Attention: Deficit

Should progressives embrace entitlement reform? Or look elsewhere to narrow the gap? An exchange between two leading fiscal experts.

ISABEL SAWHILL: The growth of entitlements is on an unsustainable path. If allowed to continue, spending on Social Security, Medicare, and Medicaid will require untenable tax increases, crowd out almost all other spending, or lead to a dangerous accumulation of debt. If any of these scenarios unfolds, the nation's ability to remain economically competitive will be substantially weakened, and enormous burdens will be imposed on the poor and middle classes.

As all sides in the debate know well, the politics of entitlement reform are toxic. Only 7 percent of the public is in favor of cutting spending on either Social Security or Medicare. Shielding these programs from change—almost any change—has been a winning hand for progressives in the past, including in 2005, when George W. Bush's Social Security privatization efforts crashed. But it's a political strategy that may jeopardize the entire liberal agenda going forward.

ISABEL SAWHILL *is the director of the Budgeting for National Priorities project at the Brookings Institution, where she also co-directs the Center on Children and Families.* GREG ANRIG, *vice president of policy and programs at the Century Foundation, is the author of* The Conservatives Have No Clothes: Why Right-Wing Ideas Keep Failing.

First, preserving the status quo will erode trust in government. A government that has lost control of its fiscal future, with most of its budget on automatic pilot and a fifth of its expenses unpaid for, cannot garner much respect from its citizens. The Urban Institute's Eugene Steuerle calls this a decline in "fiscal democracy," because mandated spending—the product of past decisions—absorbs all revenues, leaving no scope for policy innovation if these programs are considered untouchable. Already the "big three" entitlements are absorbing 71 percent of all revenues. The erosion of trust that fiscal indiscipline engenders will, over time, leave the party that wants to use government for progressive ends unable to win elections. We are already seeing public frustration with fiscal profligacy producing political victories for those who seek to minimize the activist state.

Second, preserving these programs is a transactional strategy that, despite its political benefits, is at odds with transformational ideals such as providing greater prosperity and opportunity for all Americans. If progressives care about protecting the less advantaged along with other social programs, finding savings in the big three entitlement programs will be essential. Unless we free up resources to invest in education and job opportunities for younger Americans, and provide a healthy start for children from less advantaged families, prosperity and opportunity will elude us. The rapid growth of spending on entitlements has already forced the Obama Administration to propose a freeze in non-security domestic spending. In California, Governor Arnold Schwarzenegger has proposed eliminating the state's welfare-to-work program as well as most child-care assistance for low-income families, a harbinger of what may happen at the national level as the budget squeeze plays out over the next decade or two.

Third, the higher tax rates that unreformed entitlements will demand in the future will be even more unpopular than making the needed reforms now. Without reform, taxes would have to double or triple by 2050, according to the Congressional Budget Office (CBO). There is no lock box out of which the government can fund the costs of those who are retired. Yes, there are trust funds for Social Security and a portion of Medicare, but these funds contain nothing more than paper IOUs, not real resources that can be used to pay the costs of these programs. There are only today's and tomorrow's workers, whose capacity to pay the retirement costs of their parents' generation will depend on earlier investments in their own education and other productivity-enhancing programs. Higher taxes are inevitable, but a doubling or tripling of taxes for working-age families is neither economically sensible nor politically feasible. Even before the current recession, the high costs of housing, child care, and college tuition left their wages stagnant, their job security threatened, and their pocketbooks flattened.

Reforms enacted now can be phased in gradually—no one need be seriously hurt in the process. Pushing through such changes now would send the right signals to financial markets, while slowing their implementation would provide time for the economy to recover from recession and for those approaching retirement to adjust to any reform.

What kinds of changes should progressives support? First, because health care is the biggest problem we face, we should craft reforms recognizing that not all spending on health care improves health. Second, reforms should trim benefits for the more affluent while protecting those at the bottom. Third, reforms should leave our core commitments to Social Security and Medicare intact and ensure that no one is left bereft of access to basic health care and a decent income in old age. It is only by returning these programs to solvency that we can ensure that they will be there for those who need them most.

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Everyone knows that health care is the big enchilada. The recently enacted Affordable Care Act expands access to health care, but its effects on projected deficits and health-care spending trajectories are very small and highly uncertain. (For more on the health-reform legislation, see Jacob S. Hacker's piece, "Health-Care Reform, 2015," starting on page 8.) While a portion of the projected increase in Medicare and Medicaid spending can be attributed to the aging of the population, a bigger portion is due to rising health-care costs per capita in the public and private sectors. Health spending has grown about 2.5 percentage points faster than the economy over the past four decades. If this trend continues, Medicare and Medicaid *alone* will absorb every dime of federal revenues at current tax rates by some time in the 2040s. These cost increases are driven by the availability of new and better treatments and drugs, the open-ended, fee-for-service nature of the system, and a lack of incentives for either providers or beneficiaries to control costs given that most of the bills are sent to third parties (either employer-based insurance plans or the government).

Given these problems, what can be done? Over the long term, there will need to be structural reforms to the health-care system, with the goal of providing better care for less money. In the shorter term, reducing costs may well require setting limits on per-capita public spending. Such limits could lead to cost shifting to individuals or to the private sector, or to a denial of needed care to consumers. However, without such limits, it's doubtful that the needed reforms would happen quickly, and some of them may not happen at all. Limits provide the discipline within which greater efficiency becomes not just possible, but also necessary.

How do we achieve greater efficiency? One option is to link provider reimbursements and public subsidies for patients to evidence of effectiveness. Right now, there is little relationship between medical expenses and patient outcomes. Indeed, some estimates suggest that roughly 30 percent of all health-care expenditures do nothing to improve people's health. Instead of paying for more and more treatment, we need to start paying for better outcomes wherever possible.

Social Security is a far smaller problem than Medicare. Like Medicare, the costs of the program are rising because of the aging of the population. Because of increased longevity, today's seniors are expected to spend one-third of their adult lives in retirement. If enacted soon, Social Security reform could make the system solvent again without reducing benefits at all for those who are most vulnerable or dependent on the system, such as the disabled, low-income individuals, and the frail elderly. Indeed, any reform of the system would probably shore up benefits for at least some of these groups and address any gaps or inequities in the process.

To reduce costs, one alternative is to slow the growth of benefits for the more affluent while protecting, or even improving, promised benefits for those whose lifetime earnings have been more limited. No one would get less than they do now, in inflation-adjusted terms, but the amount of income replaced by Social Security benefits alone would decline modestly for those whose incomes were in, say, the top fifth of the distribution. Currently, household incomes of seniors in this quintile exceed $75,000 a year, a figure that will be closer to $100,000 a year by the time any change in the benefit formula were to take effect. This linking of benefits to income is something that liberals should applaud. It would not only make benefits more progressive but also increase public confidence in the system and its ability to provide for all those who really need it.

Another option is to raise the retirement age. Under a law enacted in 1983, the normal age of eligibility was gradually increased to 67—but this provision will not take full effect until 2027. By accelerating the implementation of that provision and then indexing the normal retirement age to increased longevity for younger cohorts until it reaches age 70, a significant portion of the current financing gap (about one-third) could be closed.

Although there are other reforms that might make sense, these two illustrate what needs to be done, and by themselves would eliminate the 75-year fiscal imbalance in the Social Security system.

None of these reforms, if done right, would deprive seniors of effective health care or a basic income in retirement. Indeed, by making current systems more sustainable, these reforms would actually increase the likelihood that they will still be there for future generations. And by making Medicare, Medicaid, and Social Security less costly, the reforms would free up resources to invest in the younger generation and keep tax burdens for working-age Americans at reasonable levels.

Providing a basic entitlement to health and retirement in old age has reduced economic insecurity and made government a positive force in people's lives. But promised benefits are no longer affordable. Americans are living longer than ever, and health care advances are swallowing a larger and larger fraction of the budget. An increase in the size of government is inevitable. The trick will be finding the right balance between higher taxes on the working-age population and slower growth in promised benefits for those who have retired. By addressing this challenge head-on, progressives can protect the vulnerable, make the system still more progressive, reallocate resources to investments in the young, and restore confidence in government's ability to act responsibly.

GREG ANRIG RESPONDS: Isabel Sawhill believes that the best way for progressives to restore public trust in government is to make painful cuts to highly popular and effective social-insurance programs. This is, to put it one way, a counterintuitive position. My view is more straightforward: For progressives to restore public faith not only in government but in themselves, they have to forcefully defend and build on their greatest successes, such as Social Security, Medicare, and, to a lesser extent, Medicaid and its companion Children's Health Insurance Program. These programs improved security and opportunity for all generations of Americans. They don't need to be cut; they need to be enlarged and strengthened.

Fiscal responsibility is important, and Democrats have demonstrated for many years that they take that responsibility far more seriously than Republicans: Witness President Bill Clinton's remarkable success in transforming deficits into surpluses as far as the eye could see. But accounting prudence is not a cause that in its own right can directly improve the lives of Americans in lasting, concrete ways that generate political excitement and attachments. Clinton's feat yielded neither political benefits to Democrats, nor economic gains to Americans, nor a continuation of sound budgetary practices in the decade that followed.

Even worse, the mania for deficit reduction threatens to sabotage the economic recovery. The preoccupation with deficits is preventing a more robust federal response to unemployment levels near 10 percent, even with large Democratic majorities in Congress, a demonstration of just how self-destructive budget hawkery has become. Undue concern over deficits is impeding additional public investment that would lead to job growth, higher consumption, and increased tax revenues from rising incomes. Virtually all economists agree that last year's stimulus bill helped to stanch job losses, so why not build on that proven success with a major bolus of additional stimulus to drive unemployment down further? Because, we're told somberly, our grandchildren will suffer for it in 2050.

Once solid job growth finally resumes, whenever that might be, then indeed major steps will need to be taken to prevent deficits from climbing to unsustainable levels beginning in the 2020s. As Sawhill indicated, those daunting projections derive almost entirely from expectations that health-care costs will continue to rise much faster than inflation. Skyrocketing costs will cause spending on Medicare and Medicaid to soar, just as private insurance expenses are also expected to continue escalating rapidly. The new health-care legislation—a huge progressive accomplishment, not incidentally—extends Medicare's solvency by a full decade while including many provisions aimed at making the program more cost-effective, primarily by reducing the use of unnecessary tests and procedures. We don't yet know which, if any, of those changes will work. But the bill creates the beginnings of an institutional framework that has the potential to eventually reduce the rampant wastefulness in our health-care system and curb the unsustainable rate of spending growth. Going forward, progressives should be prepared to aggressively build on that structure by expanding on the successful experiments and recalibrating less effective initiatives. The next round of reforms also ought to include a public option for the new insurance exchanges that would have the potential to exert leverage in ways that further control costs.

Beyond that, though, the kinds of changes for Medicare that Sawhill recommends would do nothing to affect the central cost-effectiveness challenge. Setting arbitrary limits on per-capita public spending, as she concedes, would almost certainly lead to cost shifting to individuals or to the private sector (which in turn is already shifting them further and further to individuals as well). Given the extent to which Medicare beneficiaries already bear a substantial and rising share of their health-care costs—the program's deductibles are generally higher than is standard in private insurance, for example—imposing a global cap on spending would simply weaken already modest protections for individuals without constraining costs. What's progressive about that?

Deficit hawks habitually invoke bank robber Willie Sutton when they talk about having no choice but to cut social-insurance programs, arguing "that's where the money is." But actually, there are all kinds of multi-trillion dollar targets for long-term deficit reduction that could be tapped without imposing unnecessary pain on the vast majority of Americans, and which in many cases would make the government more cost-efficient. Taking aim at those pots wouldn't bend the notorious health-care cost curve, but going after them beginning later in this decade would keep deficits at a manageable level until reforms eventually do significantly rein in medical costs.

The most obvious source of savings is the defense budget. A bipartisan task force organized by the Project on Defense Alternatives issued a report in June spelling out specific defense cuts that would save $960 billion between 2011 and 2020 alone. The report emphasizes how those changes would not weaken America's military capabilities. While the powerful defense industry lobby will fiercely resist reductions to their federal largesse, the pushback arising from their parochial interests would be meek compared to the public backlash against deep cuts in universal programs.

Another massive target is the welter of so-called "tax expenditures"—basically, government subsidy programs that take the form of tax breaks. The CBO tabulates that there are some 165 tax expenditures that will cost the federal government more than $5 trillion over the next five years; those include the home-mortgage-interest deduction and 401(k) tax-deferred savings plans, as well as industry-focused write-offs like the percentage depletion allowance for oil companies. Unlike conventional discretionary spending programs, tax expenditures are not subject to ongoing congressional oversight or annual appropriations, so there's little accountability in assessing how effective they are at advancing their intended purpose. Many of them disproportionately benefit high-income individuals or narrow industry classes.

One particular inequity is the tax-favored treatment of capital gains and dividends. Taxing income from investments at the same rate as income from work would raise upwards of $1 trillion over a decade while almost exclusively affecting very high earners—the 0.3 percent of tax returns reporting income in excess of $1 million accounted for 61 percent of all capital gains in 2006. The tax code would become much simpler, more equitable, and economically efficient in the process, without significantly affecting the economy. Such a change also happens to be a reform that Ronald Reagan signed into law back in 1986 as part of a major overhaul that reduced overall income tax rates while eliminating many write-offs, a model that just might be politically plausible again in the coming decade.

One thing we definitely don't need to do is cut Social Security by further raising the retirement age or otherwise reducing what future retirees will receive. The program is essential to many millions of Americans, including 4.4 million dependent children—about 3.5 million under age 18 and 900,000 adults disabled before age 22. Another 3.4 million children, though not receiving benefits, live in households with one or more relatives who do. But it is by no means overly generous; the annual benefit of about $13,860 a year for an average retired worker is only slightly above the poverty level of $10,830. Compared to 30 Organization for Economic Cooperation and Development (OECD) nations, the United States ranks 25th in the share of an average worker's earnings that is replaced upon retirement by a country's public pension program. And those Social Security replacement rates are already scheduled to be declining in the years to come, and will continue to be substantially lower for relatively well-off retirees compared to other beneficiaries. Contrary to the implication that the elderly population has an abundance of "greedy geezers," just 13 percent of households headed by an individual 65 or over had after-tax non-governmental income of more than $50,000. Going after their benefits with a vengeance wouldn't raise enough money to justify the effort.

According to Social Security's trustees, the program will be able to continue paying full benefits until 2037. Over a 75-year period, the gap between promised benefits and revenues amounts to 0.7 percent of GDP. That's barely a drop in the bucket compared to the overall budgetary shortfall attributable to health-care inflation, which is unrelated to Social Security. Gradually raising the Social Security payroll-tax cap back up to its past levels of 90 percent of total payroll income—which would increase the lid from today's $106,800 to about $186,000—and removing the cap entirely for just the employer contributions would sustain current benefits in full throughout the 75-year time horizon. Only the top 6 percent of earners would be affected at all.

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The economic crisis that we have not yet fully emerged from would have been far worse without the protections that progressives built over the course of many political battles since the 1930s. They are the essence of what we have accomplished at the national level to make our society more humane. The abundant work still to be done will proceed more successfully if we embrace those popular programs and explain to the public why we need to make them even stronger. Delivering on that promise without abandoning the Democratic Party's well-established commitment to fiscal responsibility is the clearest path to restoring the public's trust in government and progressivism. For all its imperfections, the health-care legislation, which will greatly expand medical coverage while reducing future deficits, embodies what our side is about. We believe not only in efficient government, but one that effectively protects all Americans from widespread risks like inadequate retirement savings, major medical costs, and disability.

SAWHILL RESPONDS: Greg Anrig is right that my position on social-insurance programs is unorthodox. Arguing that these programs need to be transformed goes against the grain of traditional progressive thinking. But I believe that this transformation can be undertaken in a way that strengthens progressive values, paves the way for a restoration of faith in government, shores up the social safety net for the poor and working class, and frees up resources with which to tackle new problems.

Rather than repeat my earlier arguments, let me address his well-argued points. Anrig states that deficit mania threatens the nascent recovery. I agree that we need to stimulate the economy and that cutting the deficit right now would be a bad idea. However, the presumed tension between continued stimulus and fiscal constraint is a false one. It's purely a matter of timing. We need stimulus now and restraint later. The restraint should be enacted now but gradually phased in as the economy improves. Without any fiscal discipline, the recovery is endangered. Concern in the financial markets about the sustainability of our spending could produce a sharp spike in interest rates at any time and leave another economic crisis in its wake. As it stands, spending is way out of whack with revenues and it's only a matter of time before markets wake up and react in ways that could be disastrous for everyone, but especially for the less advantaged. Unemployment rates could surge way past 10 percent. To be sure, concerns about deficits have made Congress timid about supporting any new stimulus measures. But if the Administration and Congress were to enact credible legislation to bring spending and revenues into balance over the medium and longer term, that step alone would help defuse mounting anxiety over deficits.

While we both agree that health-care spending is the key to deficit reduction, Anrig is more optimistic than I am about the ability of the new health-care legislation to narrow the gap. Under realistic assumptions, deficits over the next decade are estimated at close to $10 trillion. The health-care bill will dent this amount by only a very modest $124 billion, or less than 2 percent, according to the CBO. Savings in the second decade are projected to be a little larger but still not close to what is needed, and highly uncertain in any case. Moreover, the estimates assume that Congress will not get cold feet on the proposed cuts in Medicare and on raising taxes (or fees) on so-called Cadillac health plans. The stark unsustainability of the health-care spending numbers leads me to reluctantly endorse the idea of limits on per capita public spending for health care. Other advanced countries, such as Britain and Canada, have taken this road, and their citizens are no less healthy or content with their care than those in the United States. All of the reforms Anrig mentions should be used to bend the curve, and if they work as well as he hopes, the limits I am proposing need not be binding. The alternatives are either massive tax increases on working-age Americans or a decimation of everything else that government does. It is a matter of simple arithmetic.

On Social Security, Anrig worries about the children, disabled adults, and low-income seniors who currently benefit from the system. We both agree they should be protected. But we differ on the extent to which a significant segment of the elderly can afford to contribute more to their own retirement costs in the future and should be expected to do so. Social Security was never intended to be the sole source of support in retirement, but simply one leg of a three-legged stool. The other two legs are pensions and personal savings. Encouraging, or even requiring, working-age Americans to begin saving more for their own retirement makes more sense to me than raising their taxes to unprecedented levels. Progressives like to criticize conservatives for their mindless focus on keeping taxes low, but we shouldn't assume every problem can be resolved by raising taxes and that individuals don't bear some responsibility for their own future welfare. According to Eugene Steuerle, the lifetime retirement costs of the typical married couple comes to $900,000. With a sharply declining ratio of working to retired Americans, that's a bill the next generation may have to renegotiate.

There are other sources of budgetary savings in addition to the big social-insurance programs. Anrig mentions defense spending, in particular, and I was heartened to learn that the Project on Defense Alternatives has recommended $960 billion in savings over the next decade. Yet although this sounds like real money (and it is), it is still only a fraction of the $10 trillion gap over the same period—a gap that just keeps getting bigger as we move further into the future.

Finally, we come to an issue on which we very much agree: tax expenditures. As Anrig notes, they are really just backdoor spending programs that never get reviewed and now cost close to $1 trillion a year. The biggest of these special subsidies are the mortgage-interest deduction and the exclusion from taxes of retirement savings and health-care benefits from employer-provided insurance (much debated as part of the health-reform bill, with a really wimpy outcome). The popularity of these items with the public rivals that of the social-insurance programs, with the difference being that finding a compromise with conservatives is less likely here than on the spending front. Some of the other ideas he mentions, such as curbing corporate subsidies and raising taxes on dividends and capital gains, are all worth pursuing. We should make all of this part of broad-based tax reform that would not only raise more revenue in the future, but also make the tax code simpler, more efficient, and more progressive. We should also allow most of the Bush tax cuts to expire as soon as the economy recovers, a step that would close at least a quarter of the projected budget gap five years from now. Unfortunately, the President and most congressional Democrats don't want to raise taxes on anyone making less than $250,000, even though a lower threshold makes a lot of sense. We lived with higher tax rates in the 1990s, and we could do it again.

At the same time, progressives should not assume, as so many seem to, that hiking taxes can be the entire solution to our fiscal problems. It will be hard to find even half the needed savings, especially in the longer term, through tax reform. Of course, the American public has an irrational prejudice against the kind of higher taxes found in some other advanced countries. But it's not irrational for them to be leery of taxes that are double what they pay now. Politics aside, working-age Americans, the group that pays most of the taxes, have endured tough economic times. Their future prospects will be compromised unless we find the resources to invest more in education, infrastructure, and new technologies. At present, these resources are simply not available.

So, my question for Anrig is this: What should we do about looming deficits in both our budget and our public investments? Is he arguing that we can address the problem just with revenue increases and some cuts in military spending, or counting on more savings in the health-care programs than CBO assumes? Or would he support some changes in the big social-insurance programs, both to reduce the red ink in our future and to finance education, infrastructure, and other priorities that can improve productivity and standards of living? No one likes eating spinach, but I have a hard time seeing how we can face the future without some serious reform in these programs.

ANRIG RESPONDS: It's clear that Isabel Sawhill and I would have relatively little difficulty reaching agreement on many reforms that would advance progressive goals and strengthen the federal government's long-term fiscal outlook. We both support greater and more effective investment in early childhood programs, education, and infrastructure; we both advocate overhauling the tax code to produce substantially greater revenues while making the system more fair, efficient, and simple; we both favor streamlining defense spending to eliminate unnecessary, high-cost projects; and we both think that our social safety net is inadequate and needs to be strengthened.

But, in contrast to Sawhill, I believe that reducing Social Security, Medicare, and Medicaid benefits would unnecessarily impose new financial burdens on American families, alienate the public, and fail to address the core problem of soaring health-care costs. To answer her question about whether the ideas I proposed would be sufficient to adequately address looming deficits while allowing for new public investments, the answer is yes—at least until the early 2020s or so.

After that point, if medical inflation remains out of control, deficits would start to rise again. But that would be the case even if the social-insurance reductions that Sawhill recommends were implemented. It's the high rate of growth in health-care costs that's driving the spiraling deficit projections, not the baseline benefit levels. And as we have seen with past unsuccessful efforts to impose a cap on Medicare fees to doctors, as well as the old Gramm-Rudman-Hollings Act, which futilely tried to keep a lid on federal spending through rigid targets, ceilings don't work in practice because they cause too much pain to be politically sustainable.

I prioritize universal social-insurance programs so highly because they represent what government does best. By including all citizens in the pool covered by insurance protections, the programs spread risks across the entire population. That feature, along with economies of scale and the absence of a need to earn profits, enables the government to minimize costs relative to private-sector insurance. And, in contrast to means-tested programs like Medicaid and Head Start that struggle perpetually against public hostility, the popularity of social insurance creates a virtuous cycle in which the programs are continually improved over time. In an April *New York Times* poll, 76 percent of respondents said that "the benefits from government programs such as Social Security and Medicare are worth the costs of those programs," versus just 19 percent who disagreed. Even among the 18 percent in the sample who said they supported the Tea Party movement, 62 percent concurred with the statement. Trying to impose new forms of means-testing on those programs, as Sawhill suggests she would, risks undercutting that public enthusiasm by moving them in the direction of welfare.

I also question Sawhill's premise that constraining social-insurance programs will "free up resources to tackle new problems." I don't share her optimism; it seems doubtful that the same collection of political actors who would reduce Social Security and Medicare benefits would also simultaneously redirect the money toward something like universal pre-K. On the other hand, the newly enacted health-care legislation, the stimulus bill's investments, and the creation of the Children's Health Insurance Program under President Clinton are all examples of tackling problems in fiscally responsible ways without reducing social-insurance protections.

Efforts to cut benefits are frequently predicated on data that seeks to portray retirees as having more financial security than they actually do. Sawhill cites Eugene Steuerle's claim that the lifetime retirement costs to the government of a typical married couple amount to $900,000. This is the kind of nugget that can create the misleading impression that older Americans are living high off the hog on the backs of workers. It omits the payroll tax contributions retirees made when they were employed and the medical insurance co-payments they owe in their old age. And however one might choose to make this sort of calculation, you can come up with a big number mainly because of high and rapidly rising health-care costs, which disproportionately affect the elderly because they need more medical care.

Again, compared to other countries, Social Security pays only modest benefits. As the Baby Boom generation retires, benefits will go from today's 4.8 percent of GDP to about 6.2 percent by 2035 and level off thereafter. There's nothing unaffordable or excessive about that, and the increase has been long anticipated. The 1983 reforms that Ronald Reagan signed into law have already largely sorted out how what he called an "iron-clad commitment" will be met. That agreement entailed raising payroll taxes on the Boomers and younger generations while delaying the retirement age, which already has been raised from 65 to 66 and is scheduled to be gradually increased to 67 over the next dozen years. Reneging on that deal by cutting benefits further now would be simply unfair—and fairness is a cornerstone progressive principle.

Imposing new forms of means-testing on Social Security and Medicare, as Sawhill suggests, risks moving them in the direction of welfare.

All this brings us back us to our hugely inefficient health-care system, which may be the focal point of our debate. Sawhill was rather dismissive of the impact that the health-care legislation will have on medical costs, which is somewhat understandable because so much uncertainty is involved. But it's worth noting that in the CBO's newly released long-term "extended baseline" forecast, the 50-year fiscal gap declined from 2.6 percent of GDP in its previous report to 0.8 percent—entirely because of the effects of the health-care legislation. This suggests that caution is in order before taking painful action today.

Sawhill argues that she supports per capita public spending limits on health care because some other advanced countries have instituted caps, and "their citizens are no less healthy or content with their care than those in the United States." But comparisons with other advanced nations also show that those countries have figured out ways to cover all their citizens at a much lower cost than we do, while generally providing better care. A new report from the Commonwealth Fund, a health-policy institution, examined the U.S. system in relation to six other countries, including Canada and the United Kingdom, and found that the United States "fails to achieve better health outcomes than the other countries, and…is last on dimensions of access, patient safety, coordination, efficiency, and equity." In that context, placing caps on public health-care spending, without first instituting a national system of universal coverage that would also give the federal government much greater cost-control leverage, will inevitably impose large new financial burdens on the elderly and poor.

Building on the new health-care legislation to implement changes that would elevate the United States from its abysmal international rankings will require a more robust federal role in the system. I have argued previously in *Democracy* in favor of federalizing Medicaid, in part because that highly decentralized program contributes to the fragmentation that enables rampant cost growth. ["Federalism and Its Discontents," Issue #15] The health-care reform bill takes important steps in the direction of federalizing Medicaid, but it still relies too heavily on states to carry out regulatory reforms and create insurance exchanges. It will be an ongoing project for decades to come to make our system much more efficient. Throughout the process, the goal for progressives should be to strengthen the rather meager protections Americans now receive. Every other advanced nation has managed to afford universal health care, and the United States can as well.

Sawhill emphasizes that individuals "bear some responsibility for their own future welfare." No one can disagree with that sentiment. But where would she draw the line? Given payroll taxes that workers have already contributed, at what individual income and/or asset levels should Social Security and Medicare benefits be reduced? Is there another country that might serve as a model for the United States, one that has found the right balance between individual responsibility and governmental protections?

Instead of serving up raw spinach that hardly anyone wants to swallow—for good reason!—progressives should be offering a menu that features more of what once made them popular. Every entrée should also include fiscal responsibility as a side dish, but deficit reduction isn't the main course.

SAWHILL RESPONDS: As Greg Anrig notes, he and I agree on many issues, from the need to reform taxes to the importance of spending more on public investments to the centrality of health-care costs in creating a fiscally unsustainable future. Where we disagree is on the most promising ways to constrain future health-care costs, on the right balance between spending cuts and tax increases, and on the relative importance of fiscal responsibility versus other goals.

We both believe that the health-care reform bill should be strengthened in ways that will reduce cost inflation. Anrig mentions a public option and the federalization of Medicaid as possible strategies for achieving this goal. These are promising ideas, but I am not convinced they are sufficient. He dislikes my proposals to cap spending and pay providers based on evidence of effectiveness. The fact is neither of us really knows what will happen to medical costs or what it would take to slow them down. But in the absence of stronger measures than those contained in the recent reform bill, I see nothing that reassures me. In light of four decades of costs rising 2.5 percentage points faster than GDP, I fear that progressives are engaged in wishful thinking about the seriousness of the problem.

Anrig buttresses his own optimism by citing a recent CBO report indicating that under their long-term extended baseline forecast, the 50-year fiscal gap has declined from 2.6 percent of GDP to 0.8 percent, entirely because of health-care reform. (The improvement is primarily due to the excise taxes on high-end plans, which 50 years from now will impose higher taxes on just about everyone.) But this estimate is, by CBO's own admission, based on a set of very unrealistic assumptions, such as the elimination of all the Bush tax cuts and reductions in doctor's fees that Congress is unlikely to support. Under CBO's more realistic "alternative fiscal scenario," this same gap is 6.9 percent! What this means is that Congress would need to enact an immediate reduction in spending or increase in revenues of about $1 trillion a year to put us on a sustainable course. If all of this money had to be found on the revenue side of the budget, taxes would need to increase by more than a third over current levels. Perhaps even more telling is the fact that CBO is unwilling to assume that health-care reform will have any effect on health-care costs over the long run. (They do expect some one-time savings over the next 20 years.)

One theme of Anrig's argument is the need to preserve and strengthen Social Security and Medicare—at all costs. My focus is on the costs, on what progressives give up by taking this stance. As I have tried to emphasize, these costs include: first, a loss of confidence in government's ability to manage its fiscal affairs; second, a crowding out of most other spending, some of it essential to the broad-based prosperity that progressives support; and third, punishing and politically unpopular tax increases for working-age Americans. Anrig argues that people who have paid into the system should receive their promised benefits. Unfortunately, these benefits are no longer affordable without raising taxes to unthinkable levels and increasing the fraction of Medicare expenses that come out of general revenues. My argument is that fairness demands that we balance the needs of senior citizens against the needs of working-age Americans and their children. Is it unfair to expect that future retirees in a household with an income above $75,000 might accept a little less from their government when we are asking working-age households with the same incomes to pay much higher taxes? (Anrig argues that such households are a very small fraction of the elderly. My data sources say they are about 20 percent of all households 65 and over, and I predict they will be a bigger fraction by the time any change in promised benefits is phased in.) Is it fair to cut spending on child-care and job programs for welfare recipients (as California has proposed) in order to preserve programs for those who are living quite comfortably? Progressives should fight for the kind of reallocation of resources toward the less advantaged that both Anrig and I favor. But they should not assume such resources will be available through tax increases and cuts in non-entitlement spending alone. Nor should they be sanguine about the possibility of preserving, much less improving, programs for the poor in the absence of responsible reforms.

We can escape the costs of unfettered growth in social-insurance programs in the short term by tolerating large and growing deficits while keeping our fingers crossed about the consequences. But a day of reckoning may not be far off. Anrig calls fiscal responsibility "a side dish," not the "main course." He states: "[A]ccounting prudence is not a cause that in its own right can directly improve the lives of Americans in lasting, concrete ways that generate political excitement and attachments." Ross Perot and the Tea Party might suggest otherwise. But more importantly, deficits *do* affect the lives of Americans. Deficits are not bad in and of themselves. They are bad because they adversely affect productivity and living standards, make us dangerously dependent on unfriendly nations, create a serious risk of an economic crisis, and limit what government can do in response to a crisis—whether a financial meltdown, a pandemic flu, or a natural disaster. And though it's a less tangible cost, I believe that, to many people, deficits are a symptom of a government that no longer works. When government is discredited, only conservatives benefit.

The costs of not acting: a loss of confidence in the government's fiscal management, a crowding out of other spending, and new taxes.

This has been a very useful dialogue, and I have learned a lot in the process. Hopefully, our debate will help other progressives think a bit more clearly about where they stand and catalyze a broader debate beyond these pages.

ANRIG RESPONDS: Isabel Sawhill nicely encapsulates our central differences when she writes that the costs of preserving and strengthening Social Security and Medicare are "first, a loss of confidence in government's ability to manage its fiscal affairs; second, a crowding out of most other spending…and third, punishing and politically unpopular tax increases for working-age Americans."

On the first point, polling data have consistently shown strong public support for Social Security and Medicare, and deep opposition to most forms of proposed benefit reductions like raising the retirement age. That's true in red, blue, and purple states, across income levels and age groups, and even among anti-government Tea Party supporters. In contrast, public concerns about deficits ebb and flow, largely depending on economic conditions rather than the actual balance between government outlays and revenues at any point in time. Ronald Reagan crushed Walter Mondale in 1984 notwithstanding the large deficits Reagan created, mainly because the economy had significantly improved. Democrats didn't benefit in 2000 from transforming deficits into surpluses during the previous decade.

John Sides, a political scientist at George Washington University, has concluded: "In Congressional elections, just as in presidential elections, the president and his party are not punished for running up the debt. They are punished for a weak economy." If the goal is to regain public trust in government, there's little evidence that strengthening fiscal conditions will matter much, and a lot of reason to believe that cutting Social Security and Medicare would only further alienate Americans.

On the second point, as I have argued, nothing has happened to date to support the belief that spending on the elderly deters new initiatives geared toward other generations. The health-care and stimulus bills are only the most recent examples. Big social-insurance programs directly and indirectly improve economic security for all generations. By reducing poverty rates among the elderly from more than 35 percent before 1960 to around 10 percent today, Social Security, Medicare, and Medicaid (which assists low-income Medicare beneficiaries) have significantly alleviated pressures on families to house and otherwise care for older members. That's a huge quality-of-life improvement for all ages. Moreover, most proposed benefit reductions over time would take deeper and deeper bites out of the payments owed to successive generations as they retire.

On the third point about tax increases, asking the 16 to 20 percent (depending on one's source) of older Americans with income above $75,000 to accept "a little less," as Sawhill proposes, would make barely a dent in the shortfall. The same would go for imposing a cap on Medicare and Medicaid spending, since it would be unlikely to yield lasting reductions based on abundant past experience with similar ceilings. The kinds of benefit cuts that would hammer away at federal outlays enough to bring down future deficits would also have to significantly weaken the economic security of American families who are far from comfortable. For example, raising the normal retirement age to 70 by 2036 would lead to a 10 percent reduction in Social Security benefits for workers between the ages of 40 and 44, according to the Center for Economic and Policy Research. That price is too heavy to pay and unnecessarily painful relative to other options.

Sawhill didn't respond to my question about which country is doing a better job than the United States in finding the right balance between individual responsibility and protection against costly risks that we all face. I would argue that pretty much every other advanced nation does a much better job, especially with respect to health care. They all get far more for their medical spending than we do. Since rising health-care costs are the only reason we are having this debate about high future deficits, progressive reformers should be focusing on making the system more cost-effective, rather than ratcheting back past, hard-won accomplishments.

In addition to the fallout from the severe recession, states are cutting back on a broad range of services mainly because they have little leverage to control their soaring costs for Medicaid. Shifting those responsibilities over time entirely to the federal government would greatly alleviate state fiscal pressures and create promising opportunities to control health-care costs system-wide. Without question, increasing federal involvement in the health-care system is a highly problematic political challenge in this country, particularly given existing health-care arrangements and the small-state bias of the Senate and its sundry supermajority rules. But it is the fight progressives should be focusing on.

A team of researchers led by Yale political scientist Jacob S. Hacker just released a report documenting that the proportion of households that experienced at least a 25-percent drop in available income has risen over the last 25 years, with projections showing a new high in 2009. As employers have dropped or curtailed health-care coverage and shifted workers from defined-benefit pensions to volatile and poorly performing defined-contribution plans, the only reliable protections for average Americans have been Social Security and Medicare, buttressed by Medicaid. Those programs are the beachhead upon which progressives should continue to advance.

Many public policy debates periodically heat up and then cool down. But the discussion we have been having on entitlements and the deficit will soon reach a full boil—and will likely continue for years to come. **D**