COMMITTEE FOR A RESPONSIBLE FEDERAL BUDGET

MEMORANDUM

To:	Interested Parties
From:	The Committee for a Responsible Federal Budget
Re:	Policies to Grow the Economy
Date:	May 18, 2017

The aging of the population will make achieving past levels of economic growth much more difficult in the years ahead. The Congressional Budget Office (CBO) projects that real GDP growth will average 1.9 percent annually over the next 30 years, far below the 3.2 percent it has averaged since the end of World War II. However, structural reforms to the nation's tax, spending, and regulatory policies can have a meaningful impact in accelerating the pace of economic activity.

We recommend any pro-growth agenda focus on the following:

1. Modernize the Tax Code
2. Encourage Productive Aging
3. Reform the Immigration System
4. Promote Work Throughout Government Programs
5. Reallocate the Budget Toward Investment
6. Pursue Regulatory Reform
7. Ensure Prosperity is Widely Shared
8. Fix the National Debt

1. Modernize the Tax Code

The last time the United States reformed the tax code was over 30 years ago, and the need for modernization is as great as ever. The current tax code is a drag on economic growth because of its high rates (our statutory corporate rate is highest in the world), significant complexity, and broken rules for international taxation. The code also includes $1.6 trillion in annual tax breaks that lose revenue, undermine fairness, and distort economic decision-making.

Pro-growth tax reform would ideally reduce tax breaks, lower rates, improve simplicity, promote investment, overhaul rules for cross-national taxation, and set aside funds for debt reduction. The Joint Committee on Taxation has estimated such reforms could increase GDP by anywhere from 1.7 to 2.2 percent over the long-term. Importantly, revenue-positive tax reform has the greatest pro-growth potential because it will contribute to slowing the unsustainable rise in government borrowing that will crowd out private investment.

2. Encourage Productive Aging

The aging of our population is a key cause of slower projected growth. In 1987, there were 30 million Americans over 65; today there are 50 million, and by 2047 there will

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be 84 million. With fewer children to replace retiring workers, labor force growth has slowed to a fraction of its historical average.

One way to offset some effects of an aging population is to encourage those in their early to mid-60s to continue working (perhaps on a part-time or more flexible basis) and delay their retirement. CBO has estimated that if the average worker worked just 8 months more, GDP would be 1 percent higher. The federal government can do more to encourage longer and more flexible working lives by improving incentives and signals throughout the tax, spending, and regulatory codes. A place to start would be a review of all statutory retirement ages under current law.

3. Reform the Immigration System

Another way to mitigate the effects of the aging population is to increase the size of the workforce through immigration reform. By allowing more young workers to enter and work in the country, policymakers can help promote a younger and larger workforce. Reducing barriers to high-skilled immigration could be particularly important, as these are the individuals most likely to contribute to innovation. CBO has estimated that immigration reform could increase GDP by up to 3.3 percent after 10 years and up to 5.4 percent after 20.

4. Promote Work Throughout Government Programs

The federal government provides a number of important safety net programs that help low-income and vulnerable Americans when they are most in need. Unfortunately, most of these programs also discourage employment, either by phasing out as income rises or disappearing altogether when individuals return to work. As a result, CBO estimates many low-income families face marginal effective tax rates as high or higher than the highest-earning households.

To some degree, safety net programs will always create some work disincentive, but with labor force participation among prime-age men below historic averages, more could be done to promote work. Thoughtful reforms should review and adjust the signals and incentives in various government programs, while expanding access to job training, worker rehabilitation, and other support systems. As an example, our recent SSDI Solutions Initiative released a book full of ideas that could support work for individuals with disabilities. These and other changes could help increase labor force participation and boost growth.

5. Reallocate the Budget Toward Investment

Public investments that boost productivity and innovation are a key source of growth, but the share of the budget devoted to investments in infrastructure, education, and research has fallen from over 30 percent in the 1960s to just 13 percent in 2015. Meanwhile, consumption-fueling transfer payments have increased from about 30 percent of the budget to 72 percent. And whereas transfer spending is projected to rise rapidly in the coming years, federal investments are projected to remain flat or decline.

To promote growth, policymakers should slow the growth of consumption-based spending and use some of the proceeds to promote public investment. CBO estimates that $500 billion of (paid-for) public investment would increase the size of the economy by 0.06 percent after 20 years. The effects could be larger if the money comes from reductions in anti-growth spending.

6. Pursue Regulatory Reform

Since 1975, the number of pages in the Code of Federal Regulations has grown from 71 thousand to nearly 180 thousand. Many of these regulations serve important public purposes, but on net they also tend to slow economic growth by preventing businesses and individuals from making economically-efficient decisions. While the societal benefits of many regulations justify their economic costs, other regulations do not pass the cost-benefit test. Some regulations may be redundant, overly burdensome, or could simply be better written to improve effectiveness.

Any economic growth strategy should include a full review of federal regulations at all levels. Many regulations should be retained, but those with costs that outweigh benefits should be reformed or in some cases removed altogether.

7. Ensure Prosperity is Widely Shared

The best way to lift income and wealth is through faster economic growth. However, for growth to be sustained it will have to be shared broadly, and thus it is important to ensure that the gains to the economy are widely shared and contribute to a broad and growing middle-class. Despite the economic recovery, inflation-adjusted median income is still below its pre-recession level. Broad-based and inclusive economic growth not only benefits more people, but also builds the social cohesion and faith in our institutions necessary for our democracy.

8. Fix the National Debt

Perhaps the most significant policy action lawmakers could take to restore growth would be to address our high and rising national debt. At 77 percent of GDP, debt is higher as a share of the economy than any time in our history except after World War II. Under current law, it is projected to grow to 150 percent over the next three decades. High and rising debt crowds out private investment, slows wage growth, increases interest rates, reduces the government's ability to respond to a future recession or disaster, and increases the risk of a fiscal crisis.

Getting the national debt under control through a thoughtful mix of tax and spending changes will reduce the risk of fiscal crisis while accelerating income growth. CBO estimates income per person in 2047 would be $5,000 higher if we reduce the debt modestly as a share of GDP compared to if we continue on our current course.

Importantly, fixing the national debt also makes all other pro-growth policies easier to pursue. By creating the fiscal space for tax reform, federal investments, and other priorities, controlling the national debt can pay dividends and ultimately allow for a comprehensive pro-growth agenda.

Appendix: Specific Examples of Policies to Encourage Growth

- Lower the corporate tax rate while repealing corporate tax expenditures
- Allow “full expensing” of investment while repealing the deductibility of interest
- Lower individual tax rates while repealing most deductions, credits, and exclusions
- Replace tax preferences for mortgage interest, charitable giving, health insurance, and state and local bonds with better targeted credits
- Replace the current international tax system which taxes worldwide income after deferral with a more modern and pro-growth system
- Raise and/or longevity index various ages for Social Security, Medicare, federal retirement, and retirement account withdrawals
- Eliminate Social Security’s “retirement earnings test”
- Modify Social Security’s benefit formula to be based on each year of work (“mini-PIA”)
- Modify Social Security’s actuarial reduction factors to encourage delayed claiming
- Make Medicare the primary payer for eligible older workers
- Raise the maximum eligibility age for the Earned Income Tax Credit to 67
- Revise pension benefit formulas to reward longer careers
- Modify and improve enforcement of age discrimination laws
- Increase total number of H-1B visas granted
- Address benefit cliffs in means-tested programs
- Offer disability applicants training and support to remain in the workforce
- Time limit SSDI benefits for beneficiaries expected to recover
- Improve access to vocational rehabilitation and employment support services
- Use transitional jobs to increase employment of disability applicants and beneficiaries
- Allow states to use a small portion of SSI, SNAP, and Medicaid funds to encourage and support back-to-work initiatives
- Support initiatives that encourage lifelong learning
- Replace certain unemployment programs with relocation subsidies
- Fully fund the highway trust fund through a higher gas tax or other means
- Increase non-defense discretionary spending caps, paid for by adopting the “chained CPI”
- Increase funding for the National Institutes of Health and the National Science Foundation, paid for by reducing federal health costs
- Revisit the budget process treatment of investment spending
- Make Social Security sustainably solvent through a mix of revenue and spending changes
- Slow the growth of Medicare and Medicaid, especially with reforms designed to “bend the cost curve” and improve the quality and value of care.

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