President Obama's National Commission on Fiscal Responsibility and Reform recommended a set of steps that are projected to stabilize the federal debt in the short term and eventually reduce it to 40% of GDP by 2015. (Currently at about 60% of GDP, debt/GDP is projected to rise to 90% by 2020 and grow at an increasing rate thereafter if current policies continue.) The Commission proposes large cuts in virtually every aspect of federal spending, including defense and non-defense discretionary spending, Social Security, Medicare, and Medicaid. The spending caps would be enforced by new tougher budget rules that would require a super-majority to override in the Senate as well as a set of other process reforms. There would be significant cuts in the size of the federal workforce and a three-year pay freeze for civilian federal employees (including members of congress).

The proposal also calls for sweeping tax reforms—eliminating most deductions, exclusions, and credits, which would allow income tax rates to be reduced from current levels while increasing tax revenues, by about $1 trillion over the next ten years. Over the long run, tax revenues would be limited to about 21 percent of GDP, almost 3 percentage points above the post-war average of 18.3 percent, but far below projected spending under current law. Outlays would gradually be reduced from projected levels to match spending at about 21% of GDP, roughly the average level over the past 30 years.

<u>Questions</u>

1. Both the president's commission and a competing proposal by the Bipartisan Policy Center (of which I was a member) rely heavily on cuts in medical spending, especially for Medicare and Medicaid, to meet long-term budget targets. Past efforts to do this have been spectacularly unsuccessful (note the periodic "doc fix" legislation that regularly undoes limits on payments to providers under Medicare). Is tight spending constraint on medical spending unrealistic and what would happen to these plans if that key component proves to be unsustainable?
2. The aging of the baby boomers will put unprecedented demands on the public sector to pay for Social Security, Medicare, and Medicaid (which will fund most nursing home care). In that context, is it realistic to limit spending to historical levels or should it be allowed to increase somewhat (as recommended by the BPC task force)?
3. However, there is clearly much dissatisfaction about the size of government and a perception that taxes are too high. Should these commissions have tried to reduce spending even more? If so, how?
4. Both the president's and the BPC commissions called for tax reform as a way of reducing the debt. Tax reform is always politically difficult because it creates winners and losers. Is tax reform easier or more difficult in the context of budget reform?
5. The BPC plan called for the creation of a national "debt reduction sales tax"—basically a value-added tax—as a way to allow for more significant income tax reductions and somewhat higher spending. The president's commission considered a VAT and ruled it out. Which is a better approach?
6. Erskine Bowles, co-chair of the president's commission, said that his plan means that "the era of deficit denial is over." Based on the reaction to the plans by politicians and the public, do you think the prospects for budget reform are better or worse than they were a few months ago?

7. The BPC plan included a substantial short-term economic stimulus—a one-year payroll tax holiday estimated to cost $650 billion. The president’s commission acknowledged that spending cuts and tax increases might be premature with the economy weak, but did not make a specific proposal to address that problem. How should policymakers balance concern about potentially ruinous accumulations of public debt against the real concern that spending cuts and tax increases right now might plunge the economy back into a recession?