REAL Debt Reform

If you want to watch something alarming, look at the U.S. Debt Clock (http://www.usdebtclock.org/), which calculates, second-by-second, America's rising debt (approaching $14 trillion), federal spending (nearly $3.5 trillion a year) and budget deficit (roughly $1.3 trillion). Second-by-second the numbers increase, and you can also watch (more slowly) the inexorable rise in the average debt per U.S. citizen--currently more than $44,000, perhaps more by the time you read this and check for yourself.

The Debt Clock also lists the largest budget items and THEIR growth, and you can quickly see that they are not where most of the politicians have focused their attention and public statements. While incoming Congressional leaders talk about ending earmarks and cutting foreign aid, the back-breaking line items on the federal budget are Medicare/Medicaid, Social Security, Defense and war expenditures. At the bottom of the Debt Clock screen are some truly frightening statistics: add up all the future unfunded liabilities for Social Security, the federal prescription drug program and Medicare liability, and you get a future cost of $111.5 trillion. That's a little over $1 million per taxpayer.

Like any debtor who gets in over his head, the U.S. Congress faces painful choices. They can either make very difficult decisions now--and possibly alienate voters--or kick the can further down the road and leave a bankrupt country or crushing debt for our children or grandchildren to pay. The problem is great enough that a coalition of the very rich, including Bill Gates and Warren Buffet, are doing something unheard of: they are publicly arguing that Congress should end the tax cuts for them and others of the wealthiest Americans.

Is there a way to get both political parties talking about the hard choices? On December 1, a bipartisan National Commission on Fiscal Responsibility and Reform, made up of 18 prominent Republican and Democratic leaders, released "The Moment of Truth," a set of recommendations that would, if enacted, achieve a $4 trillion reduction in government debt. The group includes the chairmen and ranking members of the Senate and House Budget committees, the chairman of the Senate Finance Committee, a former White House budget director and a vice chairman of the Federal reserve board. To achieve their deficit reduction goals, the commissioners put everything on the table--Social Security, Medicare, tax rates, government spending, even the elimination of popular tax deductions.

You can read the full 49-page report here: http://www.cbsnews.com/8301-503544_162-20024235-503544.html. The report lists, on page 10, some of the considerations that went into the decisions, which you may or may not agree with: "We all have a patriotic duty to make America better off tomorrow than it is today;" "Don't disrupt the fragile economic recovery;" "Cut spending we cannot afford--no exceptions;" "Demand productivity and effectiveness from Washington;" "Don't make promises we can't keep;" "Keep America sound over the long run."

The plan would cut government discretionary spending and impose spending caps, including annual limits on war spending, impose 15% reductions in Congressional and White House budgets, a three-year freeze on annual Congressional pay raises, and eliminate all Congressional earmarks (9,000 in FY 2010, costing close to $16 billion).

The commission also recommends lowering tax rates and eliminating many deductions. There are actually several alternatives in the final proposal (pages 25-27), depending on which deductions are eliminated. One possible plan is to bring us down to three tax brackets of 12%, 22% and 28%--replacing five brackets ranging from 15% to 39.6% that is due to take effect in 2011. Corporations would pay at a flat rate somewhere between 23% and 28%, and lose most of their special subsidies and tax loopholes.

To get there, the Commission proposes that Congress eliminate all itemized deductions (everybody would take the standard deduction) and replace today's mortgage interest deduction with a 12% tax credit for mortgage loans up to $500,000. Capital gains and dividends would be taxed at ordinary income rates (rather than the preferential rates under current law) and the dreaded AMT, year by year affecting more and more "middle" class taxpayers, would be eliminated altogether.

More controversially, charitable donations, which are currently deductible for itemizers, would only qualify for a 12% tax credit, and only then to the extent that the gift exceeded 2% of a taxpayer's adjusted gross income. The Commission also proposed replacing the current melange of retirement plans (Roths, IRAs, 401(k)s, 403(b)s, defined benefit plans etc.) with one type of tax-favored retirement account for everybody; the maximum tax-preferred contribution would be $20,000 or 20% of income, whichever is lower.

The commission proposes to raise the age at which you could receive full Social Security benefits by indexing it to life expectancy. The Normal Retirement Age, which reaches 67 in 2027, would go up to age 68 by the year 2050, and 69 by 2075. The Early Retirement Ages, when people could opt for lower annual benefits, would go up to age 63 by 2050 and 64 by 2075. The taxable maximum wage cap on Social Security taxes, currently $106,800, would grow more rapidly than it has in the past, reaching $190,000 in 2020, versus roughly $168,000 under current law.

Finally, the current federal gas tax would be increased by 15 cents per gallon, a figure which is still significantly lower than most European countries. Among a variety of Medicare reforms, the Medicare physician payment formula would be changed to reward quality of care and outcomes, rather than the quantity of visits or procedures. And the government's civilian workforce would gradually be cut by ten percent.

If 14 of the 18 members of the Commission had voted to endorse the recommendations, then the full report would have been sent to Congress for a vote. As it is, only 11 endorsed their own recommendations.

Endorsing: Senate Majority Whip Richard Durbin (D-IL); Senate Budget Committee Chairman Kent Conrad (D-ND); House Budget Committee Chairman John Spratt (D-SC); former Federal Reserve Board vice chairwoman Alice Rivlin, Republican Senators Tom Coburn (OK); Mike Crapo (ID) and Judd Gregg (NH), plus Ann Fudge of Young & Rubicam, and Dave Cote of Honeywell International. Co-chairs Erskine Bowles (former Clinton White House Chief of Staff) and former Republican Senator Alan Simpson also voted for the proposal.

Opposed: Senate Finance Committee chair Max Baucus (D-MT); Rep. Xavier Beccera (D-CA); Rep. Jan Schakowski (D-IL); Rep. Dave Camp (R-MI); Rep. Paul Ryan (R-WI), Rep Jeb Hensarling (R-TX) and Andy Stern of the Service Employees International Union.

Nevertheless, even the dissenting members of the Committee believe it will change the debate in Washington, and focus Congressional attention on the hard choices rather than the easy sound bites. Let's hope so for the sake of our children and grandchildren.

Sources

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