America's Ticking Bankruptcy Bomb

Testimony of

Peter Ferrara
Senior Fellow for Entitlement and Budget Policy
The Heartland Institute

Author of
America's Ticking Bankruptcy Bomb
(New York: HarperCollins, 2011)

Before the
Small Business Committee
United States House of Representatives

February 1, 2012

Even President Obama's own 2011 budget projected that by 2012 the national debt held by the public will have more than doubled in only 4 years, to $11.9 trillion from 5.8 trillion in 2008 That alone means that in just one term of office, President Obama will have accumulated more national debt than all prior Presidents combined, from George Washington to George W. Bush. By 2021 the national debt held by the public will have more than tripled since 2008 to $19 trillion, again under President Obama's own projections.

By the end of 2010, the national debt had already reached 62% of GDP, higher than at any time in our history except for World War II and shortly thereafter.[1] By 2023, CBO projects that under current policies the national debt held by the public will grow past 100% of GDP,[2] which means the federal government will owe more than our entire economy produces in a year. These projections assume that the 2009 stimulus spending is not continued, and consequently that federal spending outside of entitlements and debt interest is cut permanently by 16% as a percent of GDP.[3] The U.S. Government Accountability Office (GAO) presents an alternative fiscal simulation based on the best work of the government's own actuaries which projects that by 2020 the national debt held by the public will exceed even the World War II historical peak of 109% of GDP.[4]

But it gets worse. Even President Obama's budget projects that the federal government's Gross Federal Debt, which includes such items as the debt held in the Social Security trust funds (real debt that will have to be paid in the future), would be over $26.3 trillion by 2020, or 110% of GDP. It will be even worse than that, because that estimate is based on phantom budget cuts and inflated growth estimates. The Bank for International Settlements (BIS) estimates that this Gross Debt will accelerate faster, hitting 200% of GDP by 2022, and 300% by 2030.[5] The federal debt ceiling, or debt limit, we often hear about in the news applies to this Gross Federal Debt, which was $13.7 trillion as of September 30, 2010,[6] rising rapidly at the start of 2011 to the then federal debt limit of $14.3 trillion.

Under current policies, CBO projects that even the smaller national debt held by the public, as opposed to the Gross Federal Debt, would rocket to 185% of GDP by 2035,[7] and to 200% by 2037,[8] twice as large as our entire economy. This national debt would explode further to unprecedented levels of 233% of GDP by 2040, and to 854% by

---

[1] Congressional Budget Office, The Long Term Budget Outlook, June, 2010, pp. 1, 13.
[2] Id, p. 6.
[3] Id., p. 12.
[4] U.S. Government Accountability Office, The Federal Government's Long Term Fiscal Outlook: Fall 2010, GAO-11-201SP, December, 2010. CBO projects the national debt will exceed the World War II historical peak by 2025.
[5] Nicholas Eberstadt and Hans Groth, "Time for Demographic Stress Tests," *The Wall Street Journal*, November 27-28, 2010, p. A17; Stephen G. Cecchetti, M.S. Mohanty and Fabrizio Zampolli, The Future of Public Debt: Prospects and Implications, BIS Working Papers No. 300, Bank for International Settlements, March 2010, p. 10.
[6] United States Department of the Treasury, 2010 Financial Report of the United States Government, December 21, 2010, pp. vi.
[7] Id., p. 1.
[8] Id., pp. 6, 14.

2080.[9] As Erskine Bowles, Co-Chairman of President Obama's Deficit and Debt Commission and White House Chief of Staff under President Clinton, has said, "This debt is like a cancer that will destroy the country from within."

An international study for the National Bureau of Economic Research by Kenneth Rogoff of Harvard and Carmen Reinhart of Maryland, covering the experience of 44 countries over 200 years, found that economic growth slows substantially when national debt climbs over 90% of GDP.[10] In 2009 the national debt of Greece reached 115% of GDP. Within a year, the international markets refused to lend the Greek government any more money by buying its government bonds. That meant that Greece could not borrow the money to finance its budget deficit, sparking the Greek/Euro crisis. That resulted in a trillion dollar bailout from the European Union (EU), financed by EU taxpayers.

America is almost at this same disastrous level of debt as Greece, and on our current course we will soon be there. Indeed, on our current course we will rocket right through that level, and well beyond.

But the national debt is just the starting point for toting up everything the government owes, or may owe. The unfunded liabilities of Social Security and Medicare together run up to over $100 trillion according to the government's own actuaries.[11] The so-called trust funds for Social Security and Medicare provide exactly zero help in financing those long term liabilities. The Social Security trust funds are reported to hold close to $3 trillion in assets. But those assets are all special issue government bonds which just represent still more government debt, more accurately viewed as internal federal IOUs.

In reality, and as a matter of federal law, the Social Security trust funds are nothing more than a statement of the legal authority that Social Security has to draw from general revenues, meaning ultimately you the taxpayer, when the money is needed to pay benefits. That is why all the "assets" in the Social Security trust funds are actually included in the federal government's Gross Federal Debt, subject to the debt limit.

In addition, there are the further unfunded liabilities for federal military pensions, promised veterans benefits, and the retirement benefits for federal civil service workers. The FDIC is responsible for trillions in guarantees of government insured deposits, the FHA is liable for another trillion dollars of home mortgage insurance guarantees, and the National Flood Insurance Program is responsible for over a trillion in outstanding coverage, with nothing of significance to back it up.

Then there are all the guarantees piled up by the TARP and other bailouts over the past few years. As of September 30, 2010, the Treasury still held close to $200 billion in

---

[9] Committee for a Responsible Federal Budget, CBO's Long Term Budget Outlook, July 1, 2010, p. 1.
[10] Carmen M. Reinhart and Kenneth S. Rogoff, Growth in a Time of Debt, National Bureau of Economic Research, Working Paper 15639, January, 2010.
[11]

outstanding direct loans and stock investments due to the TARP bailouts.[12] Altogether the Treasury held nearly $1 trillion in net loans receivable and stock equity interests, including 33% of the stock of General Motors,[13] 10% of the stock in Chrysler,[14] $42 billion (80%-90%) of AIG stock,[15] and over $100 billion in the stock of Fannie Mae and Freddie Mac.[16] Fannie Mae and Freddie Mac alone hold $4.4 trillion in mortgage backed securities (MBS's), with another $1.4 trillion in debt not counted in the national debt.[17] The Federal Reserve, the FHA and the U.S. Treasury hold trillions more in MBS's and federal guarantees of those toxic securities that were at the root of the financial crisis.[18] The federal bailout of Fannie Mae and Freddie Mac has already cost $150 billion, projected to rise ultimately to half a trillion.[19]

Total federal loan guarantees have now climbed close to $2 trillion. The face value of federal loans outstanding in 2010, including education, agriculture, housing and other loans, reached over $700 billion.[20] With long term near double digit unemployment, those education loans are now particularly risky. The federal government is also responsible for an estimated $320 billion in environmental cleanup costs for federal properties required under current law.[21] All these liabilities are in addition to the national debt discussed above.

Thoroughly wrong headed Obamacare just adds further trillions to all these liabilities, as discussed further below. The additional unfunded liabilities of state and local governments are also on top of the national debt discussed above. That includes over $3 trillion in municipal bond and state level debt, close to $4 trillion in unfunded state and local pension liabilities, and over one trillion more in completely unfunded retirement health benefits promised to state and local employees.

Most people do not know that since soon after World War II federal spending as a percent of GDP has been fairly stable at around 20%, until recently. That covers a period approaching two-thirds of a century. All of the great debates, the political crusades left and right, the liberal War on Poverty, the steady rise of the entitlements, the Reagan revolution, the Clinton sellout of the Left, the Bush sellout of the Right, amounted to

---

[12] United States Department of the Treasury, 2010 Financial Report of the United States Government, December 21, 2010, pp. vii,6,69,71,74,84; Statement of the Acting Comptroller General of the United States, U.S. Government Accountability Office (GAO), December 21, 2010, pp. 4.
[13] Id., p. 6.
[14] Id., p. 71.
[15] Id., p. 69,74.
[16] Statement of the Acting Comptroller General of the United States, U.S. Government Accountability Office (GAO), December 21, 2010, pp. 4; United States Department of the Treasury, 2010 Financial Report of the United States Government, Notes to the Financial Statements, December 21, 2010, p. 84.
[17] Congressional Budget Office, Federal Debt and Interest Costs, December, 2010, p. 2.
[18] Statement of the Acting Comptroller General of the United States, U.S. Government Accountability Office (GAO), December 21, 2010, p. 5. United States Department of the Treasury, 2010 Financial Report of the United States Government, December 21, 2010, p. 82.
[19] United States Department of the Treasury, 2010 Financial Report of the United States Government, December 21, 2010, pp. vii, 14-15, 56, 83.
[20] Id., p. 64.
[21] Id., p. 97.

holding federal spending in equipoise during this entire period, growing in the end no faster than our enormously productive economy during this time.

That crashing sound you hear is the collapse of this long term grand compromise, which until recently has allowed our economy to continue to soar ahead with world leading prosperity. Official U.S. government projections have shown for some time now that over the next 30 to 40 years federal spending as a percent of GDP will double to 40% or more. Financing that would ultimately require at least doubling every federal tax. Add in continued state and local spending growing towards 15 percent of GDP, and government in America will consume more than half of the economy. Much more than half in the end, because under that burden GDP growth will collapse, leaving the government share an even higher percentage of a shrunken GDP.

This would fundamentally transform America into a static, low growth, socialist European state. America's traditional world leading prosperity and opportunity, the American Dream, would be gone.

President Obama has only accelerated these developments, with federal spending on our current course now targeted to hit 26% of GDP by 2021. The driving factors in the long term fiscal demise of traditional American prosperity are the nation's entitlement programs – Social Security, Medicare, Medicaid and the dozens of other federal, means-tested welfare programs, and now Obamacare.

As discussed in this testimony, these multiplying, entitlement, dead weight anchors not only threaten America's future solvency and prosperity, they counterproductively fail the poor, low income and senior populations they are supposed to help, and directly contribute to America's economic decline today. The joint federal/state welfare empire crushes work and the family unit among those in the bottom 20% in incomes. Obamacare, Medicaid, and now Medicare mangled by Obamacare promise the destruction of the world leading top quality health care that has long been fundamental to America's high standard of living. Obamacare in addition imposes another trillion dollars in economically counterproductive taxes, plus the job killing employer mandate, effectively another burdensome tax. Social Security promises today's working people a miserable return on their lifetime of burdensome tax payments, and deprives the economy of mighty rivers of savings and investment that would rocket ahead America's world leading prosperity into the 21st century.

But there is good news, if we would just think anew. As I show in detail in my recent book, *America's Ticking Bankruptcy Bomb*[22], by modernizing our old fashioned, tax and redistribution entitlement programs to rely on 21st century capital, labor and insurance markets instead, we can achieve all of the social goals of these entitlement programs far more effectively, serving seniors and the poor far better, at just a fraction of the current cost of those programs. Such reforms would involve powerful market incentives driving the programs to contribute further to booming economic growth and prosperity, rather than detract from it.

[22] Peter Ferrara, *America's Ticking Bankruptcy Bomb* (New York: HarperCollins, 2011)

Ultimately, these reforms altogether would reduce federal spending by half or more of what it would be otherwise, solving the long term fiscal problem. Yet, because these reforms involve fundamental structural changes that actually serve the poor and seniors far better, rather than simple-minded benefit cuts (the political equivalent of the Charge of the Light Brigade), they are politically feasible. Modernizing the programs to the remarkable benefit of the populations they serve, which the book shows is possible by harnessing markets and incentives to achieve the social goals of the programs far more effectively, is the political key to unlock the door to the necessary entitlement reform.

The Welfare Empire

The term "welfare state" is inadequate to describe America's means tested welfare complex targeted to the poor. What we have is a welfare empire involving 185 joint federal/state means tested welfare programs, including Medicaid, Food Stamps, 27 low income housing programs, 30 employment and training programs, 34 social services programs, another dozen food and nutrition programs, another 22 low income health programs, and 24 low income child care programs, among others.

Federal and state governments spend close to a trillion dollars a year just on these means tested welfare programs[23], not counting Social and Medicare. That is roughly $17,000 per person in poverty, over $50,000 for a poor family of three. The Census Bureau estimates that our current welfare spending totals four times what would be necessary just to give all of the poor the cash to bring them up to the poverty line.[24] Charles Murray wrote a whole book, *In These Hands*, documenting that we spend far more than enough to completely eliminate all poverty in America.[25] This dramatic overspending leaves wide scope for reforms that would be far more effective in reducing poverty, while still saving taxpayers a fortune.

The War on Poverty famously began in 1965. From 1965 to 2008, the total spent only on means tested welfare for the poor in 2008 dollars has been nearly $16 trillion.[26] Rector et al. report that has been more than twice all spending on all military conflicts from the American Revolution to today.[27]

What have we gotten for all of that spending? Poverty fell sharply after the Depression, before the War on Poverty. The poverty rate fell from 32% in 1950 to 22.4% in 1959 to 12.1% in 1969, soon after the War on Poverty programs became effective. Progress against poverty as measured by the poverty rate then abruptly stopped. In 2009, the U.S. poverty rate stood at 14.3%, about where it was right after the War on Poverty

---

[23] Robert Rector, Katherine Bradley, and Rachel Sheffield, Obama to Spend $10.3 Trillion on Welfare: Uncovering the Full Cost of Means-Tested Welfare or Aid to the Poor (Washington, DC: The Heritage Foundation, 2009)
[24] Ibid, pp. 15-16.
[25] Charles Murray, *In Our Hands, A Plan to Replace the Welfare State* (Washington, DC: American Enterprise Institute, 2006)
[26] Rector et al., p. 12.
[27] Id.

began, despite the expenditure of $16 trillion. In other words, we fought the War on Poverty, and poverty won.

One major reason that poverty stopped declining after the War on Poverty started is that the poor and lower income population stopped working. In 1960, nearly two-thirds of households in the lowest income one-fifth of the population were headed by persons who worked.[28] But by 1991, this work effort had declined by about 50%, with only one-third of household heads in the bottom 20% in income working, and only 11% working full-time, year round.[29]

This was not a matter of the poor not being able to find work. While the economy was chaotic during the 1970s, during the 1980s and 1990s America enjoyed an historic economic boom creating millions of jobs. The proof is in the pudding, or in how people actually voted with their feet. Millions of illegal aliens surged across the border to gain those jobs and participate in America's economic golden age, with the unemployment rate collapsing into insignificance by the end of the 1990s.

With the government offering such generous and wide-ranging benefits, from housing to medical care to food stamps to outright cash, and many others, to those with low incomes or who are not working at all, naturally many choose to reduce or eliminate their work effort and take the free benefits. Incentivewise, it is as if the government is generously paying people not to work and to have low incomes.

But along with this collapse of work, the War on Poverty was also associated with the breakup of lower income families, and soaring illegitimacy. Prior to the War on Poverty, black families remained intact, and the overwhelming majority of black babies were born to 2 parent families. But coinciding with the War on Poverty, the black illegitimacy rate soared from 28% in 1965, to 49% in 1975, to 65% in 1990, to about 70% in 1995, where it remains today.[30] This effect has not been limited to blacks. Among whites, illegitimacy soared from 4% in 1965, to 11% in 1980, 21% in 1990, and 25% in 1995, where it also remains today. Among white high school dropouts, the illegitimacy rate is 48%. Among Americans overall, the illegitimacy rate has soared from 7% when the War on Poverty began to 39% today.

Such illegitimacy is the second key cause of poverty, in addition to nonwork. The poverty rate for female headed households with children is 44.5%, compared to 7.8% for married couples with children. The poverty rate for married black Americans is only 11.4%, while the rate for black female headed households is 53.9%. Moreover, it is primarily these single parent families that remain poor and dependent on welfare for the long term. Indeed, single parent families perpetuate poverty into the next generation.

---

[28] U.S. Bureau of the Census, Current Population Reports, Series P-60, No. 80, Income in 1970 of Families and Persons in the United States, p. 26.
[29] U.S. Bureau of the Census, Current Population Reports, Series P-60, No. 180, Money Income of Households, Families, and Persons in the United States: 1991, p. 7.
[30] The illegitimacy rate is officially reported by the National Center for Health Statistics; See also, Jason L. Riley, "The State Against Blacks: The Weekend Interview with Walter Williams," *The Wall Street Journal*, January 23-23, 2001, p. A13.

Children raised in single parent families are 7 times more likely to become welfare recipients as adults. The negative effects on children from single parent families, and crime resulting from illegitimacy, also perpetuate poverty long term. As Robert Rector of the Heritage Foundation explains, "If poor women who give birth outside of marriage were married to the fathers of their children, two-thirds would immediately be lifted out of poverty. Roughly 80 percent of all long-term poverty occurs in single-parent homes."[31]

Family break up and illegitimacy are again the natural result of the incentives created by our massive, overgrown welfare empire. Most welfare benefits are restricted to families with children. If you are a non-elderly adult in America without children, you are pretty much expected to support yourself. That is a sound principle. But it means that having a baby is the gateway to a generous package of government benefits.

Moreover, if the mother is married to a man who earns a significant income, then the benefits are lost. Indeed, if the mother is married to a man who is not working, but the government requires him to take available work before benefits are paid, then the benefits will be lost in any event, whether he refuses to work, or if he works and earns an income that eliminates benefits.

Once again, it is as if the government is paying women to have children out of wedlock. As Rector aptly puts it, "Welfare ...converts the low-income working husband from a necessary breadwinner into a net financial handicap. It transformed marriage from a legal institution designed to protect and nurture children into an institution that financially penalizes nearly all low-income parents who enter into it."[32]

<u>Winning the War on Poverty</u>

But an historic turning point in welfare policy was achieved with the enormously successful 1996 reforms of the old Aid to Families with Dependent Children (AFDC) program. Those reforms, spearheaded by then Speaker of the House Newt Gingrich, implemented the ultimate welfare policies favored by President Reagan and his long time welfare guru Robert Carleson, as explained in Carleson's recent posthumously published book *Government* Is *The Problem: Memoirs of Ronald Reagan's Welfare Reformer*.[33] (I worked directly for Carleson in the Reagan White House).

The reform returned the share of federal spending on the AFDC program to each state in the form of a "block grant" to be used in a new welfare program redesigned by the state based on mandatory work for the able bodied. Federal funding for AFDC previously was based on a matching formula, with the federal government giving more to each state the more it spent on the program, effectively paying the states to spend more. The key to the 1996 reforms was that the new block grants to each state were finite, not

---

[31] Rector, et al., p. 25.
[32] Rector, supra, p. 201.
[33] Susan A. Carleson and Hans A. Zeiger, *Government Is the Problem: Memoirs of Ronald Reagan's Welfare Reformer* (Alexandria, VA: American Civil Rights Union, 2009)

matching, so the federal funding did not vary with the amount the state spent. If a state's new program cost more, the state had to pay the extra costs itself. If the program cost less, the state could keep the savings.

To give the states broad flexibility in designing the new replacement program, the entitlement status of AFDC was repealed, as states could not be free to redesign their programs if their citizens were entitled to coverage and benefits as specified in federal standards. The reformed program was renamed Temporary Assistance to Needy Families (TANF).

The reform was opposed bitterly by the liberal welfare establishment. Their view was well expressed by Senator Daniel Patrick Moynihan, the Urban Institute, and others who predicted that the reforms would produce a "race to the bottom" among the states, and that within a year a million children would be subject to starvation.

But quite to the contrary, the reform was shockingly successful, exceeding even the predictions of its most ardent supporters. The old AFDC rolls were reduced by two-thirds nationwide, even more in states that pushed work most aggressively: Wyoming (97%), Idaho (90%), Florida (89%), Louisiana (89%), Illinois (89%), Georgia (89%), North Carolina (87%), Oklahoma (85%), Wisconsin (84%), Texas (84%), Mississippi (84%). By 2006, the percent of the population receiving TANF cash welfare was down to 0.1% in Wyoming, 0.2% in Idaho, 0.5% in Florida, 0.6% in Georgia, Louisiana, North Carolina, and Oklahoma, and 0.7% in Arkansas, Colorado, Illinois, Nevada, Texas and Wisconsin. Nationwide, the percentage of American children on AFDC/TANF was reduced from 14.1% in 1994 to 4.7% in 2006.

As a result, in real dollars total federal and state spending on TANF by 2006 was down 31% from AFDC spending in 1995, and down by more than half of what it would have been under prior trends. At the same time, because of the resulting increased work by former welfare dependents, the incomes of the families formerly on the program rose by 25%, and poverty among those families plummeted. Haskins reports, "[B]y 2000 the poverty rate of black children was the lowest it had ever been."

This illustrates the entitlement reform theme of the book that through fundamental structural reforms we can achieve the social goals of those programs far more effectively, ultimately serving seniors and the poor far better, at just a fraction of the costs of the current old-fashioned programs.

There was only one problem with the 1996 reforms – they only reformed one program. The same reforms can and should be extended to all of the remaining 184 federal means tested welfare programs. This would amount to sending welfare back to the states, achieving the complete welfare reform dream of Reagan and Carleson in restoring the original federalism and state control over welfare. It also follows the spirit of the Tea Party movement in restoring power to the states and gaining control over government spending, deficits and debt.

I discuss in the book how the states should use their newly restored powers to adopt an entirely new welfare system for the able bodied providing benefits only in return for work first. Those who were disabled or retired and so couldn't be expected to work would be assisted through separate programs. But otherwise the nation's local welfare offices would be turned into work offices. Those who reported for work early enough in the day would be assured a work assignment for that day, preferably in the private sector as temp agencies arrange for their customers, but if necessary doing some work task serving the community in some way, city, county or state.

They would be paid in cash at the minimum wage at the end of the day. If they needed more money, they could come back tomorrow. All forms of assistance would be provided to the able bodied only in conjunction with this work. Child care would be provided on site, those who reported for work consistently enough could be given vouchers to help pay for health insurance, necessary transportation assistance could be provided to get to the work office, etc.

The book shows that the minimum wage, plus the Earned Income Tax Credit (EITC), plus the Child Tax Credit are enough by themselves to bring every family out of poverty with full time employment at such work. But much of this cost would be borne by private employers paying the wages in return for work.

Indeed, the incentives of this system would push most of the costs to the private wage paying employers, instead of the taxpayers, because this system eliminates the work disincentives of welfare. Rather, the incentive is to take whatever private sector job is available, since the able bodied will have to work to support themselves in any event, and in the private sector the worker will gain skills, raises, promotions, and new opportunities over time. Those who do show up for the work assignments anyway would be assigned to private employers as well to the extent possible, and those connections would likely grow into long term employment. In any event, no one is going to keep showing up for these day jobs for years, like some stay on welfare for years.

Consequently, instead of taxpayers paying the bottom 20% in income not to work, as today, employers would be paying them to work. As a result, the bottom 20% would be contributing to the economy, rather than detracting from it by staying home idle and living off the work of others.

The welfare incentives for family breakup and illegitimacy are also eliminated entirely. No free benefits are handed out any longer for bearing a child out of wedlock. If the mother has a child without a husband, then the mother must go to work to support the child. Moreover, there is nothing to be gained under this system by avoiding marriage or by couples splitting up. No benefits are provided to the mother for being unmarried. A government welfare check does not become a substitute for a working husband. If the father has to work to support himself anyway, and will be charged for child support, then he has no economic incentive to stay away from the family either. So this system does not discourage marriage or encourage family break up.

To the contrary, since living together will reduce living expenses that the couple will have to work to pay for in any event, the incentives are for family unification rather than family breakup. Couples staying together can also help each other by sharing the necessary work if they desire. Indeed, a single mother can avoid work altogether by marrying a working husband. So the system provides reinforcing economic incentives for marriage search.

With all the programs of the current welfare empire estimated together to cost $10 trillion over the next 10 years, the resulting savings to the taxpayers would be several trillion just in those first 10 years alone. Indeed, while substantial costs would remain for a program like Medicaid, the above incentives I argue would likely drive down costs for most of the remaining programs by more than half. But at the same time, poverty in America would actually be effectively eliminated, with all able bodied people assured of work earning sufficient income to climb above the poverty line.

<u>Obamacare versus Patient Power</u>

With the overwhelming burden of already badly overpromised entitlement programs threatening long term fiscal chaos and the end of America's traditional world leading prosperity, President Obama decided the top priority was to make the problem worse with Obamacare, which adopts or wildly expands three entitlement programs. While President Obama insisted Obamacare would not add to the federal deficit, the book explains why it will add $4 to $6 trillion in additional deficits and debt in the first 20 years of implementation alone. But that is not the biggest problem. Obamacare in any event needlessly adds trillions in additional spending and taxes to an already bursting federal ledger, and promises to decimate the world leading quality health care that has long been a central component of the high standard of living of the American people.

Obamacare was advanced to address two central problems, rapidly rising health costs and the uninsured. National health care costs have been growing faster than the economy for close to 100 years. But that cost growth accelerated over the past 50 years, soaring from 5 percent of GDP in 1960 to 10 percent in 1985 to 17 percent in 2009. That is the highest proportion of output devoted to health care of any country in the world, by far. Second is France at 11.2% of GDP, followed by Switzerland at 10.7%. Germany spends 10.4%, the United Kingdom only 8.7%. The OECD average is 9%.

Since we still have the biggest economy in the world by far, that means we spend far more on health care than any other country in the world. U.S. health costs totaled $2.5 trillion in 2009, larger than the entire economies of every other country in the world except China, Japan, Germany, and France. Per person, we spent $7,538 on health care in 2008, again higher than any other country by far. That was 50% more than the second most, Norway, at $5,003, with Switzerland in third at $4,627. Germany only spent half as much, at $3,737 per person, and the United Kingdom less than half at $3,129. The OECD average was less than half as well, at $3,060.

These trends are expected to continue. CBO projects that on our current course by 2040 health care costs would consume close to one-third of GDP.

The root of these rapidly rising health costs is what economists have called the Third Party Payment problem. The great majority of health costs in America are not paid by the patients themselves. There is almost always some third party paying the bills, either an insurance company, an HMO, or the government through programs such as Medicare and Medicaid. Indeed, in 2008, 84% of health expenses in America were paid for by private health insurance, Medicare, Medicaid, or other public spending.

Try this thought experiment. Consider sending your teenage daughter to the mall on a Saturday with a debit card for a bank account with $1,000 in it. Tell her that what she doesn't spend today she can keep for the future, with interest, to spend later. Then consider sending her to the mall with Uncle Sam's credit card. Tell her you effectively have already paid for whatever she might charge through your income taxes. How do you think the magnitude of what she purchases would differ?

The fundamental problem, of course, is that with a third party paying the bills, the consumer, or the patient, has no incentive to control costs. In formal terms, the consumer has an incentive to spend until the marginal benefit of additional spending, or additional health care is zero, so different from an efficient market, where consumers spend until the marginal benefit is equal to the marginal cost. In more colloquial terms, this means consumers have the incentive to spend on health care until it hurts.

To make matters worse, consumers lack expertise in health care, and make their health care purchases on the advice of their chosen doctors and specialists, who not only also have no incentive to control costs, but, rather, have a direct financial interest in spending more. The consumer doesn't even have an incentive to shop for the lowest cost care for what he does decide to consume.

This means, in turn, that health care providers have no incentive to compete to reduce costs, since consumers and patients are not making their health care decisions based on costs. They are making their decisions based primarily on quality, and secondarily convenience. That is why the American health care system produces far and away the highest quality health care in the world, resulting from highly effective capitalist competition, and traditional Yankee ingenuity in producing the latest and best innovations.

This also explains why new medical technology increases costs, while in every other field new technology drives down costs. Since in American health care there is only competition to maximize quality, regardless of costs, developers and innovators of new medical technology are focused primarily on increasing quality regardless of cost.

The only solution is to unite the decision over what health care to purchase and consume with the economic responsibility to pay the costs, so costs can be weighed against benefits in health care consumption. There are two alternative ways to do that.

Either the third party payer is given the power to decide what health care the consumer or patient is allowed to consume, in which case the third party payer weighs the costs of the patient's health care against the benefits to the patient from that health care. Or the patients are given market incentives to consider the full costs of the health care they choose to consume, in which case the patient weighs the personal benefits of his or her health care against the costs of that care.

Most countries have chosen the former alternative through socialized medicine. With the government taking primary responsibility for paying health expenses through its taxpayer financed health programs, the government takes primary responsibility for deciding what health care its citizens are allowed to consume and when. The government then decides to what extent each individual's health care is worth the costs.

This introduces its own perverse incentives, particularly to sacrifice to broader political calculations the interests of the sickest and most costly, always a small minority not nearly fully aware of the scope of possible medical alternatives. With the government and politics ultimately deciding who gets paid how much for what health care, incentives for investment to develop new medical technology, innovation, and breakthroughs are decimated. Finally, this system raises troubling moral issues, with the government effectively deciding in place of citizens whether their health care is worth the costs, and consequently who should live and who should die.

Though initially subtle and opaque, Obamacare creates the framework to take America down this road. That can be seen for starters in the $15 trillion in future cuts to Medicare payments to doctors an hospitals, and turning over the program to the democratically unaccountable Independent Payment Advisory Board.

The alternative has been dubbed Patient Power, after the pathbreaking book of that name by free market health guru John Goodman published by the Cato Institute in 1992. The classic example of such policy is Health Savings Accounts (HSAs).

The concept behind HSAs is to start with an insurance policy with a high annual deductible, in the range of $2,000 to $6,000 in today's products (the higher the better). Such high deductibles, of course, reduce the cost of the insurance substantially, with the savings then kept in the savings account to pay expenses below the deductible. Generally, after one healthy year with little or no medical expenses, the patient by the second year would have more than enough in the account to cover all expenses below the deductible. (And even if the patient has an unhealthy first year, the net out of pocket costs after using up the first year savings in the HSA is not much more than standard deductibles and copayments in traditional health insurance). Unspent HSA funds can be used for health expenses in later years, or for anything in retirement.

This transforms the incentives of third party payment. For all but catastrophic health expenses, the patient is essentially using his own money for health care. Whatever he doesn't spend he can keep. So the patient will try to avoid unnecessary care, and look for less expensive care and alternatives for what he does need.

In turn, since patients would now be concerned about costs, doctors, hospitals and other providers would now compete to control costs, as well as maximize quality, as in all normal markets. This competition would become more intense and effective the more widespread HSAs and similar incentives become. These incentives would flow all the way through to the developers of new technologies. Since both patients and health providers are now concerned with costs, technology innovators would now have incentives to develop technologies that reduce costs, as well as improve quality.

HSAs can be expanded throughout the health care system. Workers can be allowed the freedom to choose them in place of employer provided coverage, the poor can be allowed to choose them for their Medicaid coverage, seniors can be allowed to choose them for Medicare.

Similar policies would involve providing the poor through Medicaid with designated sums for the purchase of insurance coverage in competitive markets, resulting in incentives for cost saving choices among health insurance alternatives. That can be done with employer provided health insurance as well. The same can also be done for Medicare, as House Budget Committee Chairman Paul Ryan has proposed. A similar approach for the drug coverage of Medicare Part D proved quite successful in controlling costs. By contrast, President Obama's approach to Medicare emphasizes again the other alternative of expanded government control over the health care provided to seniors under Medicare through his Medicare cuts and Independent Payment Advisory Board, ominously exempted from democratic control. This is just one reason why Ryan's Medicare reforms are actually better for seniors than Obama's approach to Medicare.

Additional reforms would provide for complete Patient Power. The interstate sale of health insurance would maximize consumer choice, and competition, which would further reduce costs. Regulations that unnecessarily increase costs should be repealed. These include the thousands of state special interest benefit mandates, guaranteed issue, and community rating, as well as regulations that unnecessarily prevent new health providers from entering markets and increasing competition, such as certificate of need requirements mandating a showing of need for the services.

A Health Care Safety Net

In *America's Ticking Bankruptcy Bomb*, I discuss how Patient Power can be extended to provide a complete health care safety net covering everybody to assure that no one will suffer lack of essential health care, for just a small fraction of the cost of Obamacare. Moreover, this is accomplished with no individual mandate and no employer mandate. Obamacare, by contrast, for all of its trillions in future taxes and spending, and both its individual and employer mandate, still does not cover everyone.

Such reform would begin with Medicaid, which already spends over $400 billion a year providing substandard health care coverage for 50 million poor Americans. Congress should transform Medicaid to provide assistance to purchase private health insurance for all those who otherwise could not afford coverage, ideally with health insurance vouchers. This one step would enormously benefit the poor already on Medicaid. The program today pays doctors and hospitals only 60% of costs for their health care services for the poor. As a result, close to half of all doctors and hospitals won't take Medicaid patients. This is already a form of rationing, as Medicaid patients find obtaining health care increasingly difficult, and studies show they suffer worse health outcomes as a result. Health insurance vouchers would free the poor from this Medicaid ghetto, enabling them to obtain the same health care as the middle class, because they would be able to buy the same health insurance in the market.

Ideally this would be done by block granting Medicaid back to the states, as with the 1996 AFDC reforms discussed above. With finite block grants for Medicaid, states that innovate to reduce costs can keep the savings. States that operate programs with continued runaway costs would pay those additional costs themselves. The voters of each state can then decide how much assistance for the purchase of health insurance to provide each family at different income levels to assure that the poor would be able to obtain essential health care. This would rightly vary with the different income and cost levels of each state.

This would not cost much because only about 12 million Americans arguably cannot afford health insurance without some public assistance. Out of the 47 million uninsured we keep hearing about, 9.7 million are already eligible for current government programs like Medicaid or SCHIP but haven't signed up. Another 6 million are eligible for employer sponsored insurance but have not signed up for that either. Another 9 million are in families earning more than $75,000 per year. Another 10.2 million are immigrants, legal or illegal, and not U.S. citizens. Just give the assistance necessary, counting what they can reasonably pay based on their income, to the 12 million Americans that need it to buy private health insurance.

A second step necessary to ensure a complete safety net is to provide federal funding to help each state set up a High Risk pool. Those uninsured who become too sick to purchase health insurance in the market, perhaps because they have contracted cancer or heart disease, for example, would be assured of guaranteed coverage through the risk pool. They would be charged a premium for this coverage based on their ability to pay, ensuring that they will not be asked to pay more than they could afford. Federal and state funding would cover remaining costs. Such risk pools already exist in over 30 states, and for the most part they work well at relatively little cost to the taxpayers because few people actually become truly uninsurable.

The law already provides that insurers cannot cut off already existing policyholders, or impose discriminatory rate increases, because they become sick *while* covered. That would be like allowing fire insurers to cut off coverage for houses once they catch on fire. If this law needs to be modernized, it should be.

With these reforms, those who have insurance can keep it, those who can't afford it are given the necessary help to buy it, and those who nevertheless remain uninsured and then become too sick to buy it have a back up safety net in the risk pools. Everyone is assured of being able to get essential health care when they need it, with no individual or employer mandate.

The Medicaid block grants would likely cost less actually than Medicaid today, but serve the poor far better, and the High Risk pools involve only marginal additional costs. Obamacare, by contrast, was estimated by CBO to cost a trillion dollars a year, more likely $2 to $3 trillion as explained in the book. But with Patient Power, the patients themselves would enjoy maximized personal control over their own health care, with the current world leading quality of American health care maintained. So again, the people are served better, at just a fraction of the cost.

Moreover, once the decision over what health care to buy is united with market incentives to control costs in the patients themselves, then the people themselves can decide what percentage of GDP should be devoted to health care, through their collective decisions in the marketplace. The health cost problem would be addressed in the competitive marketplace, consistent with the preferences of the people themselves. The health care industry would then be a contributor to jobs and growth of the economy just like any other, rather than considered a net drain on the economy. Restraint of health costs consistent with consumer preferences would further contribute to economic growth.

Social Security Personal Account Prosperity

The Baby Boom is beginning now to retire on Medicare in earnest, with retirement on Social Security starting in a year or so. For decades now, the federal government's own official reports have been showing that Social Security would not be able to pay all promised benefits to the baby boom without dramatic, unsustainable tax increases.

Last year, for the first time since President Reagan saved the program in 1983, Social Security began running a cash deficit. Under what the government's actuaries call intermediate assumptions, those deficits will continue until the Social Security trust funds run out of funds to pay promised benefits by 2037. After that, paying all promised Social Security and Medicare benefits will require eventually almost doubling the current total payroll tax of 15.3% to nearly 30%.

Under what the government's actuaries call pessimistic assumptions, the Social Security trust funds will run out of funds to pay promised benefits by 2029. After that, paying all promised benefits to today's young workers would eventually require raising the total payroll tax rate to 44%, three times current levels, and ultimately more.

Social Security operates as a pure tax and redistribution system, with no real savings and investment anywhere. Even when it was running annual surpluses, close to 90% of the money coming in was paid out within the year to pay current benefits. Even the remaining annual surpluses were not saved and invested. They were lent to the federal government and spent on other government programs, from foreign aid to bridges to nowhere, with the Social Security trust funds receiving only internal federal IOUs promising to pay the money back when it is needed to pay benefits. Those federal IOUs are rightly accounted for in federal finances not as assets but as part of the Gross Federal Debt, subject to the national debt limit. That is because they do not represent savings and investment but actually additional liabilities of federal taxpayers.

Such a pay-as-you-go tax and redistribution system does not earn the investment returns that a fully funded savings and investment system would. Consequently, over the long run the system can only pay low, inadequate, below market returns and benefits. That is why studies show that for most young workers today, even if Social Security does somehow pay all its promised benefits, those benefits would represent a real rate of return of around 1% to 1.5% or less. For many, the real effective return would be zero or even negative. A negative rate of return is like putting your money in the bank, but instead of earning interest on it, you have to pay the bank for keeping your deposit there. That is effectively what Social Security is for many people today.

Moreover, on our present course, that is what Social Security will be for everyone in the future. Whether the long term deficit is closed ultimately by raising taxes or cutting benefits, that will mean the effective rate of return from the program will be lower, ultimately falling into the negative range for everyone.

There is a better way, proven to work in the real world. Workers could be allowed to save and invest what they and their employers would otherwise pay into Social Security in personal savings, investment and insurance accounts. Studies show that at standard, long term, market investment returns, for an average income, two earner couple, over a career the accounts would accumulate to close to a million dollars or more. Even lower income workers could regularly accumulate half a million over their careers.

Those accumulated funds would pay all workers of all income levels much higher benefits than Social Security even promises let alone what it could pay, two to three times as much, and possibly even more. Retirees would each be free to choose to leave any portion of these funds to their children at death.

Another virtue of these personal accounts is that with workers financing their own benefits through their own savings and investment, they can be free to each individually choose their own retirement age. Moreover, they would have market incentives to choose on their own to delay their own retirement ages as long as possible, because the longer they wait the more they would accumulate in their accounts, and the higher benefits those accounts could pay.

As a result, millions of workers with less physically taxing jobs would choose on their own to delay their retirement well into their 70s, a result that could never be imposed politically. But other workers whose jobs required heavy physical labor or who for other physical reasons could not work past their early 60s could retire then. With planning, they or their employers could make additional contributions to the accounts over the years to finance more benefits in that earlier retirement. This is a far superior solution to the question of the retirement age than politics imposing one, uniform, unworkable retirement age on all.

Proven to Work

In 2005, Congressman Paul Ryan (R-WI) and Senator John Sununu (R-NH) introduced comprehensive legislation providing for such a personal accounts plan, officially scored by the Chief Actuary of Social Security. Workers were empowered with the freedom to choose to save and invest in the accounts just half the Social Security payroll tax, roughly the employee share of the tax. But the Chief Actuary concluded that the accounts would still be so clearly a better deal that *all* workers would choose the accounts.

Over the long term, the accounts result in breathtaking reductions in government spending, because the payment of Social Security benefits is shifted out of the federal budget altogether, financed instead through the accounts in the private sector. This would result in the largest, most dramatic reduction in government spending in world history.

Because of this, the personal accounts alone under Ryan-Sununu eventually closed the long term Social Security financing gap entirely, without any benefit cuts or tax increases. Indeed, since the employer half of the payroll tax continued to be paid, while the payment of the benefits was shifted to the personal accounts, the Ryan-Sununu plan eventually resulted in very large Social Security surpluses, which allowed for payroll tax cuts. For these reasons, the Chief Actuary of Social Security scored the plan as achieving full solvency for Social Security.

Imagine how all workers accumulating hundreds of thousands or even millions in their own personal accounts by retirement would transform society. The Chief Actuary calculated that under Ryan-Sununu after just 15 years with the personal accounts, working people all across America would have accumulated $7.8 trillion in their accounts, in real terms after adjusting for inflation. That would climb to $16 trillion after 25 years.

Moreover, all those funds would pour into our economy as mighty rivers of increased capital investment, rapidly expanding economic growth. Those funds would finance the practical implementation of our rapidly advancing science, leapfrogging our economy further generations ahead.

In 1981, the South American nation of Chile, then with a Social Security system just like ours, with the same problems, adopted a personal account option similar to Ryan-Sununu, with astounding success. Virtually all workers chose the accounts within 18 months, and for 30 years now they have paid less into the accounts and gotten higher benefits, while their economy boomed with all the increased savings and investment.

In America itself, such a system was tried in 1981 as well, for local government workers in Galveston, Texas, who still enjoyed that option under the law then. Just as in Chile, for 30 years now they have paid much less into their personal account savings and investment system than required by Social Security, but receive much more in benefits. The analogous Thrift Savings Plan retirement system for federal employees has similarly worked spectacularly well now for nearly 30 years.

The personal account option can start at whatever level is feasible at first. A reasonable beginning would be to allow each worker the freedom to choose to switch half of the employee share of the Social Security payroll tax to such an account, which would be 3.1% of taxable payroll. The initial account option can also be limited by restricting it at first to younger workers.

As in Chile, workers would choose investments by picking a fund managed by a major private investment firm from a list officially approved and regulated by the federal government for safety and soundness. The personal account investments would be kept strictly separate from the rest of the company, again as in Chile, so any financial troubles the company might experience would have no effect on the personal account investments. This would also be very much like the highly successful private retirement investment systems used for the federal employee Thrift Savings Plan and for the private alternative to Social Security used for local government workers in Galveston, Texas.

The Chilean personal account system that has been so successful for 30 years now includes a government guaranteed minimum benefit for the personal accounts that is roughly equal as a percent of income to the average benefit under the U.S. Social Security system. That is feasible because market investment returns are so much higher than what completely uninvested, tax and redistribution, pay-as-you-go Social Security even promises let alone what it can pay. That is why in 30 years, even through the financial crisis, Chile has never had to make a payment on that guarantee. Through its regulation of the private investment firms among which personal account investors can choose, the government can limit and control the risks workers can take on with their personal accounts, preventing moral hazard from the guarantee.

In these circumstances, it would be politically sensible to simply guarantee that no worker with personal accounts will get less in total benefits than Social Security currently promises, rather than try to defend a complicated, more limited guarantee. Promised Social Security benefits are weak and marginal compared to what would be gained through a lifetime of real savings and investment. The possibility that the accounts would be unable to pay at least that much over a lifetime of savings and investment is, therefore, remote, making the politically desirable guarantee economically feasible.

Such a guarantee, which was included in the Ryan-Sununu bill as well, effectively enables the personal account system to maintain the social safety net of Social Security. That is a political key to enabling the sweeping, fundamental, structural change from a tax and redistribution system to a private savings, investment and insurance system.

No worker would be required to take this personal account option. They would each be perfectly free to stay in the current Social Security system as is, with no benefit cuts or tax increases. That is feasible because based on the experience in Chile and the score of the Chief Actuary of Social Security, virtually all workers can be expected to choose the personal accounts.

After the initial reform, the account option could be expanded over time, eventually to the full amount of the employee share of the payroll tax, 6.2% of wages. The accounts could then be further expanded to allow substitution of private life insurance for Social Security survivors benefits, and private disability insurance for Social Security disability benefits. This could be accomplished with another 2.3% of wages, as in Chile, coming out of the employer share of the tax. Eventually, the accounts could be expanded to cover the payroll taxes for Medicare, another 2.9% of wages, with the saved funds financing monthly annuity benefits used to purchase private health insurance in retirement. The personal accounts would then encompass an option for 11.4% of wages altogether, about one-fourth less than the current 15.3% payroll tax.

With the accounts then paying for all of the benefits currently financed by the payroll tax, that tax would eventually be phased out altogether. Workers would instead be paying into the family wealth engine of their own personal savings, investment and insurance accounts. In the process, government spending equivalent to about 10% of GDP would be transferred to the private sector, the largest reduction in government spending in world history.

Any plan for personal accounts for Social Security involves a transition financing issue. That arises because Social Security operates on a pay-as-you-go basis, with almost all of the money coming in immediately going out to pay current benefits. If part of the money coming in goes for savings and investment in personal accounts instead, additional funds will have to come from somewhere else to continue paying all promised benefits to today's retirees. The need for this transition financing phases out over time as workers retire relying on their personal accounts instead of payroll taxes.

This is a cash flow financing issue, not a matter of transition *costs.* What the transition is really financing is the increased savings and investment involved in shifting from a tax and redistribution, pay-as-you-go system, with no real savings and investment anywhere, to a fully funded, savings and investment system, just as with eliminating the unfunded liabilities of any underfunded pension plan. When you save $1,000 in a bank, you don't think that cost me $1,000. It doesn't *cost* you anything, because you still have the money, in your savings account. Of course, because you can't have your cake and eat it too, you can't spend the $1,000 you are saving, or else you wouldn't be saving it. That may create a cash flow issue for you, depending on your personal finances. But it is not a matter of the savings *costing* you $1,000.

The transition financing money is effectively financing the savings going into the personal accounts of working people across America. That accumulated savings and investment is not a cost to the economy, it is a mighty, productive contributor to the economy. The working people seeing that money growing in their own personal accounts would certainly recognize that it is not a cost, but, in fact, an asset. The personal accounts are actually just a politically sophisticated means of shifting from the current, completely non-invested, tax and redistribution, Social Security system, to a fully funded system based on savings and investment, which should be readily recognized as the complete, responsible, desirable solution to the issue of Social Security.

But this transition financing would all be more than covered by the reduced government spending resulting from the other entitlement reforms discussed in this essay, further detailed in the book. With the transition financed entirely by such reduced spending, the personal accounts would produce entirely a net contribution to national savings and investment. The workability of this approach was demonstrated by the Ryan Roadmap, the comprehensive legislation introduced by now House Budget Committee Chairman Paul Ryan. That proposed legislation includes personal accounts for Social Security, fundamental reform of Medicare and Medicaid, general health care reform, tax reform, and other budget reforms. CBO officially scored the Roadmap as achieving full solvency for Social Security and for Medicare, and balancing the federal budget indefinitely into the future, completely eliminating all long term federal deficits, with no tax increases. In the process, the transition to the personal accounts for Social Security is fully paid for, effectively by the spending reductions.

President Obama mocks the idea of personal accounts, saying they risk your Social Security in the stock market. But personal accounts are only a choice open to each worker, no one imposes it on them. Moreover, nothing requires anyone with a personal account to invest anything in the stock market. They are free to choose from a wide range of market investments, including even government guaranteed alternatives if they want (on top of the guarantee already in the proposal).

To answer Obama's challenge, I joined with William Shipman, former Principal of State Street Global Advisors. Our work, published in the *Wall Street Journal*[34] showed that an average income two earner couple who retired in 2009 just after the worst of the financial crisis, who had saved and invested in a personal account option to Social Security for their entire lives, and invested it all in the stock market, would still have retired with $850,000 in their accounts, almost millionaires. In fact, they were millionaires, until they lost 37% of their account funds in the year before retirement. But their accumulated funds were still enough to pay them 75% more than Social Security promises them. This is effectively a worst case scenario, since 1999-2008 was actually the worst 10 year stock market performance in America's history.

But didn't President Bush already try personal accounts for Social Security and fail miserably? My book discusses in detail why Bush failed with personal accounts as well. When Bush ran for President in 2000, he explicitly campaigned on empowering workers with the freedom to choose personal accounts for Social Security, employing all

[34] William G. Shipman and Peter Ferrara, "Private Social Security Accounts: Still a Good Idea," October 27, 2010, p. A17.

the positive, populist themes originally envisioned for the reform effort, as discussed above. That included in particular contrasting the accounts and all of their benefits with the unpopular alternatives of cutting benefits or raising taxes. This worked spectacularly for him, even allowing him to win Florida by the narrowest of margins carrying the senior vote, which is what won him the Presidency.

But once elected, he turned to Beltway insiders to handle the project who were stuck inside the Washington Establishment box that insisted that Social Security reform was all about some combination of tax increases and benefit cuts. Under the new White House conception of Social Security reform, personal accounts became "the dessert" to make palatable the "spinach" of benefit reductions. The mantra came to be that “everything was on the table”, every brutally unpopular idea, such as delaying the retirement age, or means testing, or changing the basic benefit formula, along with the one politically successful and transforming idea of personal accounts. All of this just buried all of the positives of personal accounts, and at best confused the public. Were benefits going to rise under personal accounts, or fall relative to income under price indexing? The public soon was lost. Personal account advocates warned them early and often that this would fail, but they proved impenetrable.

The fatal fallacy persists that it would be politically easier to cut benefits than to enact structural reforms like personal accounts. For all of the reasons discussed above, a populist, grassroots alliance can be generated to support personal accounts, which is the one Social Security reform idea ever to show support by large majorities in the polls. The alternative is to cut a deal with the Washington establishment that will slash Social Security returns and benefits for working people, at the price of agreeing to a tax increase for “balance.” This would be politically crippling for Republicans.

A New Vision for Entitlements

This testimony projects a new, modernized, 21st century, vision for entitlements, thoroughly detailed in the book, harnessing capital, labor and insurance markets, and productive incentives, to achieve all of the social goals of those entitlements far more effectively, ultimately serving seniors and the poor far better. Yet, because those reforms rely on markets and productive incentives, the cost of those programs to taxpayers are dramatically reduced. Indeed, over time federal spending is reduced by half or more from where it would be otherwise, resulting in a complete solution to the nation’s entitlement and fiscal crisis. These modernized entitlements directly contribute to economic growth and prosperity, rather than detracting from it.

This vision is consequently the key to unlocking the door to fundamental, fiscally necessary, entitlement reforms.

Peter Ferrara is Director of Entitlement and Budget Policy for the Heartland Institute and Senior Fellow for the Carleson Center for Public Policy. He served in the White House Office of Policy Development under President Reagan, and as Associate Deputy Attorney

General of the United States under the first President Bush. He is the author of *America's Ticking Bankruptcy Bomb*, now available from HarperCollins.