subsidized to the same extent, irrespective of his or her means?

**As I understand it, you regard the prescription-drug benefit as grossly irresponsible.**

The most fiscally irresponsible act in decades.

**Are there other measures under consideration now that you would regard as equally irresponsible?**

There are always some out there, but there are very few that come with \$8 trillion price tags, which the Medicare prescription-drug bill did.

**There has been talk in the campaigns about comparing the system here with systems in Europe, Canada and elsewhere. Some of the campaign rhetoric is very negative, and it's sort of an easy shot: "We don't want to become like those Europeans who have terrible health care." How would you compare the American system to, say, a particular European system?**

Well, first, I think there is a lot of misinformation and disinformation that is being provided to the American people. Even in countries that have national health-insurance systems, like the United Kingdom, there are private supplementary-insurance systems that exist in parallel to that. Most major employers of the U.K. have private insurance policies that cover their key employees and many other employees, as well. So this idea that it is one type of system under all circumstances just is not true. Secondly, if you look at other countries that do have national health-insurance systems, they have budgets on how much money they will spend, and that is one of the reasons they won't go bankrupt on health care. We don't have a budget on what we spend. We write blank checks. Nobody with a brain writes a blank check, especially on something that is 16 percent of the economy and growing much faster than the economy.

**Just for perspective, can you compare the size of this fiscal "tsunami" [to the size of particular spending programs]?**

Well, you could decide not to renew the Bush tax cuts, you could eliminate all foreign aid, eliminate all earmarks, eliminate NASA, eliminate the National Endowment for Humanities and eliminate the entire Defense Department tomorrow, and you still wouldn't solve the problem.

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