Social Security, Generational Justice, and Long-Term Deficits

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I. INTRODUCTION

The future of the Social Security system became the focus of intense public debate as President George W. Bush’s administration moved into its second term. Guesses about the adequacy of long-term funding for the system, the consequences of diverting tax revenues into private accounts, and the interaction of Social Security’s finances with the rest of the government’s spending and revenues shape the contours of the debate. Acting today instead of tomorrow, some argue, is
necessary to stave off future disaster.\(^1\) This is almost certainly false. Moreover, the focus on Social Security’s finances in isolation from the rest of public finance distorts the debate. The goal of fiscal policy should be, as it always should have been, to balance our current well-being against concern for the well-being of generations to come. Current policy discussions, unfortunately, often allude to that goal but fail to address it meaningfully.

If current and future well-being is the focus, the question then becomes how best to measure an unknowable future in a way that will assist policymakers in making difficult trade-offs. Ideally, we would like to be able to measure the effects of our fiscal choices into the indefinite future and to decide how and when to provide benefits and to raise revenue. The further we look into the future, however, the cloudier the picture becomes. Ultimately, we must choose between imprecise ideal measures and incomplete realistic measures.

This Article assesses current methods for evaluating the long-term viability and desirability of government activities, especially Social Security and other big-ticket budget items. I reach four conclusions: (1) There are several simple ways to improve the current debate about fiscal policy by adjusting crude deficit measures, improvements that ought not to be controversial. (2) Separately measuring Social Security’s long-term balance is inappropriate and misleading. (3) The methods available to measure very long-term government financing (fiscal gaps and their cousins, generational accounts) are of very limited value in setting public policy today, principally because there is no reliable baseline of the government’s likely future expenditures and receipts. (4) Therefore, the government’s current annual and 10-year deficit projections, while highly imperfect, are nonetheless the best measure available for assessing fiscal policy, especially compared with fiscal gaps and generational accounts.

This Article provides a summary of several prominent lines of economic thinking on issues of public finance, especially regarding long-term spending and taxing issues, and also offers new and extended critiques of those mainstream theories and of the public policy choices we face. The conclusions and policy prescriptions offered here are, to my knowledge, new to the literature.

\(^1\) Restoring Fiscal Sanity: How to Balance the Budget 16 (Alice M. Rivlin & Isabel Sawhill eds., 2004) (“The right time to address this problem is now. The longer we wait to get our fiscal house in order, the greater the risks to the economy and the more painful the solutions will be.”); see also Jagadeesh Gokhale & Kent Smetters, Fiscal and Generational Imbalances: New Budget Measures for New Budget Priorities 3 (2003) (“[S]pending must be reduced and/or taxes increased in order to put federal fiscal policy on a sustainable course.”); id. at 5 (“Moreover, the size of the necessary corrective policies will grow larger the longer their adoption is postponed.”).
There is little doubt that our current fiscal policy path is unwise, but it is essential to determine how best to assess what is wrong with current policies before we can understand how to change them.

II. Fundamental Challenges in Measuring Governments’ Activities

The decisions that we make today regarding taxes and government spending have profound effects not only on those living today, but on future generations as well. These effects arise for two reasons. First, our current taxing and spending decisions help to determine how the economy’s productive resources will be used now and in the future—whether, for example, a piece of land becomes the site for a casino, a day care center, or a cancer research institute. Second, a law that a government passes generally commits it to a course of action that can last well into the future. While it is surely true that some laws that claim to set policy for years in advance do not really do so (such as tax policies passed in 2001 that purport to expire in 2010), others just as surely represent commitments from which governments would have some difficulty withdrawing (such as government employees’ pensions).

These two effects of taxing and spending policies ought to be of concern to anyone whose time horizon extends past the current fiscal year. For those who care about the state of the world that we leave to future generations, the challenge is to find an analytical framework with which to predict the impact of current policy choices on future standards of living. Typically, these analytical frameworks are found in macroeconomic analysis of fiscal policy.

Macroeconomics, however, does not figure prominently in legal analysis. While the legal literature that relies on microeconomics has mushroomed over the last two decades or so, macroeconomics has remained largely in the background. With some exceptions, legal scholars have tended not to include in their analyses the aggregate

\[2\] The law and economics literature is too vast to summarize here. For a good bibliography, see Robert Cooter & Thomas Ulen, Law and Economics (3d ed. 2000).

economy within which microeconomic efficiency analysis operates. Certainly, some very good work has been done analyzing proposed constitutional amendments to constrain government spending or to limit tax increases; but such analyses need not directly address the question of how best to measure the fiscal status of the public sector.\footnote{See, e.g., Nancy C. Staudt, Constitutional Politics and Balanced Budgets, 1998 U. Ill. L. Rev. 1105 (arguing that a constitutional amendment requiring a balanced budget is unnecessary because the budget balancers have won the political debate).}

\section{Deficits and Accounting Issues}

The default position in public debate typically has been that fiscal responsibility is synonymous with annually balanced budgets (or, more extremely, with zero public debt).\footnote{See, e.g., Stephen Moore, Seven Reforms to Balance the Budget, Cato Policy Report (Cato Inst., Washington, D.C.), July-August 1996, http://www.cato.org/pubs/policy_report/v18n4-1.html ("Most members of [the House Committee on Government Reform and Oversight] are keenly aware of the need for a balanced-budget requirement, so I will not dwell on it."); cf. Robert Eisner, Sense and Nonsense About Budget Deficits, Harv. Bus. Rev., May-June 1993, at 99, 99 ("Almost everybody talks about federal budget deficits. Almost everybody is against them in principle. And almost no one knows what he or she is talking about.").} Indeed, even in the face of a weakening economy and the threat of a double-dip recession, Presi-

\footnote{It is also notable that the volume edited by Rivlin and Sawhill, note 1, is titled "Restoring Fiscal Sanity: How to Balance the Budget," thus equating sanity with budget balancing—even though the executive summary of the volume concedes that "[n]ot all budget deficits are harmful." Id. at 1. Moreover, the final chapter of that volume, Henry J. Aaron, William G. Gale & Peter R. Orszag, Meeting the Revenue Challenge, id. at 111, states that "[i]t is my chapter is a guide to revenue options that would help balance the budget," id., making the notion of budget balance the norm against which policies are measured. Of course, the Republican Contract With America also famously committed the then-minority party to a balanced federal budget through a constitutional amendment. U.S. House of Representatives, http://www.house.gov/house/Contract/CONTRACT.html (proposing a balanced budget amendment to restore fiscal responsibility) (last visited Sept. 21, 2005).}

Regarding the less common suggestion of paying down the federal debt entirely, see Executive Office of the President of the United States, A Blueprint for New Beginnings: A Responsible Budget for America's Priorities 27-32 (2001), available at http://www.whitehouse.gov/news/usbudget/blueprint/budtoc.html (identifying as the first "Major Policy Initiative" of the new presidential administration "Pay[ing] Down the Government Debt" and arguing that "the President achieves 'maximum possible debt retirement' in his budget" and that "the Administration's Budget shows that it is possible to effectively pay off the debt"); see also Press Release, Office of Sen. Enzi, Enzi, Allard Push National Debt Repayment Bill (Apr. 5, 2000), http://enzi.senate.gov/enziall.htm (quoting an announcement by U.S. Senator Mike Enzi in which he stated, "I am pleased to join my friend from Colorado, Senator Allard, in sponsoring the 'American Social Security Protection and Debt Repayment Act.' This legislation will keep our budget balanced, protect all the Social Security surplus by preventing these revenues from being used for additional spending, and establish a concrete schedule for Congress to pay off the publicly-held debt.").

When there is no deficit, of course, the political environment changes. See, e.g., Richard W. Stevenson, Budget Deficit Is Said to Be $139 Billion, N.Y. Times, Oct. 25, 2002, at A24 ("The return to red ink brought an end to a four-year period in which surpluses and the
dent George W. Bush decided to show his economic seriousness during his August 2002 economic summit in Waco, Texas by announcing that he would refuse to spend $5.1 billion that Congress had approved for domestic security and the military. \(^6\) Explaining the decision, he declared: "More money spent in Washington means less money in the hands of American families and entrepreneurs, less money in the hands of risk takers and job creators." \(^7\)

Setting aside President Bush’s implication that government spending is presumptively harmful to the economy, the more immediate question is why we should be so concerned about an annual shortfall of revenues to cover expenditures. Why not measure the government’s cash flows quarterly, monthly, or weekly? Or, for that matter, why not instead evaluate the public sector’s fiscal health biannually or under five-year plans? Annual accounting is not necessarily worse than any of those alternatives, but it is not obviously better either.

If it were simply a matter of choosing among arbitrary accounting periods, then it certainly might be possible that annual accounting would emerge as a reasonable choice. On the other hand, it might be better to explore ways to measure government finances not based on an arbitrary accounting period but rather to determine whether the government can pay for its totality of commitments, both short-term and long-term.

In the case of individual projects, such as building a bridge, familiar accounting methods can be used to determine whether the dedicated funds to pay for the project will cover expenses plus interest. In the case of projects that have no known or planned completion date, the challenge is to determine whether the permanent funding for a project can cover its projected outlays. Social Security is a perfect example of this type of project because it has a dedicated source of financing and is set to continue forever. I explore this in detail in Section IV.

The majority of government activities, however, are not so easy to isolate. The FBI, for example, has no dedicated source of financing, so it is not meaningful to ask whether the FBI is "in balance" in an accounting sense. The defense budget, the Centers for Disease Con-

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\(^7\) Hulse, note 6, at A19 (quoting President George W. Bush).
trol, and so on are all simply part of an aggregated total of government expenditure. Measuring their individual long-term financial viability is neither possible nor meaningful.

B. Long-Term Fiscal Measurement

This suggests that we should look at the government as a whole and determine whether, in total, its expected tax revenues can finance its commitments. This sidesteps both the question of setting an arbitrary accounting period and of looking only at those items that happen to have been created with a nominally separate financing mechanism. The goal then becomes measuring whether there is a mismatch between the government’s aggregate long-term spending commitments and its aggregate long-term revenue streams. In other words, we would like to have an analogue to the notion of a cash-flow periodic deficit that captures all current and future activities of a government.

1. The Fiscal Gap and Generational Accounting

One attempt to build such a long-term analytical model is called “generational accounting.”

8 Responding to the political focus on annual cash-flow deficits, in the early 1990’s the economist Laurence Kotlikoff and his frequent co-authors, Alan J. Auerbach and Jagadeesh Gokhale, developed a theory that was motivated by concerns about the long-term effects of federal fiscal commitments. 9

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9 See, e.g., Auerbach et al., Meaningful Alternative, note 8; Auerbach et al., Generational Accounting, note 8.
portantly, moreover, they attempted not only to determine whether current projections of fiscal flows will balance, but also to determine whether the government's treatment of different generations of its citizens was, in some meaningful way, fair.\textsuperscript{10}

An initial note of caution is, however, in order. Whatever its analytical merits and shortcomings (discussed in some detail below), the generational accounting approach would put an even greater constraint on legal analysts or anyone else who might propose a change in public policy. No longer would it be enough to prove that a policy would not increase the current deficit; Kotlikoff and his co-authors offer opponents of government activism an even more powerful trump card. Their approach requires not merely that there be enough money to pay for the program today, but it also requires that the program be "affordable" into the indefinite future, as measured by long-range budget forecasts.

Adding a political (and somewhat emotional) slant to the discussion, these analysts further suggest that anything that is not affordable in this way is a transfer to the (voting) living generations from the (politically defenseless) unborn generations.\textsuperscript{11} If this approach is well-founded, of course, then the political implications should not be ignored merely because they might be unwelcome or inconvenient; but it raises the stakes in the analysis of this alternative method of measuring fiscal policy.

The basic notion behind generational accounting is quite simple (though such conceptual simplicity makes the intractable measurement problems discussed below all the more frustrating). If current spending and tax laws were to stay in effect in perpetuity, the flows of expenditures and revenues would vary depending on future economic growth, population changes, weather patterns, medical developments, and the like. To measure the infinite-future fiscal gap, one must make assumptions about the directions and magnitudes of the most important of those future trends and apply the accounting concept of net present value to discount all of those projected future expenditures and revenues into current dollar terms. The resulting estimate, the fiscal gap, tells us how much money the government would have to borrow today in order to pay for all of its future deficits in a lump sum.

\textsuperscript{10} Auerbach et al., Generational Accounting, note 8, at 82 ("Our purpose here is to... see how generational accounting can be used to design policies that can achieve an equitable intergenerational distribution of the burden of paying for the government's bills.") (emphasis added).

\textsuperscript{11} See, e.g., Kotlikoff, Deficit Delusion, note 8, at 105 ("[T]he financial sacrifice [of today's adults] will provide the means to keep tax rates on our children and grandchildren from soaring. It's high time we started focusing on the size of the tax bill facing our kids.").
Generational accounting takes this one important step further. Starting with the fiscal gap measure, generational accounting provides estimates of the lifetime net tax rates for different generations implied by current fiscal policies. Each generational cohort’s lifetime government-provided benefits are subtracted from its net taxes and divided by income. Hence, Kotlikoff and his co-authors claim that generational accounting provides a way to measure whether current generations are being “fair” to those that will follow.\footnote{See Auerbach et al., Generational Accounting, note 8, at 82. While the authors go on to disclaim any particular ethical stance, id. at 84 (“Generational equity is an ethical concern, and our choice of any particular norm for purposes of illustration is not meant to impose this norm as our preferred ethical judgment.”), Kotlikoff’s separate writings at least strongly imply an endorsement of intergenerational equity as the preferred policy norm, see Kotlikoff, Deficit Delusion, note 8, at 105 (describing high tax rates on future generations as “disturbing”); Kotlikoff, Reply, note 8, at 308 (arguing that politicians’ failure to account for the retirement of the baby boom “guarantee[s] us and our children nothing short of a fiscal disaster”).}

\section{The Current State of the Literature and Policy Debates}

Although Tax Notes—the periodical of record for tax practitioners, policymakers, and academics—has carried at least eight articles that in some way deal with generational accounting since 1991,\footnote{Karen C. Burke, VATs and Flat Taxes Reconsidered, 70 Tax Notes 899, 902 (Feb. 12, 1996) (arguing that “a consumption tax might be viewed as stimulating total savings and providing a meaningful alternative to current deficit policies,” which “shift the net burden of financing governmental expenditures away from older generations and toward younger and future generations”); Richard Goode & C. Eugene Steuerle, Generational Accounts and Fiscal Policy, 65 Tax Notes 1027 (Nov. 21, 1994) (advocating for the use of generational accounting and related measures in evaluating generational equity on a program-specific basis); J. Andrew Hoerner, NBER Conferes Discuss IRAs, Integration, Corporate Tax Shifts, 53 Tax Notes 878, 881 (Nov. 25, 1991) (discussing Auerbach’s concerns regarding intergenerational tax inequity); Barbara Kirchmeier, Generational Accounting: Are We Soaking the Young?, 62 Tax Notes 945 (Feb. 21, 1994) (providing an overview of the generational accounting model and literature); Sheldon D. Pollack, Professor Supports “PAYGO” to Restrain Worst Impulses of Both Parties, 82 Tax Notes 1035 (Feb. 15, 1999) (discussing the redistributive effect that the Social Security shortfall will have on future generations); Daniel Shaviro, Understanding the Generational Challenge, 75 Tax Notes 714 (May 5, 1997) [hereinafter Generational Challenge] (evaluating political approaches to Social Security and Medicare reform from the perspective of generational policy); Alan D. Viard, The Social Security Surplus, the Trust Fund, and the Federal Budget, 94 Tax Notes 891 (Feb. 18, 2002) (arguing that in order to avoid imposing a major fiscal burden on future generations, it is necessary to balance the budget and increase the Social Security surplus); David M. Cutler, Book Review, 60 Tax Notes 361 (July 19, 1993) (reviewing Kotlikoff, Generational Accounting, note 8).} the theory was first introduced, the appearances of generational accounting in the general legal literature have not been extensive.\footnote{A Lexis search of all law reviews turned up 25 citations to articles discussing “generational accounting.” Reuven S. Avi-Yonah, Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State, 113 Harv. L. Rev. 1573 (2000); Evelyn Brody, Charitable Endowments and the Democratization of Dynasty, 39 Ariz. L. Rev. 873 (1997) [hereinafter Charitable Endowments].} The ex-
ception is commentary by Daniel Shaviro, who has written extensively in support of the argument that the fiscal gap/generational accounting approach should be imported into legal analyses of Social Security policy and Medicare policy—and more generally into all legal analyses of fiscal policy.\textsuperscript{15} Finding that there is a long-term fiscal imbalance that makes "the current policy . . . fiscally unsustainable,"\textsuperscript{16} Shaviro asserts that it is necessary to think about these issues through the lens

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\textsuperscript{16} Shaviro, Generational Challenge, note 13, at 715.
of fiscal gap/generational accounting—\textsuperscript{17} and such an analysis, he argues, shows a grim future indeed.\textsuperscript{18}

The stakes in this debate, therefore, could hardly be higher. Anyone who wishes to write about Medicare or Social Security, and indeed anyone who might ever wish to suggest that the government should spend money on any project, plausibly might be forced to contend with the implications of fiscal gap/generational accounting.

If fiscal gap/generational accounting lived up to its billing, of course, it simply would be good policy to use it as a starting point for fiscal analysis. Unfortunately, it is not a neutral analytical tool and cannot be used dispassionately to assess the fiscal consequences of a government project, even by those who begin their analysis without a political agenda. Instead, fiscal gap/generational accounting is based on highly contestable assumptions, arbitrary analytical choices, and manipulable policy projections that fatally compromise most of its analytical value. Understanding the promise and limitations of fiscal gap/generational accounting is essential for anyone who wishes to understand the current debate over government spending and taxation.

The debate, therefore, is not over whether the future matters; that is, this is not a debate between the grasshoppers and the ants. Clearly, we always must think carefully about the future consequences of our fiscal policies. The question is \textit{how} to think about the future—what we would like to bequeath to future generations and how best to deliver it.

\textbf{D. The Imperfect vs. the Fundamentally Flawed}

Because this is an attempt to peer into the future, \textit{any} measure of the effects of fiscal policy will be imperfect. The alternatives to fiscal gap/generational accounting-style measures are, therefore, also imperfect. Choosing among these imperfect measures is not easy. Given the available options, however, I argue that we should choose tradi-

\textsuperscript{17} Id. at 716 ("Perhaps the best tool for enhancing our understanding of who wins and loses from alternative reforms is \textit{generational accounting} . . . ."). Shaviro, however, is not explicitly wedded to fiscal gap/generational accounting to the exclusion of all else. Instead, he suggests that we should use fiscal gap/generational accounting as well as other theories to learn as much as we can from a variety of approaches. See id. (stating that while generational accounting "does not suggest unique answers to the question of how to reform social security and Medicare" or "address philosophical disputes about the proper size of government or level of progressive redistribution," it "improve[s] our ability to measure the extent to which fiscal burdens are being shared equitably").

\textsuperscript{18} Recently, Shaviro has endorsed more enthusiastically the fiscal gap measure of long-term fiscal balance and has not emphasized explicit generational accounting approaches. See, e.g., Daniel N. Shaviro, Reckless Disregard: The Bush Administration's Policy of Cutting Taxes in the Face of an Enormous Fiscal Gap, 45 B.C. L. Rev. 1285 (2004) [hereinafter Reckless Disregard].
tional deficit measures over the fundamentally flawed fiscal gap/generational accounting-based measures.

Traditional measures of the deficit can be perfected to some degree, and many official forecasts have extended the accounting period to a standard 10-year window.\(^{19}\) Acknowledging that there is always some value in learning what we can from a variety of approaches to analyzing fiscal policy, I nevertheless conclude that fiscal gap and generational accounting are too often empty or even misleading measures of future fiscal developments.

### III. **Traditional Fiscal Deficit Measures**

Even the most casual observer of U.S. political debates cannot have missed the fact that politicians are obsessed with "the deficit." After decades in which Republicans regularly attacked Democrats for their spendthrift ways,\(^{20}\) Democrats turned the tables in the 1980's,\(^{21}\) as Ronald Reagan presided over the largest nominal peacetime deficits in American history.\(^{22}\) Undaunted, conservative Republicans insisted that they were the truly responsible fiscal custodians, culminating in the promise to balance the budget in 1994's Contract with America.\(^{23}\)

Capitulating to the political heat generated by this headline-grabbing issue, President Clinton announced in 1995 that he, too, was committed to balancing the budget.\(^{24}\) When the budget moved from deficit to surplus under his watch,\(^{25}\) Clinton never missed an opportu-


\(^{21}\) See, e.g., Susan F. Rasky, Economic Expansion Seen for '87, N.Y. Times, Jan. 5, 1987, at D1 (noting Democrats' desire to brand the deficits as Reagan's work).


\(^{23}\) Republican Contract With America, note 5.

\(^{24}\) See Todd S. Purdum, President Offers Plan to Balance Federal Budget, N.Y. Times, June 14, 1995, at A1. Indeed, Clinton's pre-1994 actions showed that he was strongly predisposed to the balanced-budget mantra, as he immediately jettisoned his proposals for long-term capital spending and instead pushed through a major tax increase. Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, 107 Stat. 312. (For those who approve of tax progressivity, however, one at least can note that Clinton's tax bill was top-loaded.) Id. § 13202, 107 Stat. 312.

\(^{25}\) Congressional Budget Office, Historical Budget Data, tbl.12, http://www.cbo.gov/showdoc.cfm?index=1821&sequence=0#table12 (last visited Sept. 22, 2005) (showing that budget was in deficit until 1997 and then surplus beginning in 1998). Those surpluses, of course, only lasted a few years. See Richard W. Stevenson, Budget Deficit Is Said to Be $159 Billion, N.Y. Times, Oct. 25, 2002, at A24 ("[T]he federal budget deficit for the year that ended Sept. 30 was $159 billion, a sharp swing from the surplus of $127 billion in the previous year.").
nity to take credit for this "achievement." With their own party's leadership having abandoned them, even the most progressive members of the Democratic Party became committed budget balancers. Senator Russell Feingold, for example, eagerly pointed out that he opposed President Clinton's proposed middle-class tax cut in the early 1990's, declaring that he "was for deficit reduction." Writing in 1998, Nancy Staudt reasonably could conclude that, even if one believed in the importance of budget balance, it might have become unnecessary to pass a constitutional balanced-budget amendment, because the political controversy over federal budgeting may have caused politicians to commit themselves to that goal for political reasons.

The politics of fiscal deficits, however, can change rapidly. As recently as the late autumn of 2002, it seemed that there were no longer any major voices in American politics arguing in favor of deficit spending. As 2002 turned to 2003, though, the fiscal ink turned red again, and a new consensus arose that the return to short-run deficits was not a serious problem—but that long-term deficits represent a virtual "cancer" eating away at future prosperity. During the 2004 presidential campaign, finger-pointing about the deficit again rose to a fevered pitch. The tentative consensus emerging from the presidential campaign was that cutting the deficit in half within five years was the best available policy, with the only disagreement being which candi-

28 Staudt, note 4, at 1174 ("[T]he debate over the balanced budget amendment may have produced a substantial shift in fiscal norms which, in turn, has enabled Congress and the Executive to reduce the size of the budget in the statutory context. If the legislators continue with this more restrained budgetary process, the argument for a balanced budget amendment dissolves.").
29 There were, of course, some outside of the mainstream who opposed the orthodoxy, not all of whom were at the liberal end of the spectrum. Former Congressman Jack Kemp, for example, was once the most prominent political advocate of so-called supply side economics, which holds that low tax rates are much more important than balanced budgets in generating high economic growth rates. See generally Jack Kemp, An American Renaissance: A Strategy for the 1980s (1979); see also Edmund L. Andrews, A Pragmatist at Treasury, N.Y. Times, Dec. 10, 2002, at A1 (discussing supply-side Republicans, noting that "Jack Kemp [is] a former cabinet secretary and an ardent advocate of tax cuts," and quoting Stephen Moore, another supply-sider, who criticized a likely nominee for White House economic advisor as being "hypersensitive about budget deficits").
date could meet that goal.\textsuperscript{31} In the aftermath of the election, the administration's budget proposals appear unlikely to reduce the annual deficit even by that much.\textsuperscript{32}

To some degree, this political obsession with annual deficits is quite surprising because the economic arguments in favor of deficit spending in various circumstances are well known and, to a large extent, uncontroversial among fiscal economists.\textsuperscript{33} While it is certainly possible to argue that, in spite of the economic case in favor of deficits in some circumstances, there is a colorable political case against them,\textsuperscript{34} it is at least worth remembering what the economic issues are.

In addition, the discussion below highlights measurement problems that could be changed relatively easily to the benefit of public debate. Without even reaching the question of fiscal gap/generational accounting versus traditional deficit measures, some relatively noncontroversial adjustments to measurements and rhetoric could improve analytical clarity.

\section{A. Preliminary Problems}

Economists differentiate between stock variables and flow variables. The difference between the two has to do with the passage of time. Stock variables can be measured at a moment in time, while flow variables are only meaningful per unit of time. Thus, distance is a stock variable, while speed (miles per hour, for example) is a flow variable. In economics, common stock/flow distinctions include prices (stock) versus inflation (flow) and wealth (stock) versus income (flow).\textsuperscript{35}

\begin{footnotesize}
\begin{enumerate}
\item Dustin Stamper, GOP Criticized as OMB Misses Midyear Budget Review Deadline, 2004 TNT 137-3, July 16, 2004, available in LEXIS, TNT File ("According to [Office of Management and Budget spokesman Chad] Kolton, Bush has offered the only credible plan to cut the deficit in half over the next five years. Presumptive Democratic presidential nominee Sen. John F. Kerry of Massachusetts has pledged to equal that feat if he is elected, but each side has taken issue with the other's numbers.").
\item Edmund L. Andrews, Trim Deficit? Only if Bush Uses Magic, N.Y. Times, Feb. 7, 2005, at C1 (describing President Bush's budget proposals and reporting that his spending cuts will not significantly reduce the deficit).
\item Id. at 221 (arguing that "the budget deficit is now putting a burden on America's future [. . . ] Washington's perpetual preoccupation with the budget deficit is making a mockery of federal budgeting."), and id. at 222 (In the current fiscal environment, Congress will not invest in projects with high current costs but high rates of return in the long term because of the impact on budget calculations).
\item See, e.g., Andrew B. Abel & Ben S. Bernanke, Macroeconomics 43 (5th ed. 2005).
\end{enumerate}
\end{footnotesize}
1. Debt and Deficits

In government accounting, debt is a stock variable, because it measures the total amount of money at any given moment that a government owes its creditors. The deficit is a flow variable, measuring the net amount of new borrowing that the government has engaged in during the course of a year (or any other unit of time). Deficits are, properly measured, the change in debt as time passes.\textsuperscript{36}

Importantly, the total amount of federal government debt that exists at a given moment is also tautologically equal to the total number of dollars of Treasury securities in circulation at any moment. Since the federal government borrows money by selling Treasury securities, the face value of those outstanding securities is equal to the national debt.

Here, however, is one of the first instances where reality and theory diverge. The different agencies of the federal government often hold each other’s debt instruments, so the net federal debt is lower than the number of bonds that have been issued but not redeemed. The difference is not trivial. While the infamous “National Debt Clock” on display in several major cities (the ever-rising digital readout of the nation’s supposed indebtedness, expressed both in the aggregate and as each citizen’s share) showed an outstanding federal debt of almost $8 trillion in April 2004,\textsuperscript{37} just over $4.5 trillion of that total was held outside of the federal government’s own offices.\textsuperscript{38} This was why the National Debt Clock did not initially decline when the federal government ran surpluses in the late 20th century. Even though the government was extinguishing debt held by the public, the total number of bonds in existence was not going down, so “the national debt”—by that meaningless measure—was not shrinking.

2. Dollars vs. Percentages

The common practice of expressing debt and deficits in total dollars rather than as percentages of national income also can be highly misleading. Politicians in the late 1980’s talked of “$200 billion deficits as

\textsuperscript{36} Id. at 580.

\textsuperscript{37} U.S. National Debt Clock, http://www.brillig.com/debt_clock/ (last visited Sept. 22, 2005). To be directly comparable with the most recent numbers for publicly held debt, see note 38, the national debt clock’s value on March 31, 2005 should be used. The government site from which the privately-run national debt clock’s numbers are drawn, http://www.publicdebt.treas.gov/opd/opdpenny.htm, indicates that the “debt to the penny” on that date was just under $7.8 trillion, specifically $7,776,939,047,670.14.

far as the eye can see" as if that was an unimaginable calamity.\textsuperscript{39} In fact, given that nominal GDP doubles roughly every 12 years, $200 billion annual deficits would be trivial in relatively short order.\textsuperscript{40} Referring to deficits in nominal dollar terms makes deficits in later years look larger than they really are, making references to "record-setting" deficits an empty description.\textsuperscript{41}

In the United States, deficits as a percentage of GDP peaked in 1983 at roughly 6\%,\textsuperscript{42} and the publicly-held debt peaked in 1993 at just under 50\% of GDP.\textsuperscript{43} This was, of course, only the recent peak and was not even close to the levels in excess of 100\% that it reached at the end of World War II,\textsuperscript{44} when the United States wisely spent enormous sums of borrowed money to finance the war against the Axis powers. This ratio had steadily fallen to the point where it was below 30\% from 1969-82 (bottoming out at 23.9\% in 1974), and then rose to peak at 49.4\% in 1993 before falling again through 2001 to 33\% before picking up again over the last few years to 37.2\% in

\textsuperscript{39} See, e.g., Peter T. Kilborn, 3 Who Have Been Chosen to Play Major Roles in the Bush Administration, N.Y. Times, Nov. 22, 1988, at A19 (referring to famous phrasing by David Stockman, former budget director to President Ronald Reagan). This phrasing occasionally is still used. See, e.g., Editorial, Painting the Economy Into a Corner, N.Y. Times, Aug. 12, 2004, at A24 ("Did someone say, 'Deficits as far as the eye can see'?"); Alan B. Krueger, Economic Scene: It Looks Like Red Ink and the Ills That Can Go With It Are Back to Stay for a While, N.Y. Times, Mar. 6, 2003, at C2 ("[T]he red ink is expected to last as far as the eye can see.")

\textsuperscript{40} In the first quarter of 1984, for example, U.S. GDP was $3.8 trillion, meaning that a $200 billion deficit was equal to more than 5.25\% of GDP. Bureau of Economic Analysis, Current-dollar and "Real" Gross Domestic Product (2005), http://www.bea.doc.gov/bea/dn/gdplev.xls (showing GDP in first quarter of 1984 of $3,809.6 billion). Twenty years later, with GDP in the first quarter of 2004 nearing $11.5 trillion, id., a $200 billion deficit would be under 1.75\% of GDP.

\textsuperscript{41} See, e.g., Stamper, note 31 ("House Budget Committee ranking minority member John M. Spratt Jr., D-S.C. . . . said even the new deficit figure, which Democrats estimate to be in excess of $425 billion, is record-setting."); see also Louis Uchitelle, It's the Economy, Right? Guess Again, N.Y. Times, July 4, 2004, § 3, at 1 (describing plans "to cut the budget deficit in half . . . from its projected record level of more than $450 billion in the current fiscal year"). Even if the deficit had been $450 billion in 2004, this would have been roughly 3.9\% of GDP—not even close to the post-World War II record of 6\% in 1983, and tied only for the eighth largest deficit in the last 25 years. See Congressional Budget Office, Historical Budget Data (2005), note 25 at tbl.11 (showing GDP in 2004 of $11.553 trillion); id. at tbl.2 (showing 1983 deficit of 6\% of GDP, and showing deficits as a percentage of GDP greater than 3.9\% in 1982-86 and 1991-92, and deficits equal to 3.9\% of GDP in 1990 and 1993). The actual deficit in 2004 was not $450 billion but rather $412 billion, or 3.6\% of GDP. Id. at tbl.12, tbl.2.

\textsuperscript{42} See note 41.

\textsuperscript{43} Congressional Budget Office, Historical Budget Data (2005), note 25, at tbl.2.

\textsuperscript{44} Abel & Bernanke, note 35, at 581 ("By the end of the war, the debt-GDP ratio exceeded 100\% "); see also Council of Economic Advisors, Executive Office of the President of the United States, Annual Report of the Council of Economic Advisors 304, tbl.B-79 (2005) (showing federal debt held by the public at 106.2\% of GDP at the end of 1945 and peaking at 108.6\% at the end of 1946).
2004.\textsuperscript{45} The level of deficit spending is projected to produce a deficit of 2.7\% of GDP in 2005 ($331 billion), with the federal debt at 37.7\% ($4,621 billion).\textsuperscript{46}

Presenting debt and deficit figures in dollars rather than percentages can cause confusion because it ignores the ability of a larger economy to handle larger amounts of debt and borrowing. By comparison, private lenders loan money to individuals only after determining that the potential borrowers' incomes are large enough to allow them to pay back their loans. No bank would say, “I can’t lend you $500,000, because that’s a large amount of money;” but any reasonably well-run bank would say, “I can’t lend you $500,000, because you only make $23,000 per year.” Analogously, it would be odd indeed if government spokesmen started to focus on the total number of unemployed rather than the unemployment rate, because that would not allow meaningful comparisons to previous years (when the population was lower) or to other countries (where the population might be much higher or much lower than in the United States). Seen in that light, our political focus on raw debt and deficit numbers makes no sense, and it invites the political posturing and meaningless comparisons noted above.\textsuperscript{47}

3. Federal vs. State and Local

A third measurement issue carries more direct implications for policy debates. Typically, commentators separate the federal debt and deficit from state and local fiscal positions. Since the state and local sector tended until very recently to run aggregate operating surpluses, the decision to exclude the state and local sector when discussing the “government” deficit and debt naturally made the situation look worse. On the other hand, federal measures of borrowing ignore the current situation of chronic state deficits. Foreign economists view this practice as nothing less than bizarre, because the macroeconomic consequences of debt and deficits surely do not depend on the hierarchical level of the government entity that is borrowing.\textsuperscript{48}

\textsuperscript{45} Congressional Budget Office, Historical Budget Data (2005), note 25, at tbl.2.
\textsuperscript{47} See note 41.
In the United States the public discussion of fiscal policy concentrates almost exclusively on the operations of the federal government. Yet state and local governments account for about a third of all public expenditure and taxes; moreover, their budgets are generally in surplus so that these authorities are
In addition to being logically incoherent, this practice has perverse policy effects as well. When national politicians view their job as reducing the federal deficit or debt, they are tempted either to ignore the consequences of their decisions on lower levels of government or even deliberately to shift spending obligations downward.\textsuperscript{49} Indeed, this seems to be a primary explanation for the fiscal crisis in the states over the last few years.

\section*{B. Cash-Flow Deficit Measures}

While these issues have important implications for discussing the status of fiscal policy in the United States, the discussion that follows attempts to follow the current norms in describing deficit measures. Even within the federal-only measures, however, there are significant disagreements about what is the true measure of fiscal policy.

\subsection*{1. On Budget and off Budget}

Even if one looks only at the federal government, the annual deficit is more manipulable than it might seem. A spending program can exist in a netherworld outside of the official budget simply by act of Congress. There need be no economic rationale for the decision. The 1991 Gulf War was carried off budget, for example.\textsuperscript{50} By far the biggest off-budget item, of course, is the Social Security system. The current surplus in that system (approximately $173 billion in 2005, or 1.4\% of GDP) makes the total deficit smaller than the on-budget deficit ($507 billion, or 4.1\% of GDP), but when Social Security starts to run deficits after the next decade or so, the on-budget deficit will be smaller than the total deficit.\textsuperscript{51}

The debate about whether the Social Security Trust Fund has any meaning is an important factor in determining whether the on-budget


\textsuperscript{50} Congressional Budget Office, Emergency Spending Under the Budget Enforcement Act (1998), available at http://www.cbo.gov/showdoc.cfm?index=1050&sequence=0; see also Auerbach et al., Generational Accounting, note 8, at 73-74 ("The CBO also offered \ldots a $292 billion deficit in 1992 that excluded the net payments received to help finance Operation Desert Storm as well as those made to bolster the nation's deposit insurance system.").

\textsuperscript{51} All estimates in this paragraph are from Congressional Budget Office, note 46. As the data discussed in Section IV indicate, however, these estimates are subject to revision. The contingent nature of the estimates should be borne in mind throughout this analysis.}
or total deficit is the proper measure. Because I conclude that the total deficit is the better of the two, in that it measures the amount of money that the federal government is draining from the financial markets in a given year, I focus on that measure of the deficit and possible ways to improve it.\textsuperscript{52}

A fuller discussion of Social Security's financing and long-term prospects appears in Section IV.

2. \textit{Cyclical Adjustment}

For macroeconomists, one of the most important measurement issues in deficit accounting is adjustment of the deficit for changes in the health of the economy.\textsuperscript{53} When the business cycle turns, tax receipts and government expenditures naturally change along with the GDP. Recessions bring lower revenues and higher expenditures, and boom times do the opposite. When comparing deficits at two points in time, therefore, it is important to ask, "What would the deficit be today if the economy were fully healthy?"

What it means to be "fully healthy" is a matter of contention. Nevertheless, there is a widely accepted measure of the cyclically-adjusted deficit known as the standardized-budget deficit, computed by determining the flows of revenues and expenditures if the unemployment rate were at its trend rate.\textsuperscript{54} In 2003, because of the lingering effects of the recession, the unadjusted total deficit was $375 billion (3.4\% of GDP), while the standardized-budget deficit was $313 billion (2.8\% of GDP).\textsuperscript{55}

Failing to adjust the deficit for cyclical effects is likely to lead to policy errors. First, it confuses cause and effect. Improvements in the economy decrease the nonadjusted deficit, but decreases in the cyclically-adjusted deficit (all else constant) cause the economy to decline. This causes perverse policy moves, as a worsening economy causes the deficit to rise, such that policymakers who attempt to reduce the defi-

\textsuperscript{52} For a persuasive argument that the Social Security system should be seen not as an individualized benefit plan, but rather as a redistributive fiscal program, see Deborah A. Geier, Integrating the Federal Tax Burden on Labor Income, 98 Tax Notes 563, 574-75 (Jan. 27, 2003).

\textsuperscript{53} See e.g., Blinder, note 33, at 217 ("[I]t is important to look at the \textit{cyclically adjusted} deficit, which is unaffected by changes in income.") (emphasis in original).

\textsuperscript{54} Congressional Budget Office, The Budget and Economic Outlook: Fiscal Years 2006 to 2015, Glossary (2005), available at http://www.cbo.gov/showdoc.cfm?index=6060&sequence=13 ("standardized-budget deficit or surplus: The level of the federal budget deficit or surplus that would occur under current law if the economy operated at potential GDP.").

cit with further cuts in spending (and perhaps increases in taxes) will only further weaken the economy. President Bush’s symbolic refusal to spend money that Congress had allocated, noted above, clearly demonstrates this perversity.56

This failure to comprehend simple macroeconomics is not confined to the United States. The Japanese economy went into its first of several severe downturns in 1989.57 By 1996, with the domestic economy still in deep trouble, Japanese policymakers relied on more budget cutting and tax increases to improve the economy—58—the macroeconomic equivalent of “bleeding” a patient to restore her to health. Yet, policymakers there reflexively proposed a return to budget balancing in response to the economy’s troubles.59 Now “many economists believe Japan’s long stagnation in the 1990’s largely reflected timid policymakers unwilling to boldly use the levers of fiscal and monetary policy.”60

The practical consequences of failing to adjust for the business cycle are especially severe for state and local governments, most of which operate under (modified) balanced budget requirements.61 When the economy is strong (which means that, by definition, workers are scarce because their prospects are so good in the private sector), states flush with money compete with prosperous companies for workers and other economic resources. Roads are torn up and rebuilt precisely when the disruption from such projects is the most damaging, as the overburdened highways are filled with vehicles carrying the evidence of economic prosperity. Then, when the economy weakens, states see their tax revenues decline, lay off workers, and leave highways in disrepair. It would be difficult to design a more perverse system.62

56 See notes 6-7 and accompanying text.
57 What Caused Japan’s Recession?, BBC News, Aug. 14, 2002, available at http://news.bbc.co.uk/1/hi/business/2193853.stm (“Japan has been suffering stagnant economic growth and a series of recessions for more than 10 years...Japan is still suffering from an economic crisis that hit the country in 1989-90.”).
59 Floyd Norris, Japan’s Budget Deficit Has Soared. It’s Time for a Tax Cut, N.Y. Times, Aug. 18, 2001, § C, at 1 (“The previous spending sent Japan’s debt soaring, leading [Japanese Prime Minister] Koizumi to run on a budget-balancing platform...He needs a way out of that promise without having to admit that he is breaking it.”).
60 Christopher Farrell, Capitalism’s Savior, Bus. Week, Apr. 12, 2004, at 20.
62 This is not to say that highways are the be-all and end-all of economic spending. In this analysis, they are simply the most intuitive example of public spending on infrastructure.
3. **Unfunded Liabilities**

The closest one comes in the traditional deficit debates to the central issues of long-term budgeting (that are the focus of the fiscal gap/generational accounting approach described below) is the discussion of unfunded liabilities. The basic idea is that government projects that involve spending in the future can be thought of as liabilities that must be accounted for when looking forward. This sensible observation, though, can be useful only inasmuch as projects have dedicated financing. If a high school is built with proceeds from a bond sale, for example, the liability is funded if the school district commits the funds in future budgets to cover the bond payments. Otherwise, the project is unfunded. Since most government programs are not financed through dedicated funds, most projects are unfunded liabilities. The Interior Department, the Army Corps of Engineers, and the like are all unfunded, and they almost certainly will continue to be so for as long as they last.

Estimates of unfunded liabilities are highly responsive to changes in the law. The change in withholding taxes in 1983, for example, caused the largest change ever in the long-range actuarial balance of the system. Fiscal gap/generational accounting is arguably an improvement on the arbitrary nature of these estimates, as I discuss below, but its other shortcomings ultimately make it an unappealing alternative.

4. **Extended Budget Projections**

All of the cash-flow budget measures discussed above are calculated in annual terms. It is possible, of course, to use a different arbitrary time period in such an analysis. During the Clinton Administration, it became common to provide 10-year projections of budgets, to allow policymakers to look into the relatively foreseeable future and determine whether a budget or tax measure was likely to become more or less manageable over time. The current Bush Administration some-

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64 See text accompanying notes 101-02.

times has issued five-year projections rather than 10-year projections, a move that has generated suspicion that the full costs of their policy proposals are "back-loaded." It is, of course, possible to back-load even on a 10-year horizon. It is also possible to play games for different political purposes, such as the Bush Administration's proposal to "encourage savers to move money from one type of individual retirement account to another, thus increasing tax receipts by $14.6 billion over the next four years—the period over which the president promises to reduce the deficit—while costing the government twice as much money in the following six years."

The arbitrary nature of these cutoffs is, as discussed in the next Section, a strong argument in favor of adopting an infinite-horizon model along the lines of the fiscal gap/generational accounting approach. Nevertheless, because of the critical problems in lengthening the time horizon, the 10-year projections are probably the best compromise available. I take up this point further below.

C. Effects on Consumption and Investment

The payoff for making these adjustments to the measurement of the fiscal deficit comes in analyzing the effects of current deficits on the use of society's productive resources (labor, machinery, factories, land, and the like). If the government hires resources to build or produce goods and services, and if those resources would have been used to produce something of value to private citizens, then the government has "crowded out" private activity. If the government crowds out private consumption, then there is at worst no effect on future generations, because private consumption would not have benefited future generations in any case. In such a situation, the government can make future generations better off if it replaces private consump-

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The FY06 budget proposals reflect 'back-loaded' tax cuts that provide illusory revenue increases in the short term. In particular, the administration confines its budget projections to the next five years and estimates that new proposals for savings subsidies will bring revenue gains of $14 billion over that period. Those gains are more than wiped out in the subsequent five years, yielding a net loss of $15 billion for the entire 10-year period.

tion with public investment, or it can simply substitute one kind of consumption for another—leaving future generations unaffected.

The more serious concern is that the government will crowd out private investment rather than private consumption. Wasting government money that would have gone toward private investment in productive equipment, for example, compromises the future standard of living of the country. In fact, even if the government invests resources in productive assets, it still can make matters worse if the assets it crowds out would have been more productive than the government’s investment projects. What is often forgotten, however, is the other possibility—that the government might crowd out a private investment project with a public investment project that is even more productive. Rather than building a strip mall, for example, the government might use resources to build a children’s hospital.\textsuperscript{69}

While there is no precise way to know the exact nature of these trade-offs, the fundamental question could not be more important: What effect will the government’s decisions today have on the economy’s productive capacity—and thus the real standard of living—tomorrow? It is here that the concern for future generations should be concentrated.

\textbf{D. Annual and 10-Year Deficit Estimates}

In summary, to improve public discussion of the government’s fiscal situation, the least radical alternative would be to adopt a cyclically-adjusted deficit measure (preferably for the entire government sector, though that appears unlikely). Such a measure, while still imperfect, would allow policymakers to focus on the possible crowding out caused by its annual fiscal policies.

Medium-term forecasts are also valuable. While imperfect, such measures provide policymakers with useful guidance in looking past the current fiscal year. The use of annual as well as 10-year estimates of fiscal deficits, moreover, will allow policymakers to see the effects of their decisions on the path of the economy during the time period over which they have the most direct control. The effect of current fiscal policies on the standard of living of future generations arises most directly from the effect of borrowing on private investment; so policymakers could honor their future commitments by deciding how much borrowing they are willing to vote for during the ensuing 10 years.

\textsuperscript{69} Although the discussion here focuses on spending projects, taxing decisions can be analyzed in precisely the same fashion. Every aspect of the Code has the potential to change consumption decisions into investment decisions, investments into consumption, less productive investments into more productive investments, and the like.
Admittedly, having longer-term estimates available potentially can help keep politicians more honest, by preventing them from playing games with arbitrary time periods. It is not a stark all-or-nothing choice between standard deficit measures alone or long-term estimates alone. As argued below the knowledge that can be gained from the longer-term measures is so tentative that they should be used only if they send an unmistakable signal that is invariant to plausible changes in assumptions about the future.

IV. SOCIAL SECURITY AND LONG-TERM SOLVENCY

Given the intense focus in popular discourse on Social Security as a separate program, it is important to describe the structure of that program in light of its history and goals. Such an analysis permits a deeper look at the real issues behind the notion of program-specific solvency (that is, will Social Security go “bust,” as President Bush claims? as well as the broader effects of Social Security’s financing on the rest of the budget and on the economy.

A. Supporting People in Retirement, Infancy, and Otherwise

The basic economic problem posed by retirees is that they no longer produce goods and services by working, but they continue to consume goods and services while they are still alive. Indeed, this concept extends to children and the disabled as well, such that, at any given moment, those who are working must produce sufficient goods and services to satisfy not only themselves but also everyone who is not working for any reason. Total U.S. employment in January 2005 was just over 140 million workers, while the total population was nearing 300 million, meaning that every worker is supporting herself and slightly more than one other person, on average.

The methods of providing consumption to nonworkers fall into several simple categories. Direct provision of consumption simply involves having some workers pay for the goods and services consumed

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71 Richard W. Stevenson, For Bush, a Long Embrace of Social Security Plan, N.Y. Times, Feb. 27, 2005, § 1, at 1 (“Social Security ‘will be bust in 10 years unless there are some changes,’ [Bush] said . . .”).
by a nonworker. Family arrangements are the prototype of this method, which is in part what the Social Security system was designed to replace, because some nonworkers have no families (or less economically prosperous families) on which to rely.

Absent familial connection and government transfer programs, the two remaining basic methods of financing nonworkers' consumption—individual savings accounts and social security—both involve saving during working years and consuming during retirement years. While structurally quite distinct, the two methods boil down to precisely the same trade-offs.

1. Individual Savings Accounts and Social Security Contributions

The government can assist workers in providing for their retirement years by structuring contract and property rules (and sometimes tax rules) that allow workers to save part of their incomes in interest-bearing accounts. This can range from simple voluntary savings accounts to employer-matched, tax-preferred retirement savings plans (such as 401(k) accounts and Individual Retirement Accounts). No matter the contractual complexities, the purpose is to give workers the confidence that their funds will be legally protected and available when they decide to stop working.

The Social Security system, on the other hand, looks quite different. There, workers reduce their current consumption not by making deposits into savings accounts but by making contributions to the system through payroll taxes. The result is not an individual account with funds growing at a market-set interest rate, but a programmatic guarantee that the worker’s contributions today will be rewarded with benefits paid by the government and funded by future workers when current workers are retired.

2. National Saving

From the standpoint of the aggregate economy, these formally different financing methods are indistinguishable. Imagine a country in which there is one retiree and two workers. The retiree is consuming $1,000 per month of goods and services. The workers are both consuming $2,000 per month. Shared equally, each worker must be made to produce $2,500 per month and give $500 per month to the retiree.

The method of financing cannot change this fundamental arithmetic. If the retiree is financing consumption by drawing down a savings account, he or she would withdraw $1,000 a month, which would count as negative saving. Simultaneously, the workers would be for-bearing from the opportunity to consume all of the goods and services
that their incomes could purchase, putting $500 each per month into their retirement accounts and leaving $1,000 worth of goods available for the retiree to purchase. If the amounts do not balance (that is, if the retiree tries to buy more goods than the workers are willing to forswear), and if the total amount of goods and services is already determined, then prices would have to change to balance the system. Crucially, though, the net amount of annual saving in such a system is precisely zero, because the retiree’s dissaving will exactly offset the workers’ saving.

A direct financing method like Social Security’s achieves the same result. In any time period (such as a year), workers divert $500 each from current consumption to allow the retiree to consume $1,000 of goods and services. Neither the retiree nor the workers would have any official saving or dissaving, but the government’s accounts would show $1,000 in total taxes (national saving) and $1,000 in retirement benefits (national dissaving), again with a perfect offset. The form differs, but the macroeconomic substance is the same.

B. Long-Term Balance and Imbalance

If the simple world described above were to continue in perpetuity, there would be no long-range funding problems and no macroeconomic effects created by different methods of financing. If there were already a Social Security-like funding mechanism in place, there would be no reason to change to any other mechanism. Each year’s benefits would be available to retirees because workers would be consuming less than they otherwise could purchase.

The world described above, however, assumes a stable demographic environment in which workers pass into retirement and are replaced by an appropriate number of new workers. That assumption is, of course, not true for the current U.S. retirement system. The current difficulty with the Social Security system arose because of concern over the retirement of the baby boomers.74 One consequence of the long-term demographic changes is, of course, that the number of workers per retiree will soon change dramatically. Starting in the mid-1970’s, the ratio of workers to beneficiaries has fluctuated between 3.2 and 3.4, but that number is projected to fall to 2.6 in 2020 and to level off at 1.9 starting in 2065.75


While this decline might seem to suggest that there is no way to save the system short of significant benefit cuts, the worker-to-retiree ratio is only half the story. If the average productivity of each worker rises by enough to offset the decline in the relative number of workers producing goods, then the demographic change need not portend lower standards of living for either future workers or future retirees.

1. The Trust Funds

When a government-run retirement system is in annual balance, there is no need to carry over balances or to borrow in any given year. In 1983, the Social Security system was changed to collect more in taxes every year than would be paid in benefits, while the baby boomers were still in their prime earning years. Then, when they worked their way through retirement, the system deliberately would be underfunded by design, with benefits exceeding revenues for several more decades. During the fat years, the excess tax revenues would be credited to a trust fund, and in the lean years, the deficit in the system would count as a withdrawal from the funds.

This accounting convention, of course, was consciously set up only as a bookkeeping matter. In any given year, since the rest of the government’s budget almost certainly would be in deficit, the excess from Social Security would finance all or part of that deficit. In 2004, for example, the non-Social Security deficit was $567.4 billion, while Social Security ran a surplus of $151.1 billion.

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76 For example, a recent letter to The New York Times treated the workers-to-retiree ratio as the only relevant datum for understanding long-term solvency. Karen Burke, Letter to the Editor, N.Y. Times, Dec. 10, 2004, at A40 (“When benefits exceed the payroll tax receipts . . . [,] demography is destiny: a ballooning cohort of retirees will be dependent upon a relatively stable working-age population.”).


78 See Nataraj & Shoven, note 63, at 2 (“[T]he Greenspan Commission’s plan was for Social Security to depart from pay-as-you-go (PAYGO) financing and to partially prefund the retirement costs of the baby boom generation.”); see also Buchanan, note 74; Spencer Rich, The Old-Age Fund Again Is Secure, Washington Post, Nov. 6, 1983, at F1 (“[T]he old-age and disability funds were put in secure position for a number of years and perhaps for many decades into the next century.”).


It should be remembered, moreover, that there is no aggregate difference between having Treasury directly use the annual Social Security surplus and having Treasury borrow more on the financial markets while Social Security lends on those same financial markets. Either way, in 2004, the federal government would have drawn a net $412.1 billion from the financial markets.81

2. Turning Points in the Trust Funds

Since the trust funds were created to deal with the large, but gradual, shifts in the financing of the nation’s retirement system, the system was designed to go through two phases. In the first phase, the Social Security system would run surpluses that grew from year to year. At some point, revenues would stop growing faster than benefits, such that there still would be annual surpluses, but they would shrink inexorably each year. The second phase would see the emergence and growth of annual deficits, followed by gradually shrinking deficits trending toward annual balance.

The date when the system moves from the first phase to the second phase is, from the standpoint of 1983, not particularly interesting. It is simply an artifact of the system’s design. There had to be a turning point, and it would happen somewhere between the point when the trust funds began and the point when the system returned to annual balance. This was part of the plan, not a crisis date.

In addition, with the system no longer designed to generate annual balance, the possibility arose that the system not only would be financially imbalanced in specific years but also as measured in the aggregate over all future years. There was thus a possibility that the system might not perfectly hit a “smooth landing,” as it were, with benefits exceeding revenues for more years than originally planned. Again, this was implicit in the system’s design from the beginning. If the surplus years did not last as long (or were not as bountiful) as originally projected, or if the deficit years lasted longer (or were leaner) than projected, then there would be a date at which the trust fund would go negative.

3. Are the Turning Points Important?

The important point to recognize is that those two dates—the turning point from annual surpluses to annual deficits, and the date of possible trust fund depletion—are not dates at which something dra-

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81 See id. (citing $412.1 billion as the total budget deficit for 2004). Figures do not add up due to rounding error and miscellaneous items.
matic must change in the system. The year before the first turning point would have a very small annual surplus, and the year after would have a very small deficit, but the difference between those two years would not be meaningfully larger than the difference between any other two-year span in that era.

The lack of drama is even more pronounced regarding the date of possible trust fund depletion.\textsuperscript{82} There, Social Security would be running annual deficits both before and after the depletion dates, and those deficits would be of relatively equal size. Unless the depletion date arrives much earlier than anticipated, in fact, the year after depletion would actually see a somewhat smaller deficit than the year before depletion because the system at that point will be gradually moving toward balance as the ranks of the baby boomers thin, making each year's deficit somewhat smaller than the last.

The decades-long maturation and eventual passing of the baby boom generation, therefore, does not cause sudden shifts that automatically must throw a system out of balance. Nor need this evolution create any specific dates when a crisis occurs. The dates that one might focus on are artifacts of the system, not points of real economic interest. The important economic issue is, instead, whether the long-term balances or imbalances will lead to unfortunate consequences. It is long-term trends that matter, not the dates associated with specific turning points. The political discussion, unfortunately, has tended to focus almost exclusively on those turning points.

\section{C. Competing Analyses of Long-Term Solvency}

Two government agencies, the Social Security Administration and the Congressional Budget Office (CBO), provide regular analyses of the long-term finances of the system. The most recent Trustees Report from the Social Security Administration provides estimates that are, on the whole, less optimistic than those provided by the CBO.

The Social Security Trustees use three sets of economic assumptions to generate their forecasts,\textsuperscript{83} whereas the CBO provides a mid-range estimate and a probability distribution of possible alternative paths.\textsuperscript{84} Each agency focuses on the intermediate assumptions when summarizing their findings. Differences arising from these assumptions are noted below.

\textsuperscript{82} This assumes that the law allows continued borrowing after a depletion date. See Section IV.D.
\textsuperscript{83} Trustees Report, note 75 (providing pessimistic, optimistic, and mid-range scenarios).
1. The First Turning Point

As noted above, the point at which the system turns from annual surpluses to annual deficits is interesting more as a symbolic matter than as a real one. Even so, because public discussion has begun to focus on these issues, both agencies have provided estimates of this turning point. The Trustees estimate that, under their intermediate set of assumptions, the system will swing from surpluses to deficit in 2018.\textsuperscript{85} Under the most pessimistic assumptions, the turning point comes in 2014, and under the more optimistic assumptions, the turning point is in 2022.\textsuperscript{86}

The CBO’s estimates are not much different. In its 2004 report, the CBO estimated (under what it views as the most reasonable economic assumptions) that the turning point would come in 2019.\textsuperscript{87} Only seven months after issuing that estimate, though, the CBO’s revised estimates put the turning point a year later, in 2020.\textsuperscript{88}

Given that the first turning point is driven by the retirement of the baby boomers, which is not very far in the future, it is not surprising that the CBO and the Trustees provide similar estimates. Their differing estimates of the depletion date, though, bear some consideration.

2. Trust Fund Depletion

The Trustees’ forecasts of the date of trust fund depletion are 2031 under the most pessimistic assumptions and 2042 under the mid-range assumptions, whereas the trust fund is never depleted at all under the more optimistic assumptions.\textsuperscript{89} The CBO’s mid-range estimate projects that the trust fund will be depleted in 2052,\textsuperscript{90} 10 years later than the Trustees’ intermediate estimate.

The CBO presents an analysis of the difference between its projections and the Trustees’ projections. While the CBO relies on the Trustees’ demographic assumptions, it uses different economic assumptions,\textsuperscript{91} and concludes that some differences “improve the financial outlook for Social Security and others worsen it.”\textsuperscript{92} Specifically, the CBO assumes that real earnings will grow at a 1.3% annual rate,
as opposed to the Trustees' assumption of 1.1% annual growth. The CBO assumes an average real interest rate of 3.3%, higher than the Trustees' assumed 3% rate. The CBO also assumes lower inflation (2.2% per year against 2.8%) and a lower unemployment rate (5.2% versus 5.5%).

It is not my purpose here to delve into the vagaries of economic forecasting. Instead, it is important simply to point out that widely varying long-term projections are based on relatively minor (and utterly defensible) differences in economic assumptions.

D. A Key Question: What Is "Current Law"?

As described in Section V, the baseline used to compute the fiscal gap (and thus generational accounts) is "current law." That is, the mental exercise involves asking what would happen if current law were completely unchanged forever. In the context of Social Security, however, there is a conflict between two aspects of existing law. The benefits and revenues anticipated under current law, under the intermediate and most pessimistic assumptions, lead to a point at which the trust fund is depleted. If the system is not allowed to borrow to cover full benefits after that point, benefits must be cut immediately, by 22% starting in 2053, under the CBO's assumptions.

On the other hand, if the scheduled benefits continue to be paid after the depletion date, the Social Security system continues to run annual deficits unless and until it comes back into balance or surplus. Indeed, the CBO's updated estimates changed the label of these two scenarios. The "scheduled benefits" scenario remains in place, but the "trust-fund-financed" scenario has now become the "current law" scenario.

Under the assumption that benefits will continue to be paid even after trust fund depletion, the Trustees estimate that the aggregate Social Security gap over the 75-year period from 2004-2078 is $3.7 trillion, while the gap over the infinite future is $10.4 trillion. These rather dramatic differences highlight just how artificial the "current law" assumption is. The current law that the CBO assumes actually provides a less pessimistic forecast, because Social Security benefits

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94 Id.
95 Id.
96 CBO Update, note 88, at 1.
97 Id.
98 Trustees' Report, note 75, at 57-58. Note that $10.4 trillion is only 1.2% of GDP over the infinite future. Id. at 58.
must be cut absent intervention by policymakers. The more dramatic measures of long-term imbalance, on the other hand, assume that a future Congress will prevent such automatic cuts. For example, the estimate of a long-term $7 trillion Social Security deficit, noted below, can only be valid if Congress allows Social Security to continue to run deficits even after the trust fund is depleted.

V. FISCAL GAPS AND GENERATIONAL ACCOUNTING

The fiscal gap/generational accounting approach is built upon some very appealing foundational arguments and uses an apparatus similar to that described in Section IV regarding long-term Social Security forecasts. First, as noted above, deficit accounting is arbitrary, because there is nothing special about a year as the unit of analysis. Second, even without any political games, there is no good analytical reason to assess government programs on an annual basis. One should analyze projects that last longer than a year in their relevant time frame. Surely, a year is far too short a time in which to measure meaningfully the impact on the economy of the vast majority of government programs and tax policies.

Of course, once one realizes that a year is arbitrary, one also must recognize that there is no nonarbitrary alternative. The infinite future is out there, and perhaps the best way to proceed is to use the simple financial concept of net present value discounting to bring all future receipts and expenditures into one current estimate. This approach has an added benefit in that it avoids the issue noted earlier of whether a program has a dedicated financing mechanism. While it

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99 Because all spending laws require the appropriation of funds, but no appropriation has been enacted to permit borrowing by Social Security after the trust fund has been depleted, the system will be forced to cut benefits to the level supported by incoming revenues. The law is silent, however, on how the cuts must be made. While the CBO assumes across-the-board cuts, see CBO Update, note 88, figs. 2-1, 2-2 & 2-3, tbl.2-1, there is no statutory authority for that position. Here, therefore, there is no current law at all.

100 See text accompanying note 110. Cf. Gokhale & Smetters, note 1, at 19 (describing Social Security “shutdown” measure as alternative to the authors’ approach).

101 As above, arbitrarily aiming to balance annual books can introduce its own set of bizarre games. In 2001, for example, temporarily focused on the non-Social Security deficit, the Bush administration included surpluses in their forecasts that were so small—yet definitely surpluses—as to strain credulity. See Glenn Kessler, Surplus Plunges in New Forecast, Wash. Post, Aug. 23, 2001, § A, at A01 (“For the fiscal year that ends Sept. 30, the administration projected a budget surplus of $158 billion, but only $1 billion remained after the surplus generated by Social Security payroll taxes is excluded. The administration estimated another slim $1 billion non-Social Security surplus in 2002, $2 billion in 2003 and $6 billion in 2004.”); see also Elizabeth Garrett, Accounting for the Federal Budget and Its Reform, 41 Harv. J. on Legis. 187, 194 (2004) (“Budget windows were extended to five and then ten years because of egregious trickery such as moving a pay date one day from one fiscal year to the next.”).
arguably makes sense to compare the long-term planned expenditures and expected receipts for something like the highway trust fund, the majority of government programs can meaningfully be assessed only in the aggregate, because most programs are not supported by their own tax regimes.

A. Computing the Accounts

1. The Fiscal Gap

The fundamental analytical achievement of the generational accounting framework is its attempt to compute an aggregate, discounted federal deficit or surplus into the infinite future. Many federal budget documents starting more than a decade ago included estimates generated using a fiscal gap/generational accounting framework, and Kotlikoff has provided a great deal of input over the years to the work of the CBO.

The basic logic of fiscal gap/generational accounting, as described above, is based on the assumption that current law remains unchanged indefinitely (assuming, of course, that one knows what current law is). What are the likely paths of government spending and tax receipts, given expected trends in population, economic growth, and the like? Given those likely paths, what is the aggregate gap between spending and tax revenues into the infinite future? Taking the analysis one step further, it is then theoretically possible to estimate the net amount of money that an individual will pay in taxes to the government over his or her lifetime, which is the generational accounting part of this approach.

The appeal of moving to long-term budget calculations loses its luster rather quickly, however, in the face of the complexity of long-term budget estimation. If the Social Security calculations described earlier are challenging, these calculations are significantly more so. Consider the inputs necessary to generate a fiscal gap/generational accounting estimate. Tax receipts for each future year must be calculated on the basis of estimates of the number of taxpayers, their gross incomes, their deductions (and exclusions and exemptions), and their tax rates. Only the last of these numbers is written into law (and highly variable law at that), whereas the others depend on long-term estimates of birth rates, death rates, net immigration rates, productiv-

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102 Note, though, that this is still only a federal calculation. If one were to adopt fiscal gap/generational accounting as the preferred accounting framework, it surely would be desirable to extend it to the entire government sector.

103 See sources cited in Robert Haveman, Should Generational Accounts Replace Public Budgets and Deficits?, 8 J. Econ. Persp. 95, 95 n.1 (1994).

104 See Section IV.D.
ity growth rates, homeownership rates, trends in medical insurance coverage by the private sector, and on and on.

Certainly, some long-term estimates can be quite reliable. Birth and death rates change rather slowly, so projecting the number of native-born Americans likely to be living in 30 or 40 years is not much of a stretch. On the other hand, other estimates are notoriously volatile. The CBO changed its estimate of the 2004 annual deficit, for example, by over 200% over the space of several months in 2003; and it even changed its estimate of the then-current year’s deficit by 100% over that same span. Even longer-term forecasts, which plausibly are less prone to temporary blips, are more prone to cumulative error. Indeed, even history is unstable, as the “New Economy’s” performance in the 1990’s has been substantially reduced by updated official estimates.

Gokhale and Smetters have provided a recent calculation of the fiscal gap, using the most current version of the fiscal gap/generational accounting methodology. Admirably transparent in its description of how the calculations were derived, this study estimates a fiscal gap of $44.2 trillion, of which $7 trillion is attributable to Social Security, $36.6 trillion is attributable to Medicare (split roughly equally be-

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106 The pioneering economic forecaster Otto Eckstein, founder of Data Resources, Inc. (now DRI/McGraw-Hill) in 1982 offered advice to his graduate students in words to the following effect: “You can believe our quarterly forecasts rounded to a full percentage point (for example, 4.3% growth forecasts mean that growth will be somewhere in the neighborhood of 4% in the next quarter). You can believe the sign of our annual forecasts. And you should just ignore our five-year projections.” (notes on file with author).

107 See Jeff Madrick, A Tarnished New Economy Loses More Luster With Revised Productivity Data, N.Y. Times, Aug. 30, 2001, § C, at 2 (“The overly romantic faith in a new economy has already done plenty of damage . . . But recent revisions to the productivity data reported by the Bureau of Labor Statistics show how thin the new-economy thinking has been all along.”).

108 Gokhale & Smetters, note 1.

109 See id. at 7-9, apps. A & B (setting forth and explaining the authors’ formula for calculating fiscal imbalance). While the discussion of the mechanics of their estimates is clear, it is hardly dispassionate. The authors inform their readers that their calculations show “how much money the government must come up with immediately,” id. at 3 (emphasis in original), that long-term sustainability requires an additional 16.6% of payrolls to be “taxed away forever beginning today,” id. at 5 (emphasis in original), and that alternatives to that policy are “equally drastic,” id. at 5. The authors’ tone wavers between urgent and alarmist.
between Part A and Part B), and only $.5 trillion is attributable to the
rest of the federal government.\footnote{Id. at 3. \(\text{Gokhale and Smetters prefer the term "fiscal imbalance," id. at 2, but I use the more common fiscal gap."}\) This is a midpoint estimate. The lower bound is $29 trillion, while the higher bound—"under still quite conservative assumptions"—is $64 trillion. Id. at 6.}

Gokhale and Smetters provide a range of scenarios under which the fiscal gap could be erased, suggesting as their most likely choice an immediate and permanent 16.6% increase in wage taxes.\footnote{Id. at 5.} Updated estimates based on the same model (crucially including the just-passed Medicare drug benefit) show the fiscal gap to have reached approximately $73 trillion.\footnote{Shaviro, Reckless Disregard, note 18, at 1299.} \footnote{Gokhale & Smetters, note 1, at 36-37 tbl.4.} (Note, however, that these estimates are presented as dollar figures with no standard of comparison. $44 trillion is simply a big number. Since the corresponding measure of discounted infinite-horizon GDP is $682 trillion,\footnote{The $44 trillion figure has received prominent placement in The New York Times. See Edmund L. Andrews, Fearing That a Gap Will Become a Chasm, N.Y. Times, Mar. 2, 2004, at C1.} the fiscal gap-to-GDP ratio is just under 6.5%—perhaps an important number, but much less likely to grab headlines.\footnote{Auerbach et al., Generational Accounting, note 8, at 77-79.})

The analysis below shows that the exact estimates provided by such studies—whether $44 trillion, $73 trillion, or some other large number—are ultimately not very helpful in fiscal analysis. The purpose, again, is not to engage in dueling long-term estimates, but to assess what can be learned from such long-term estimates.

2. \textit{Lifetime Net Tax Rates}

Although it is analytically separable from the long-term budgeting calculation, the "generational" part of generational accounting provides perhaps its most potent political impact. Kotlikoff argues that it is possible to move from the "what if we did nothing?" question to compare the treatment of different generations based on their lifetime receipts of government benefits and their lifetime tax payments. Using the same method described above, it is possible to choose arbitrary cutoff dates for different generations and then to calculate their "lifetime net tax rates," that is, the net present value of their lifetime tax payments minus the net present value of their lifetime government-paid benefits.\footnote{Id. at 7.}

Seeming to confirm the suspicion that a large population cohort in a democracy could distort the benefit system in its favor (especially in a
democracy in which the young are less likely to vote), Kotlikoff made national headlines when he announced in 1993 that the lifetime net tax rate of younger generations would be 71%, whereas the rate faced so far by the generation born in 1960 is 32%, the rate faced so far by the generation born in 1930 is 28%, and the rate faced so far by the generation born in 1900 is 21%.116 A few years later, the numbers became even more dramatic, when the 71% figure was increased to 84%.117

B. Weaknesses in the Fiscal Gap/Generational Accounting Framework

As appealing as the basic foundations of fiscal gap/generational accounting might be, the theory does not deliver what it promises. Far from being a neutral tool for dispassionate evaluation by policymakers, the generational accounting model makes the fiscal horizon look far worse than it probably will be, and these results can color the policy debate for the worse. Moreover, the hope that fiscal gap/generational accounting calculations can act as a default early-warning system is at best overdrawn. It is simply not possible to define a clean baseline. Finally, the economic assumptions on which fiscal gap/ generational accounting is based are too contestable to use for meaningful policy analysis.

1. Paying Down the Debt

The source of the huge differences between generations noted above is quite peculiar. The generational accounts assume that, as of the date that an account is calculated, there are two groups of citizens: the generations that are already born and the one that is about to be born.118 Then, the accounts compute the taxes that the already-born will pay minus the direct cash benefits that they will receive under the current tax and spending regimes.119

116 Kotlikoff, Deficit Delusion, note 8, at 105.
117 Cohen cites this higher figure, Cohen, note 14, at 2238 n.72, as does Shaviro, Generational Challenge, note 13, at 716. On the other hand, when Kotlikoff recently recalculated his generational accounts and found that the 84% rate for future generations had fallen to 35.81%, Laurence J. Kotlikoff, The Coming Generational Storm (2001), available at http://www.econ.bu/kotlikoff, the “good” news was not met with fanfare. (The incredible precision of those estimates is a separate issue.)
118 This means, of course, that the political audience for these estimates, the younger nonvoters, in fact was not included in the group that is supposed to be paying nearly all of their lifetime income in net taxes.
119 See Haveman, note 103, at 97 (“For people of different ages alive today—current generations—the values reflect only the flows of aggregate future taxes and transfers due
The soon-to-be-born, however, are treated differently. For them, lifetime taxes include not just those that they would be forced to pay under current law, but also taxes sufficient to pay down the entire national debt (accumulated before they were born) during their lifetimes. There is no good reason to assume that the entire national debt will or must be paid in that time, but that is the assumption that drove the dramatic 84% result.

On its own, of course, this assumption cannot help but make things look much worse for the new generation. With an entire lifetime of work ahead of them, and with the government unable to borrow money, they must pay for their own benefits as well as those of their parents and grandparents. The older generations, meanwhile, had a good ride, and they are allowed to continue that ride even while their heirs are paying for the difference.

The intergenerational impact of current fiscal policy, however, is better viewed through the more traditional crowding-out lens. Current deficits are likely to decrease future growth in GDP, which makes future generations worse off than they otherwise would be. The intergenerational comparisons are becoming less relevant as the generations that benefited from the expansion of Social Security and Medicare die off. Moving forward, the real question reduces to the now-versus-later question that always should have been the central focus of budgetary analysis. We cannot know whether any single future generation will be called upon to pay down the debt, but we can say that any decision that raises deficits at one point in time—assuming that those deficits do not finance productive public investment—is likely to cumulatively decrease future GDP.

2. Benefits Not Counted in a Generation’s Accounts

The calculation of any particular generation’s lifetime net tax rate also excludes many of the indirect benefits provided by governments—indeed, the very benefits for which governments traditionally are thought to exist. The only benefits that go into the fiscal gap/generational accounting calculation are those that are paid in cash. The benefits from cleaner air, pleasant parks, medical research and

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120 Id. at 100 n.5 ("In effect, there are two implicit fiscal regimes in place during the future years when both members of current generations and members of future generations are living. The net taxes of currently living people do not include a required contribution for debt retirement; the net value for future cohorts does.").

121 Since the government’s bondholders tend to be older (especially indirectly through retirement funds), this also skews the intergenerational comparison as income is redistributed upward.
development, lower crime, and the like, are not counted as benefits. Taxes pay for them, but they are a net cost of government in the fiscal gap/generational accounting calculations.\textsuperscript{122}

It is not clear a priori how this fault in the generational accounts would affect intergenerational comparisons. Indeed, it is imaginable that these benefits are so diffuse that they benefit every citizen equally. It is also possible, though, that some of these benefits are disproportionately shared. The cost of educating the baby boomers was borne by their parents, yet all future generations will benefit from it.\textsuperscript{123}

Leaving that very open question aside, though, the fact that the fiscal gap/generational accounting calculations of lifetime net tax rates are skewed upward is important simply because it skews the political response. If the members of Gen X are told that their net tax rate is 84%, while that of their parents is 35%, they are likely to have two responses: (1) Our generation is being cheated, and (2) all generations are being cheated. After all, while 35% is better than 84%, paying more than one-third of your lifetime earnings to a government that (according to this model) does not do anything useful with the money is likely to be rather upsetting.

If, on the other hand, the numbers were 8.4% and 3.5%, the magnitude of the intergenerational backlash would be muted (since outrage is likely to be based at least partly on the magnitude of the difference as well as the proportional comparison), and the antigovernment reaction might not even register politically.

In other words, the effects on society of this widely-quoted statistic go beyond the simple, modest claim that fiscal gap/generational accounting is just a diagnostic tool. It is a political tool, and its effects are predictable.

\textsuperscript{122} It is, of course, always possible to adjust the fiscal gap/generational accounting calculations to take these noncash benefits into account. To the extent that this can be done, fiscal gap/generational accounting begins to resemble capital budgeting. For a description of capital budgeting and an argument that the federal government should adopt capital budgeting in its official accounts, see Neil H. Buchanan, What Is Fiscal Responsibility? Long-term Deficits, Generational Accounting, and Capital Budgeting 38-43 (Apr. 7, 2004), available at <http://law.bepress.com/rutgersnewarklwps/fp/art8>.

\textsuperscript{123} While it is not immediately obvious how people, say, six generations in the future will benefit from the education that baby boomers have received, the education of each generation is important to the well-being of all future generations. As a generation is educated, the possible standard of living for that generation goes up; and from that platform, the next generation's education can increase people's social and economic well-being still further. Failing to educate a generation, conversely, sets all future generations back because an entire cohort of people will have failed to innovate and to build the productive capacity that will enrich those who follow.
3. Demographic Trends and Health Care Spending

As discussed above, the most important demographic phenomenon facing the United States and other Western countries is the baby boom and the subsequent dramatic decline in birth rates after 1964. While this phenomenon will end within a few decades, the death of the boomers will not solve at least some parts of the fiscal gap.

An important trend is the general increase in life expectancies over the long term. Indeed, given long-term trends in health, even after the 75-year window, the paths of receipts and expenditures continue to diverge, as an increasingly large nonworking aged population consumes more of the economy's resources, largely through the health care system.

If this turns out to be true, it would mean that the focus should not be on the effects of the baby boomers but on eventually reining in the seemingly insatiable appetite for medical care. While that might be a wise policy on its own, however, the fiscal gap/generational accounting framework does not provide a compelling reason to adopt such limits.

For example, Shaviro cites research indicating that "healthcare expenditures on the elderly will continue to rise significantly relative to GDP." This, however, assumes that health care spending on an aging population will show the same trends as current health care expenditures. For example, if the typical 75-year-old today consumes a given amount of health care, and if there will be twice as many living 75-year-olds in 50 years, then it would appear that health care spending would have to double in the future. This assumes, in turn, that even though life expectancies will rise, elder health at specific ages will not improve.

A large fraction of the money spent on health care, however, is spent at the very end of life—heroic, life-prolonging procedures that add a few weeks or months to the lives of chronically ill patients. If those chronically ill patients do not become chronically ill until 20 years later in life, however, there is no reason why overall health care spending must rise—even if we never change the way we deal with end-of-life decisions.

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125 Shaviro, Medicare, note 15, at 98.

126 Daniel Altman, How to Save Medicare? Die Sooner, N.Y. Times, Feb. 27, 2005, § 3, at 1 ("For the last few decades, the share of Medicare costs incurred by patients in their last year of life has stayed at about 28 percent . . . .").
This is not to say that it is impossible to imagine a future with higher health care expenditures. It does indicate, however, just how difficult it is to rely on estimates of health-related spending decades in the future. Current estimates indicate that health care spending will rise from 15.4% of GDP in 2004 to 18.7% in 2014 and that the federal government's share of that spending will rise to 49% of the total.\textsuperscript{127}

The calculations in Gokhale and Smetters, on the other hand, are based on a much simpler assumption, that medical care will grow for the next 75 years at a rate one percentage point faster than the growth rate of GDP, then fall over the ensuing 30 years to grow at a rate equal to GDP growth.\textsuperscript{128} These assumptions mirror those made by the Medicare Trustees.\textsuperscript{129} The vast majority of their estimated fiscal gap, both pre- and post-2078, is caused by the Medicare growth assumption,\textsuperscript{130} suggesting that it is probably more accurate to describe any long-term fiscal crisis as an economy-wide health care crisis.\textsuperscript{131}

If the cost of medical care continues to grow in future decades at rates consistently exceeding the growth rate of GDP, then certainly a policy intervention will become necessary. While it is possible to starve everything else in the service of health care, it would be more sensible to recognize that the core of the problem lies not in public finance but in health policy. Fixing that problem will prevent needless and possibly unwise cuts in other fiscal priorities.

4. After-Tax Standard of Living

Finally, it is important to emphasize that the estimates of lifetime net tax rates are analytically incomplete. What is left out is the question of whether future generations are worse off because of the higher net tax rates. If pretax income is rising faster than tax rates, future generations can be better off even though they will pay higher tax rates.

According to the CBO, this is precisely what would happen under their mid-range assumptions (that is, the assumptions that lead to trust fund depletion in 2052). In its most recent report, the CBO analyzed the benefits received by workers, organized in 10-year birth cohorts


\textsuperscript{128} Gokhale & Smetters, note 1, at 23.

\textsuperscript{129} Id.

\textsuperscript{130} See note 154 and accompanying text.

\textsuperscript{131} See Paul R. Krugman, Social Security Scare, N.Y. Times, Mar. 5, 2004, at A23 ("The projected rise in Medicare expenses is mainly driven not by demography, but by the rising cost of medical care, which in turn mainly reflects medical progress, which allows doctors to treat a wider range of conditions.").
from 1940 (the group that is currently retiring) to 2000 (today’s toddlers).\textsuperscript{132} Even after assuming an across-the-board cut in benefits starting in 2053 ("current law"), the CBO’s estimates show that no birth cohort has a lower present value of inflation-adjusted lifetime benefits than any previous generation.\textsuperscript{133} Only the lowest quintile of the population shows any cohort facing a net decrease in real lifetime benefits (for the 1980 and 1990 cohorts), and even those cohorts do better than the 1940, 1950, and 1960 cohorts.\textsuperscript{134} Future policymakers also could address this difference if they choose not to make cuts across the board but rather adjusted relative benefits to prevent low income workers from facing cuts.)

In short, the issue presented by the generational accounts estimates is misleading in that it focuses on lifetime tax rates rather than lifetime standard of living. While dramatically high tax rates grab headlines, they should not be the focus of fiscal policymakers or the public.

\textbf{C. Generational Accounting Without Generations?}

Populist appeal aside, the importance of the generational part of the fiscal gap/generational accounting approach should not be underestimated. Kotlikoff and his co-authors argue that they have created a meaningful baseline, allowing assessment of the effects of any proposed government policy over the long run, and potentially comparing that affect on different age groups.\textsuperscript{135} If these claims were true, then it would be important for everyone to send their policy proposals through the fiscal gap/generational accounting machine. If the results of such an analysis turned out negative, the policy would be presumed harmful until proven beneficial.

On the other hand, one also could take a step back and remove the generations out of generational accounting, simply stopping after computing the fiscal gap. One thereby could look at long-term trends and calculate long-term tax revenues and government spending, assuming a continuation of current policies. If this calculation were to show a deficit, then it is a warning: Unless something is changed, the government will have to cut spending or raise taxes on future generations. While we might still choose to do nothing, the argument contin-

\textsuperscript{132} CBO Update, note 88, at 1 \& tbl.2-1.
\textsuperscript{133} Id.
\textsuperscript{134} Id.
\textsuperscript{135} Auerbach et al., Generational Accounting, note 8, at 92 ("Generational accounting represents a new and comprehensive method of long-term fiscal planning. . . [I]t is a prescription, based on economic theory, for how to assess the generational burden and macroeconomic effects of fiscal policy.").
ues, at least the fiscal gap would provide a fair number from which to work.\textsuperscript{136}

1. Another Baseline Problem

The asserted agnosticism behind fiscal gap calculations thus rests on the idea that they are warnings, not predictions. Indeed, if fiscal gap analysis is used as its proponents suggest, we enable ourselves to make "tough but sensible" choices now to prevent the disaster that surely awaits us if we fail to act.\textsuperscript{137} In fact, though, the theory is not agnostic, and its proponents' call to action rests on weak assumptions.

The underlying question is one of default. Once the cross-generational comparisons are set aside, fiscal gap claims to ask, in essence: If we were to change absolutely nothing, and if we can believe the forecasts on which our estimates are based, are our current fiscal policies allowing living generations to steal economic resources from their grandchildren and their grandchildren’s grandchildren? But it does not stop there. If the answer to that question is yes, then the argument is that we must act now. Why now? Because our current path is unsustainable, and delay is only going to allow matters to worsen.\textsuperscript{138} Sacrifice today means sowing a greater harvest tomorrow.

While this logic surely appeals to our Puritan roots, it is misleading. We should only enact new policies now if we believe that we will not change policies along the way for other reasons. By way of analogy, consider the concept (known as "bracket creep") that tax rates in the 1970's would have led to an ever-higher percentage of GDP being collected by the IRS, because inflation was pushing everyone inexorably into the highest tax brackets. If that argument had been coupled with a call to raise government spending immediately, because the fisc can count on ever-higher revenues in the future, surely that would have been widely derided as a foolish conclusion. Everyone knew that Congress would pass regular tax cuts to undo the effects of bracket creep; so even if no one anticipated the indexing of brackets to inflation in the 1981 tax bill,\textsuperscript{139} certainly no one thought that everyone

\textsuperscript{136} Even Haveman, despite offering a withering criticism of generational accounting, allows that this "base case" analysis can provide useful information. Haveman, note 103, at 99-100, 110.

\textsuperscript{137} Shaviro, Generational Challenge, note 13, at 716 (arguing that politicians should "openly face[e] today painful choices that ultimately will have to be faced anyway").

\textsuperscript{138} Id. (arguing that we should act "sooner rather than later"); see also Gokhale & Smetters, note 1, at 5 (arguing that "the size of the necessary corrective policies will grow larger the longer their adoption is postponed").

would end up in the 70% tax bracket when inflation had made even a street-sweeper "rich."\textsuperscript{140}

Similarly, the fiscal gap call to action loses much of its appeal when one realizes that the basis for this "interesting calculation" is arbitrary economic forecasts\textsuperscript{141} combined with the arbitrary assumption that only a few things are set in stone. Consider the current path of tax rates. Current tax law is in a bizarre state because of the 10-year reversion feature of the 2001 tax bill.\textsuperscript{142} The estate tax is set to decline, disappear, and reappear.\textsuperscript{143} The 28% tax bracket declines to 25% and then returns to 28% (with similar moves in the other brackets, and some brackets merge into others only to reappear in 2011).\textsuperscript{144} No one expects the reversion to happen. The House in 2002 passed, on partisanship lines, a bill to make the 2001 cuts permanent\textsuperscript{145}—although many viewed that action as nothing more than election year posturing. Even with the current one-party dominance of the federal government increasing the likelihood of tax cuts, it is not clear what form those cuts will take.

With the status quo ante not a serious possibility, and the status quo post unlikely ever to become the status quo at all, how can one even formulate a call to action on the basis of a fiscal gap calculation? In addition, current projections assume that the alternative minimum tax (which is not indexed to inflation) will remain in place, even though Congress almost surely will alter or repeal it when it begins to affect large sections of the middle class.\textsuperscript{146}

\textsuperscript{140} There are, of course, strong political economy arguments for indexing the Code rather than relying on ad hoc corrections, but those are beside the point here.

\textsuperscript{141} See Haveman, note 103, at 99 & n.4 (noting that generational accounting assumes current government policies will remain constant forever).

\textsuperscript{142} See Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, § 901, 115 Stat. 38, 150 (providing generally that the provisions of the Act are not applicable to tax years beginning after December 31, 2010). The Byrd rule, codified at 2 U.S.C. § 644 (2005), provides, upon any Senator's raising a point of order, for striking from reconciliation bills any provision that "decreases, or would decrease, revenues during a fiscal year after the fiscal years covered by such reconciliation bill or reconciliation resolution . . . ." 2 U.S.C. § 644(b)(1)(E). The inability to gain 60 votes to waive the point of order led the Senate to make all provisions of the 2001 Act void in 2011, the final fiscal year the bill covered.


\textsuperscript{144} Id. § 101, 115 Stat. 38, 41-42.


\textsuperscript{146} See Leonard E. Burman, William G. Gale, Jeffrey Rohaly & Benjamin H. Harris, The Individual AMT: Problems and Potential Solutions, 55 Nat'l Tax J. 555 (2002) (predicting that the nonindexed AMT will become a substantial burden on the middle class within the next decade and discussing options for reform).
2. What Happens When People Live Longer?

Applying this analysis to the demographic argument is potentially even more devastating to the fiscal gap position. If the time paths of revenues and expenditures do not reconcile after the death of the baby boom generation because of the trends in life expectancies, then surely it is important to forecast how those longer life expectancies will change both individual behavior and government policy. The Social Security Trustees estimate that the average life expectancy for women will rise from 74 in 2000 (the last year for which final calculations are available) to 78.8 in 2045 and 81.6 in 2080, with women's longevitys lengthening over those same years from 79.4 to 82.9 to 85.3.\textsuperscript{147}

As people live longer, they naturally will use more economic resources, possibly including medical care. People also might produce more economic resources. Based on current law under which retirement ages are rising to 67 and then staying put,\textsuperscript{148} fiscal gap/generational accounting estimates would have us believe that in 75 years—assuming that all of the other forecasts over that time span are true—we will have a nation of impressively healthy septuagenarians (and older) living off of the sweat of a relatively tiny population of younger workers.

Why make the assumption that the retirement age (effective if not statutory) will remain fixed as the population inevitably ages (relatively) healthfully? Boredom alone is likely to lead to a changed politics of retirement, with some people voluntarily staying employed or returning to the work force to fill the void. Moreover, the increasingly fragile financial condition of the elderly is keeping many people involuntarily in the labor force after reaching retirement age.\textsuperscript{149} The CBO estimates that accelerating the increase in the retirement age to 67 and then further increasing it to keep up with life expectancy would reduce Social Security outlays by 12\% in 2050.\textsuperscript{150} While an increase in the retirement age would be the arithmetic equivalent of a benefit cut, the point is that such a change or something like it is likely to happen

\textsuperscript{147} Trustees Report, note 75, at 81 tbl.V.A3.

\textsuperscript{148} See Congressional Budget Office, Budget Options 239 (2005), available at http://www.cbo.gov/ftpdoc.cfm?index=6075&type=1 ("Under current law, the age at which workers become eligible for full retirement benefits—known as the normal retirement age, or NRA—varies, depending on the individual's year of birth. For workers born before 1938, the NRA is 65 [and it reaches 67 for workers born in 1960 or later.")

\textsuperscript{149} See, e.g., Jennifer Bayot, As Bills Mount, Debts on Homes Rise for Elderly, N.Y. Times, July 4, 2004, § 1, at 1 ("Many [elderly borrowers] are forgoing retirement and taking on part-time work."); Eduardo Porter & Mary Williams Walsh, Retirement Becomes a Rest Stop As Pensions and Benefits Shrink, N.Y. Times, Feb. 9, 2005, at A1 (reporting that many older Americans are returning to work out of economic necessity).

\textsuperscript{150} Congressional Budget Office, note 148, at 239.
in any case, making the "nothing else changes" baseline assumption particularly problematic.

While an advocate of fiscal gap/generational accounting always can claim that his calculations can tell us what happens if retirement ages do not change, that is a far cry from justifying the argument that we need to cut benefits and raise taxes today on retirees in order to bring the long-term budget into balance. Indeed, Gokhale and Smetters do allow themselves to make a single departure from their blanket assumption that policy is set in stone. Separate from the bracket creep caused by inflation, real economic growth can cause "real bracket creep," whereby increases in real income cause every taxpayer's income ultimately to rise to the highest bracket. Gokhale and Smetters quite reasonably view this as absurd and thus assume that Congress will adjust the brackets over time to prevent this.\(^{151}\) This, of course, makes the estimated fiscal gap look worse, but more importantly, it raises the question of why this is the only concession to reality allowed in the estimates going forward.

3. The Fiscal Gap and the Annual Deficit

Perhaps the fiscal gap calculation should not be viewed as an important measure of the level of future deficits, but rather as a way to measure changes in future deficits. In other words, even if one does not feel confident that a $44 trillion fiscal gap estimate (or any other estimate) is reliable, one still might use it to measure the effects of the change in policy. (By analogy, we know that GDP is an imperfect measure of well-being; but if we conclude that the unmeasured aspects of GDP move roughly in proportion to measured GDP, we might use GDP as an acceptable proxy for well-being.) If a new policy raised the fiscal gap calculation from $50 trillion to $60 trillion, under this view, that would be valuable information.

There is something to be said for this argument, and it certainly supports the conclusion that there is no reason to have statistical agencies simply discontinue fiscal gap calculations entirely. It remains to be proven—although it seems plausible—that the weakness of the fiscal gap calculations does not make estimated changes in fiscal gap just as weak as the fiscal gap calculations themselves. Unless that can be

\(^{151}\) Gokhale & Smetters, note 1, at 30 (noting that OMB revenue estimates, which Gokhale and Smetters reject, "include a secular rise in revenues relative to GDP that could arise from . . . real bracket creep . . ."). Smetters also made this point much more clearly in a 2004 oral presentation on tax policy. Kent Smetters, Comments at the NYU School of Law Colloquium on Tax Policy and Public Finance (Jan. 29, 2004) (notes on file with author).
shown, relying on fiscal gap estimates for this purpose is a leap of faith.

The absolute level of the estimated fiscal gap is important for another reason. "[T]he [Fiscal Gap] grows by about $1.6 trillion per year to about $54 trillion by just 2008 unless corrective policies are implemented before then. This rapid annual increment is also about ten times as large as the official annual deficit reported for fiscal year 2002." Gokhale and Smetters thus suggest that the "true" deficit is not measured accurately by the annual cash-flow deficit but by the change in the fiscal gap from year to year. Because that annual change, in the absence of policy enactments, is simply equal to the previous year's fiscal gap times the assumed annual interest rate, this annual quasi-deficit measure will be much smaller if the forecasts in the fiscal gap include changes in retirement ages, health care cost trends, and the like. If the estimated fiscal gap were something like $15 trillion, in other words, the annual quasi-deficit would be just over $500 billion, whereas a fiscal gap of $88 trillion would imply an annual quasi-deficit of $3.2 trillion. The accuracy of the annual changes depends completely on the accuracy of the aggregate estimate of the level of fiscal gap.

4. Making the Fiscal Gap Disappear

Even if it were possible to agree on the likely future path of policy decisions, Congress can manipulate the fiscal gap simply by enacting policies that will take effect in the future. If, instead of Gokhale and Smetters's suggested immediate increase in wage taxes of 16.6%, Congress enacted an increase in wage taxes that started at .1% in 20 years and rose to some level well in excess of 16.6% 20 years later, the fiscal gap immediately would become zero. Cynics would argue that this is noncredible, and they would have a point. As enacted policy ("current law"), however, such a law would make the fiscal gap equal to zero, by definition. The annual quasi-deficit then also would equal zero. While nothing would have changed, these fiscal measures would show nothing amiss.

It is true that there would still be a relative burdening of future generations. As discussed below, it is not immediately clear that relatively burdening future generations is to be avoided, given that even the most pessimistic estimates of future GDP predict that future gen-

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152 Gokhale & Smetters, note 1, at 3.
erations are likely to enjoy significantly higher levels of income than we currently do.\footnote{Trustees Report, note 75, at 92 (projecting 2.2% growth in real GDP through 2013 for the pessimistic path, with real GDP growth converging on projected productivity growth after that); id. at 6 tbl.II.C1 (projecting annual productivity growth under the pessimistic assumption of 1.3%); id. at 79 tbl.V.A2 (projecting population growth under the pessimistic scenario from 2005 through 2080 from 301,429,000 to 351,414,000, a total increase of less than 17%). By contrast, 75 years of 1.3% growth in real GDP (even ignoring the higher 2.2% growth rate in the first decade) results in an increase of total real GDP of 163%, making output per person almost 150% higher than in 2005 (as an approximation, 163% minus 17%). See also Eissner, note 77 (describing similar calculations using varying economic assumptions).

5. How Far Into the Future?

Finally, Gokhale and Smetters use an infinite horizon rather than the 75-year horizon that is the norm in such analyses. As they point out, their model predicts a Social Security gap of $1.6 trillion over the 75-year horizon, compared to an infinite-horizon gap of $7 trillion, while the 75-year Medicare gap is $15.1 trillion, compared to the $36.6 trillion in their infinite-horizon model.\footnote{Gokhale & Smetters, note 1, at 3, 34.} In other words, over 60% of the fiscal gap occurs from 2078 through infinity. Prescribing policy initiatives for current lawmakers on the basis of such long-term projections borders on being arbitrary.

In short, the fiscal gap and generational accounts are generally not useful in guiding policy, because they are based on highly questionable forecasts, they ignore the effects of likely future political decisions, and they are far too easy to manipulate. Moreover, they cannot meaningfully compare the relationships among generations in how they share the cost of running the federal government, at least in a way that is different from the standard crowding-out approach. While the exercise of measuring fiscal gaps is based on a reasonable desire to see what we might be getting ourselves into, the mechanisms for such long-term forecasts are simply too crude to add meaningfully to our arsenal of policy choices.\footnote{Arguably, the lesson to be drawn from an exercise like that of Gokhale and Smetters is that the news is good; that is, other than the more general question of how to handle health care costs (both inside and outside of Medicare), we apparently do not face significant long-term budget problems. If so, then the exercise is worthwhile in a negative sense. Still, there are less favorable assumptions that could make the fiscal gap calculation look worse, especially the extension of the 2001 and 2003 tax cuts and the elimination or indexation of the AMT, and those assumptions are subject to all of the uncertainties described here. If fiscal gap calculations are to be but one piece of information among many, therefore, they at least should not be given the prominence that Gokhale and Smetters would give them.}
long-term estimates available at least will be useful in the situation where any plausible set of assumptions shows that current policies will lead to huge future fiscal imbalances. The more robust these long-term estimates are to varying assumptions, the more seriously we should take them. The current fiscal gap estimates, though, as dramatic as they may seem, do not add meaningfully to knowledge of how wrong-headed our current fiscal policies are. The problems arising from deficits estimated over the 10-year horizon should be more than enough to give reasonable policymakers pause.156

VI. WHAT DOES IT MEAN TO BE FAIR TO FUTURE GENERATIONS?

The unspoken assumption in this discussion is that the government should never make decisions that would reduce economic well-being in the future. Even if one completely agrees that the measurement problems discussed above must be addressed, one is still proceeding from the assumption that a decision is bad per se if it would reduce the level of real goods and services available to future generations.

The policy regime that fiscal gap/generational accounting analysis implies is thus clear: immediate fiscal contraction, austerity, and pain. The positive spin is that the pain can be “shared.” Two somewhat inconsistent norms are offered in designing policies to redress the long-term imbalances.

A. The Norms of Generational Equality vs. Shared Sacrifice

The most obvious norm, upon which Kotlikoff and his co-authors explicitly rely, is simple cross-generational equality of tax rates.157 Every generation should pay a lifetime net tax rate no higher than the last. Other than symmetry, though, there is no apparent philosophical imperative behind this norm. Indeed, since the notion of lifetime net tax rates tells us nothing about real after-tax living standards, there is no obvious reason to be concerned about lifetime net tax rates at all.

Recognizing this, Shaviro argues for a shared sacrifice norm rather than equal tax rates. “With respect to generational distribution, once

156 See Gale & Orszag, note 19, at 105 (“For example, to pay for the tax cuts in 2014 would require a 45 percent reduction in Social Security benefits, a 53 percent cut in Medicare benefits, or changes of a similar magnitude.”). While Gale and Orszag’s paper also presents long-term fiscal gap projections, id. at 110-12, the extra information that those projections provide is marginal at best. At the very least, it is difficult to imagine how estimates of problems arising in 2080 or beyond would spur a policymaker who was not moved to action by the 10-year estimates.

157 See Diamond, note 14, at 604 (discussing the idea of generational balance with regard to government action as the foundation for the work of Auerbach, Gokhale, and Kotlikoff).
the members of a given age cohort have died, they can no longer be asked to share in the pain of tax increases or benefit reductions."158 In other words, it is important to take the benefits away from the old people now because they are alive now. While there are certainly colorable (but highly debatable) arguments that the elderly overconsume,159 the current elderly also have a strong argument that they earned it.

B. How Much Is Enough?

It is possible, as noted earlier, that even a decision by the government to consume economic resources rather than to invest them will not harm future economic prospects. This will happen if the resources that the government purchases for its use would have been used to produce private consumption rather than private investment. Conceptually, if the government throws a wild party by hiring the people who would have worked at a privately-funded wild party, future generations are unaffected. It is only if computer programmers and construction workers (at least indirectly) staff the government’s party that the future productive capacity of the economy is reduced.

This, however, still leaves open the question of why we must maximize what we pass on to our heirs. Given that economic growth is generally on an upward trend, why is it necessary to give our wealthy grandchildren even greater wealth? The bipartisan (within the economics profession as well as among politicians) silence on this question is notable, to say the least. While there have been preliminary attempts to estimate how much capital should be produced for future generations,160 the unspoken norm is quite blunt: We should not do anything to reduce the standard of living that we bequeath to our children and grandchildren from the higher level that we already have guaranteed them.

The assumption that future generations are entitled to “their” share is tendentious. The higher living standard that future generations will enjoy arises from productivity gains that are themselves largely the results of technological innovations for which those future generations will not be responsible. If workers in the automated plant of 2030 can be expected to produce many more widgets per hour than their 2005 predecessors thanks to the invention of a robot in 2005, it is hardly

158 Shaviro, Medicare, note 15, at 100.
159 See Cohen, note 14, at 2236-46.
160 See N. Gregory Mankiw, Macroeconomics 111-12 (4th ed. 2000) (showing preliminary calculation intended to suggest that “policymakers should want to increase the rate of saving and investment.”).
clear that the 2030 workers are entitled to all the fruits of this productivity gain, even on Lockean premises. Shaviro offers an interesting defense of favoring (richer) future generations, on utilitarian grounds.\textsuperscript{161} He suggests that, precisely because future generations are likely to have higher standards of living, they might value a marginal dollar more highly than we currently do.\textsuperscript{162} While thought-provoking, this argument is simply a variation on the notion of “utility monsters,” that is, rich people whose subjective enjoyment from increased consumption is so much greater than other people’s enjoyment that a utility-maximizing social planner would continue to shift consumption to them from poor people because the monsters’ increase in happiness is, in the aggregate, worth it. Redistribution from poor to rich, under such an assumption, would increase total utility.

This argument, while innovative, is simply too conjectural to guide policymakers. If we are to start redistributing upward because rich people might like consumption more than poor people do, then we can redistribute to any favored group for the same reason. More importantly, as Shaviro concedes, this argument provides no way to measure how much is enough.\textsuperscript{163} Even if we were to agree that future generations’ ability to enjoy their wealth might be relatively high, that does not tell us that every policy that results in smaller increases in GDP is a utilitarian loss.

Perhaps it is time, therefore, at least to question that assumption. (Moreover, although the subject for a different essay, it is equally important to account for the “intergenerational unfairness” created by problems such as environmental damage.) Although many analysts (including the current author) would be unlikely to call for policies that would absolutely decrease future living standards, there is still plenty of room for debate regarding how much of an increase is enough.

\textbf{C. The Real Intergenerational Issues}

The very language of intergenerational transfer is, therefore, potentially misleading. Indeed, it is not possible to “pass the bill to future generations” for current spending.\textsuperscript{164} When the government uses eco-
nomic resources, the rest of the economy currently cannot use those resources. (This, of course, assumes that those resources were going to be used at all. Given the prolonged slack in the global economy, even that assumption is often contestable.) That means that we pay for what we do, in the fundamental sense of opportunity cost.

These decisions, of course, affect future generations too. If, as discussed earlier, the government's decisions are likely to decrease the net capital stock passed on to future generations, then their output will be lower than it otherwise would be. Therefore, the best approach is to think about how the government is using current resources. If it is investing them, then future generations will benefit. If it is consuming them (or simply wasting them), then they will not.

Even more fundamentally, it is not at all obvious that cutting benefits to seniors today will hurt only seniors. When the elderly lose benefits, they may turn to their children to make up the difference. Even if they do not do so directly, they can consume more of their estate than they otherwise would have, thus reducing the wealth of their children. This incidence question indicates just how difficult it is to measure meaningfully the impact on different generations of fiscal policies.

VII. Conclusion

The traditional debate about budget deficits witnessed a divergence between the economic analysis, which saw that deficits are poorly measured in the United States and argued that certain deficits are actually beneficial for the economy, and the political view that every deficit is evidence of moral failure. This peculiar stalemate is currently on hold, as the brief era of surpluses gave way to the (hopefully even more brief) era of terror and war, leading to a decreased emphasis on fiscal orthodoxy and tolerance for relatively high annual deficits into the foreseeable future—even though most of those deficits are not related to terrorism or war.

In place of a debate over our general fiscal status, political leaders currently focus on the supposed long-term problems faced by the Social Security system. While a need ultimately might rise to make some adjustments to future Social Security benefits and tax rates, the evidence available to this point does not call for immediate action but rather cautious monitoring of future developments.

In addition, an alternative approach to budgeting, the computation of fiscal gaps and generational accounts, has emerged over the last 15 years. Designed to correct some of the analytical weaknesses of annual budgeting and to extend to the entire budget the long-term analysis usually associated only with Social Security projections, fiscal gap/
generational accounting purports to provide an early-warning system that permits a correction to broader long-term fiscal imbalances before it is too late. Unfortunately, as appealing as this approach is in theory, it is based on highly contestable assumptions, makes questionable analytical choices, and is inherently incapable of providing the useful baseline that its proponents promise. While long-term estimates of huge fiscal imbalances obviously must not be ignored out of hand, the sensitivity of those estimates to highly volatile assumptions undermines the case for responding to the current estimated fiscal gap.

Perhaps surprisingly, then, the best response is for policymakers to continue to rely on the current (admittedly imperfect) budget measures, which at least provide some useful guidance regarding the immediate and intermediate effects of our fiscal policies. Annual and 10-year forecasts of deficits are admittedly arbitrary, but they tell us what today's politicians are committing us to over time horizons that permit relatively reliable measurement. While it is always wise to look at all of the available evidence, current policy is not well measured or guided by long-term fiscal policy estimates.