



## The Incredible Shrinking Budget for Working Families and Children

C. Eugene Steuerle

Programs for working families and children are scheduled to shrink rapidly over the next few years, squeezed between rising expenditures on programs for the elderly and declines in tax revenues. This scenario will play out even if only modest defense and international needs are factored into the division of federal funds. Temporary deficit financing can delay the day of reckoning very little, since borrowing against the future only compounds today's problems.

Of course, policymakers aren't likely to zero out *all* spending on working families and children. They could instead revamp elderly programs, reform taxes, or do both. But here's the rub: programs for the politically disadvantaged wear stone slippers in the dance of budget legislation. Put another way, programs for families and children do not receive the large, automatic, built-in growth of many elderly programs or the automatically growing costs of many tax breaks.

Let's get personal here. Current law promises that typical couples retiring today will get a government-paid insurance package worth about \$600,000, while those now in their early 40s will retire with about \$1 million (in today's dollars). Federal spending on children pales beside such figures. Nor are funds for families backed by any guarantee of growth. In fact, many of these programs require a type of supermajority (support by both houses of Congress and the president every year) simply to remain above zero. Contrast, if

you will, the annual budgetary debate over the popular child development program Head Start with the lack of discussion on the growing level of Social Security support provided to the average retiree every year. In short, the budget for working families and children is largely discretionary and too often treated as a leftover in the annual appropriations process.

Consider this trade-off from a lifetime perspective. The federal government promises citizens born today very little in their early years, when an investment might have a big payoff. However, to those who grow up and enter the workforce, the government promises subsidized consumption and decades of supported retirement when they are older. Is that a trade-off anyone would choose?

As budgetary push comes to budgetary shove, it's no longer prudent for legislators, foundation officials, and other leaders who care about children and working families to stay aloof from these budget issues—even though, as Pennsylvania Republican Sen. Arlen Specter recently quipped, the amount of pork is "giving sausage a bad name." Anyone who cares about how money is allocated to particular programs should care about the budget and even about those arcane matters of budget process that determine what gets debated—and how.

Traditionally, many of those people concerned with families and children did not like to move into the budget arena. The budget is complicated. Especially when deficits

---

*The budget for working families and children is largely discretionary and too often treated as a leftover in the annual appropriations process.*

are being reduced, the broader budget process tends to identify losers, not just winners. But, more and more, the allocation of the overall budget determines policy decisions about programs for poor families and children. Partisan politics only compounds the problem: in the squeeze between rising costs of elderly programs and falling revenues, liberals do not like to admit the first cause of the squeeze, and conservatives do not want to own up to the second.

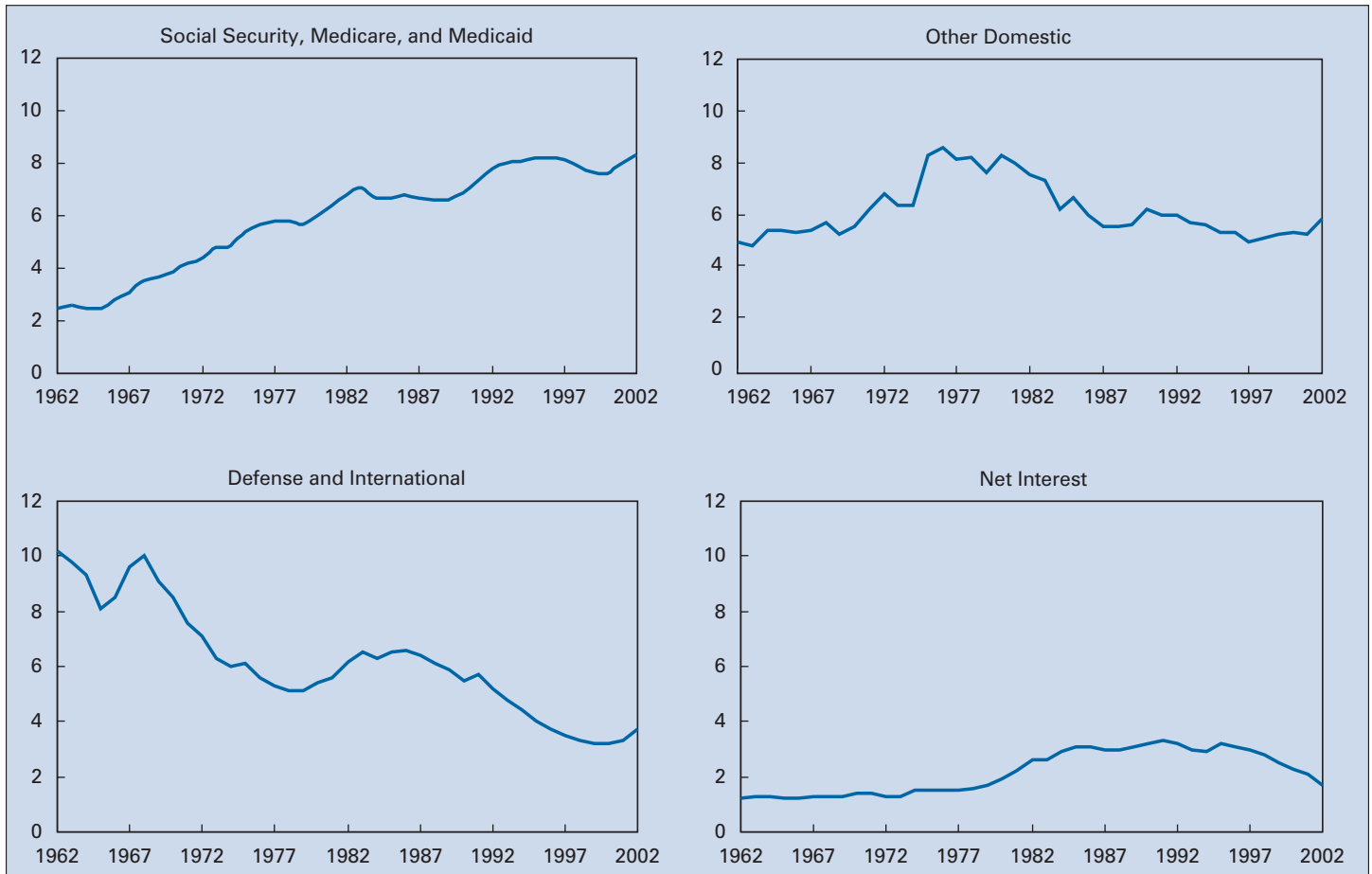
### The Recent Decline in Other Domestic Policy

Outside of interest on the debt, U.S. spending can be divided roughly into two parts: (1) defense and international affairs and (2) domestic programs—mainly Social

Security, Medicare, and Medicaid—and “other domestic outlays.”<sup>1</sup> This last, rather dry-sounding category consists of programs for children, welfare, education, the environment, community development, housing, energy, and justice—the very programs that touch working families’ lives and reach the majority of all Americans.

When the share of one of these categories grows, less money is left for the others. Moreover, since taxes have generally represented the same percentage of gross domestic product (GDP) for five decades, the percentage of GDP spent on a particular program generally has fallen whenever its share of the budget has fallen. (That is, the federal slice of GDP wasn’t made larger, so when a program got a smaller share of the federal slice, it got a smaller share of GDP.)

FIGURE 1. Federal Outlays as a Percentage of GDP, 1962–2002



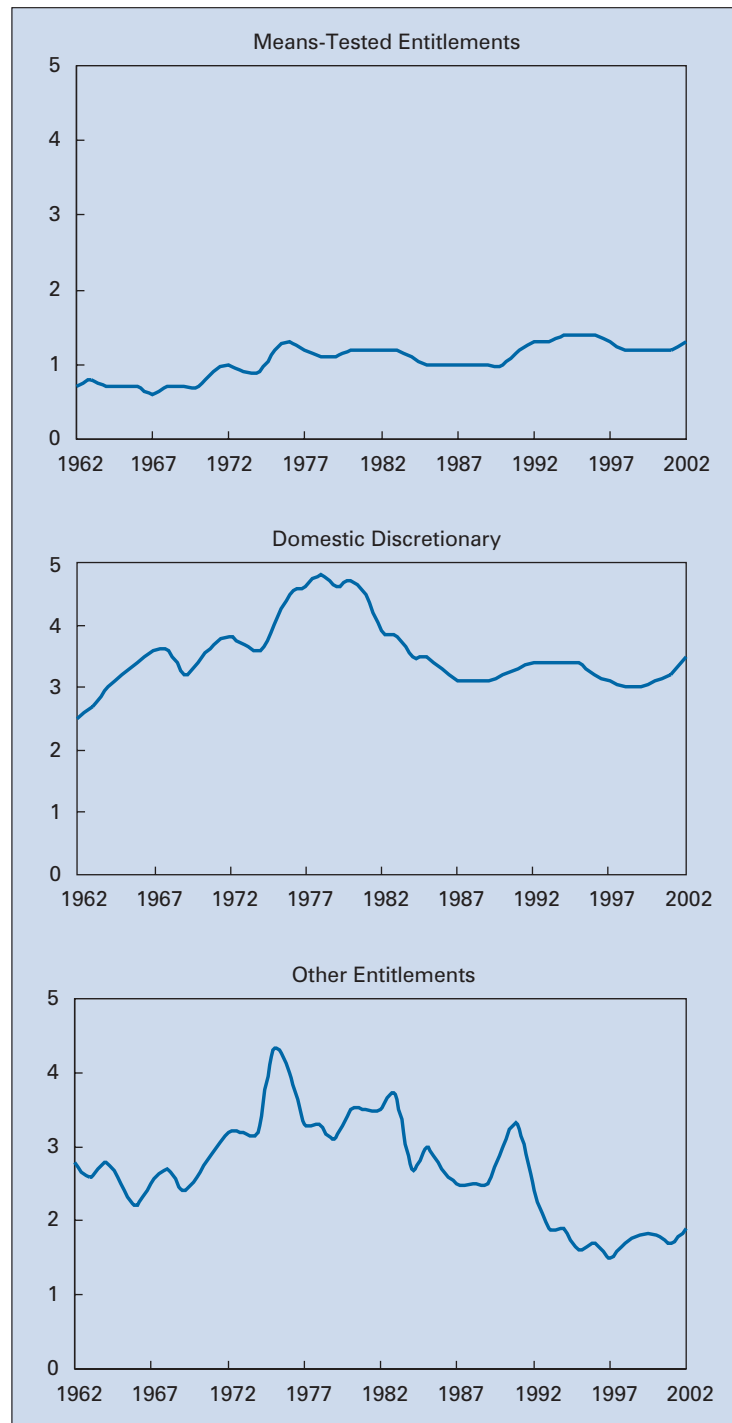
Source: Eugene Steuerle and Adam Carasso, The Urban Institute, 2003. Based on data in the Congressional Budget Office’s *Economic and Budget Outlook FY 2004–13*, Appendix F: Historical Budget Data.  
 Note: All graphs exclude Social Security, Medicare, and Medicaid.

In effect, rising spending on the elderly brought about lower spending—whether measured as a share of the budget or of GDP—for everything else.

From the mid-1950s to the end of the 20th century, the continual and rapid rise in percentage of GDP budgeted for the elderly was financed largely, but not entirely, through offsetting declines in the defense and international budget. Other domestic outlays have been falling since the mid-1970s as a share of GDP (figure 1) and as a share of federal expenditures as well. Within other domestic outlays, only means-tested entitlements, including the earned income tax credits (EITCs) and Temporary Assistance for Needy Families (TANF), which are largely welfare-oriented and limited by income level, held their own or grew slightly as a share of GDP (figure 2). These gains came mainly through new legislation; even though technically categorized as entitlements, most are scheduled to decline over time as a percentage of GDP without new legislation.<sup>2</sup>

It was only a matter of time before defense cuts would no longer offset the ever-expanding budget for aging Americans. After declining from about 14 percent of GDP to less than 4 percent by the late 1990s, defense cannot fall another 10 percentage points, and further engagement with, rather than retreat from, the international arena now seems likely for some time to come. Thus, without an overhaul of entitlement

FIGURE 2. Other Domestic Outlays as a Percentage of GDP, 1962–2002

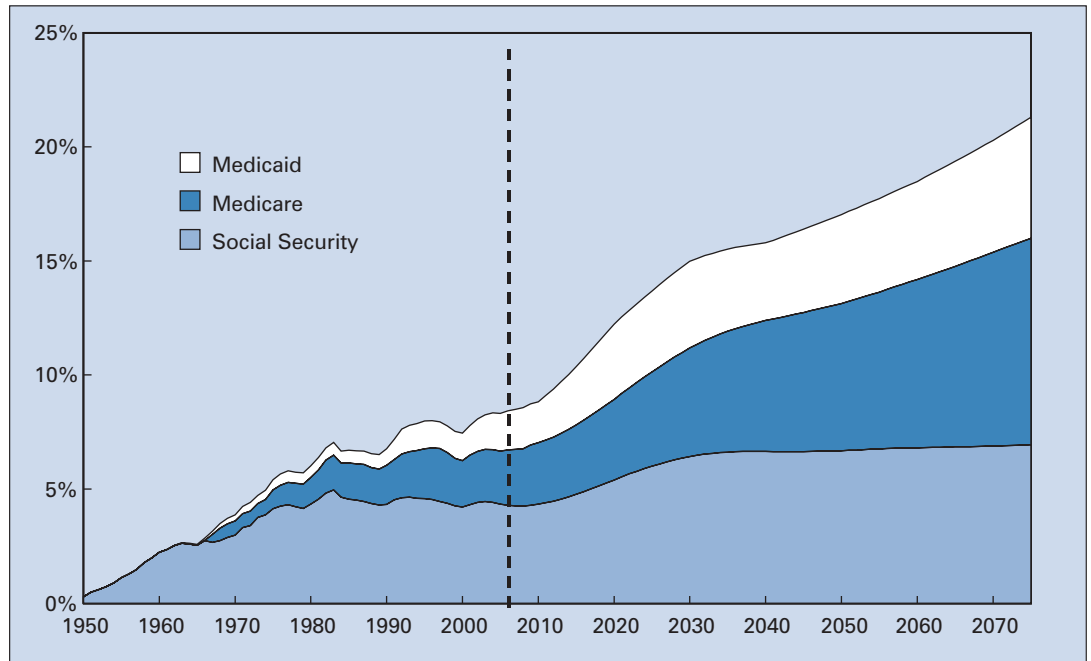


Source: Eugene Steuerle and Adam Carasso, The Urban Institute, 2003. Based on data in the Congressional Budget Office's *Economic and Budget Outlook FY 2004–13*, Appendix F: Historical Budget Data.

Note: All graphs exclude Social Security, Medicare, and Medicaid.

programs or tax-revenue reform, the ever-expanding Social Security, Medicare, and Medicaid budgets will tighten the squeeze on other domestic spending (figure 3).

FIGURE 3. Social Security, Medicare, and Medicaid Outlays as a Percentage of GDP, Fiscal Years 1950–2075



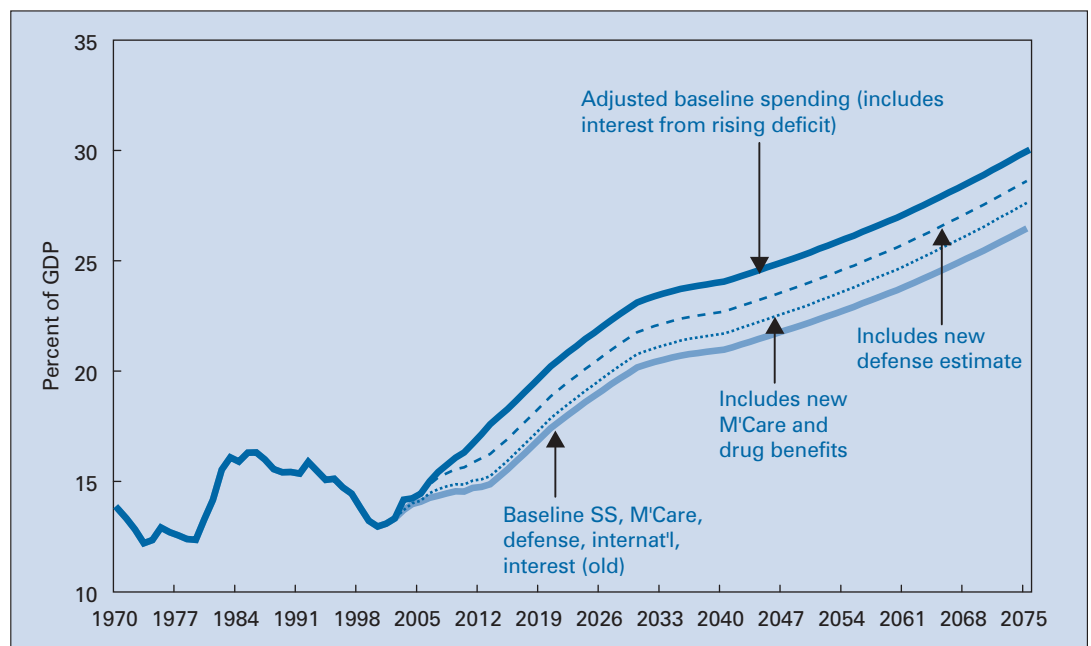
Source: C. Eugene Steuerle and Adam Carasso, The Urban Institute, 2003. Based on data from the Congressional Budget Office, "A 125-Year Picture of the Federal Government's Share of the Economy, 1950 to 2075," July 3, 2002, table 2.

### The Recent Spending and Tax-Cutting Spree

From the mid- to late 1990s, a slowdown in the Medicare growth rate and an unexpected

rise in revenues gave government programs for families and children some breathing room. But behind that rise in revenues was a host of factors unlikely to converge again soon: unusual amounts of capital gains real-

FIGURE 4. The Path of Spending Obligations



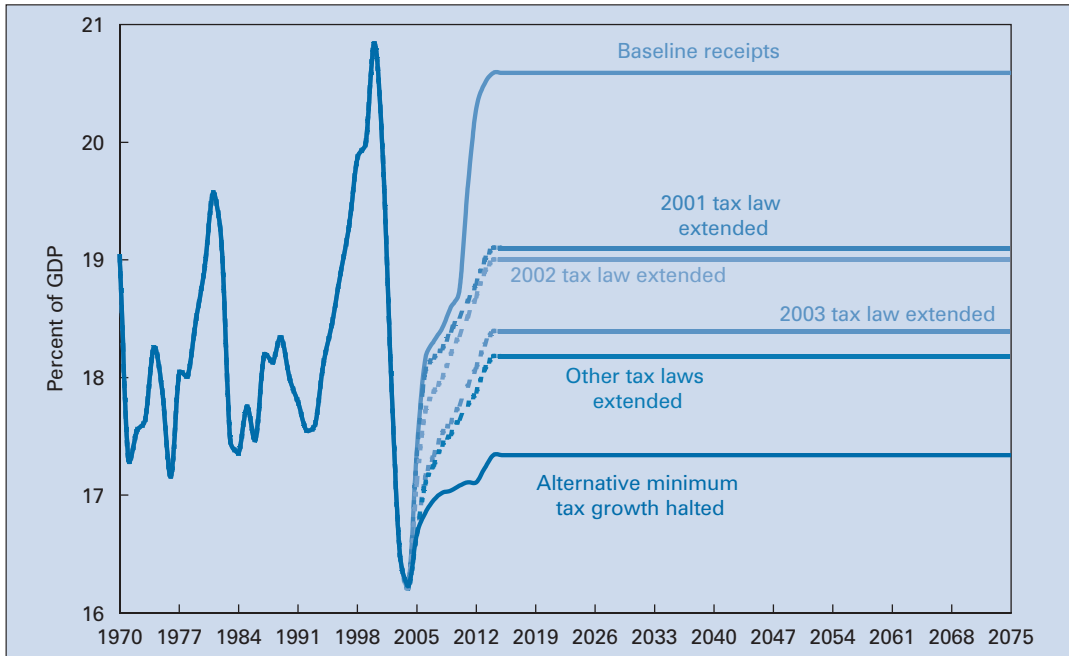
Source: Eugene Steuerle, Adam Carasso, and Meghan Bishop, The Urban Institute, 2003. Based on data from CBO and OMB budget documents.

izations, significant stock option recognition, and increasing inequality in income (which increases average tax rates).<sup>3</sup>

It took only a modest economic downturn and a more realistic assessment of technol-

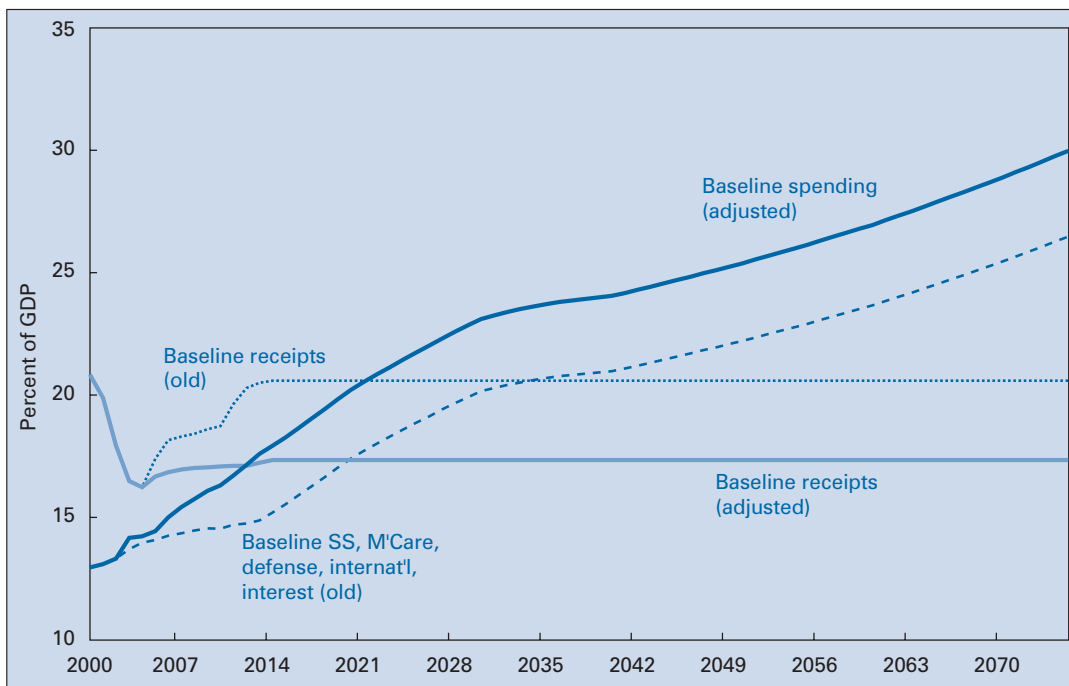
ogy stock values to shift from the unexpected revenue windfall to a revenue shortfall. The terrorist attacks of 2001 led to increases in defense spending. Meanwhile, Congress continued on an extraordinary tax-cutting and

FIGURE 5. Revenues if Tax Law Remains Constant

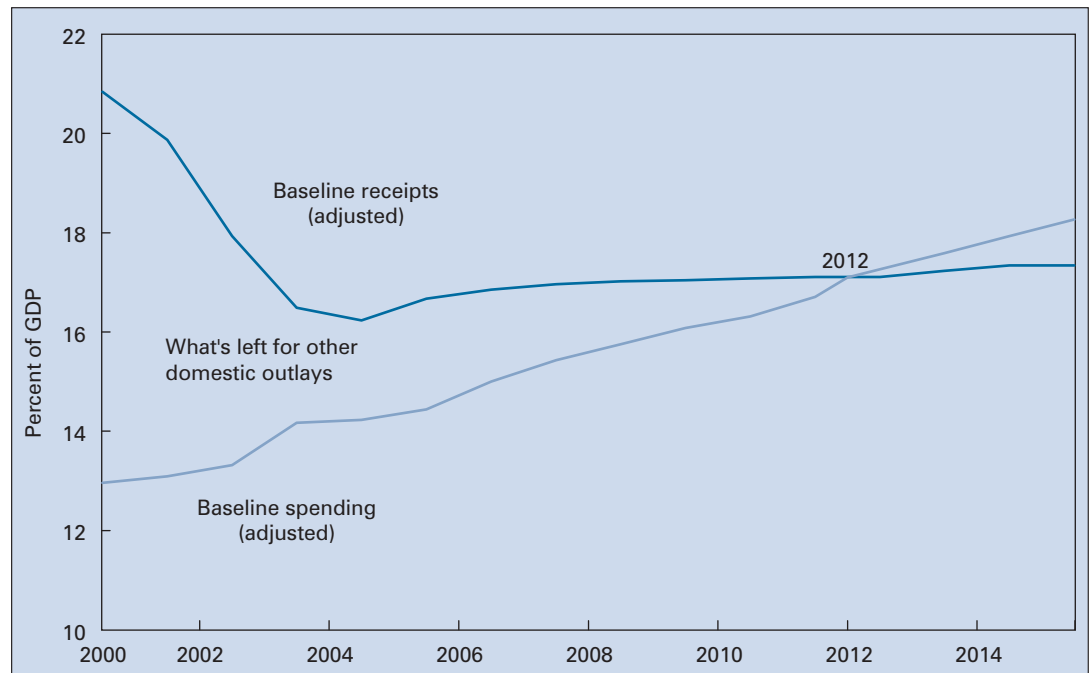


Source: Eugene Steuerle, Adam Carasso, and Meghan Bishop, The Urban Institute, 2003. Based on data from William Gale and Peter Orszag's "Sunsets in the Tax Code" (2003), Urban-Brookings Tax Policy Center.

FIGURE 6. Lower Receipts and More Spending Move the "Cliff" Up from 2041 to 2012



Source: Eugene Steuerle, Adam Carasso, and Meghan Bishop, The Urban Institute, 2003. Based on data from CBO and OMB budget documents.

FIGURE 7. *The Current Squeeze*

Source: Eugene Steuerle, Adam Carasso, and Meghan Bishop, The Urban Institute, 2003. Based on data from CBO and OMB budget documents.

*If the budget simply were balanced, and recent tax cuts and spending increases were made permanent, then existing commitments would totally wipe out other domestic outlays by 2012.*

spending spree, ranging from large tax cuts in 2001, 2002, and 2003 to a loosening up on Medicare-cost constraints to farm subsidies to, well, you name it. The combined effect meant that expenditures rose relative to revenues by \$800 billion or 7 percent of GDP for fiscal year 2004 alone—more than the entire income loss from the downturn.

Other domestic spending initially shared in a bit of the largess. But tax cuts and increases in spending on the aged got the lion's share. Even recently, the major debates in the nation were over more tax cuts and a drug benefit in Medicare.

A modestly optimistic, but still reasonable, assumption is that defense and international obligations will level off at about 4 percent of GDP (still below today's spending levels, which includes requests for keeping peace around the world). Of course, maintaining the promises embedded in recent tax cutting and spending expansions makes the already scheduled squeeze on other domestic spending even more immediate and untenable. Figure 4 shows how much lower tax levels will be if recently enacted rates are made perma-

nent, while figure 5 shows how new drug-benefit, defense, and mounting debt costs add to growing spending obligations.

Look carefully. If the budget simply were balanced, and recent tax cuts and spending increases were made permanent, then existing commitments would totally wipe out other domestic outlays by 2012. Even if no major tax or spending legislation had passed since 2000, the squeeze that had already been inherited from the past century would have wiped out those programs for families and children by 2041 (see figures 6 and 7). No provision is made under these calculations for any domestic or international emergency, whether an act of terror, a large earthquake or hurricane, a crime wave, or an energy crisis. Nor is any new national initiative to meet the needs of children today part of this calculus, never mind that our educational system still fails millions of children and revolves around a schedule created years ago to meet farming demands. And, beyond 2012, a nation already bent on financing consumption rather than investing in people will find that the economic growth rate declines

further as the baby boomers move into the retirement population.

While the budget squeeze on programs for families and children may appear ominous, the problem is mainly political, not economic. This political course *can* be altered.

No natural law requires us to retire for nearly one-third of our adult lives. We don't have to receive close to \$1 million in aging benefits per couple. And we don't have to maintain federal tax receipts at 17 percent of GDP. Programs for families and children are getting squeezed mainly because they lose out to such political wants as retirement in middle age and elimination of the estate tax.

In this milieu, budgetary and economic analysis has a vital role to play. The United States is still a rich nation with growing abundance, and it can afford to do many things and do them well. It cannot do everything, however, and it must eventually develop a legislative and budget process that no longer places programs for working families and children at a disadvantage in the allocation of its abundant, yet finite, tax resources.

## Notes

1. Social Security, Medicare, and Medicaid are the only programs for which 75-year projections are made. They are largely elderly programs, and much of the growth in Medicaid is due to projec-

tions of long-term care costs for the elderly and disabled. The "elderly" budget is approximated by these items, even though not all Medicaid goes to the elderly. Then again, these items exclude other programs such as civil service and military retirement, Supplemental Security Income, and veterans' old-age benefits.

2. Some programs like TANF have been kept by the government in the category of "means-tested entitlements" even though they no longer have the primary features of entitlements. Unlike health and retirement programs, however, these means-tested entitlements do not grow automatically with increases in economic income and wages. Past growth came about through constant legislation and new enactments, such as when legislated increases in the EITC offset some of the scheduled decline in the share of GDP devoted to programs like TANF. The point here is that even if some of these means-tested entitlements do technically avoid the discretionary budget process, they still differ substantially from those entitlements that have automatic growth built into them.
3. For a warning about counting on these revenues, see Gene Steuerle, "Will the Revenues Last?" a four-part series in *Tax Notes*, September 14–October 5, 1998.

## About the Author



**C. Eugene Steuerle** is a senior fellow at the Urban Institute. Dr. Steuerle is a former Deputy Assistant Secretary of the Treasury, and former president of the National Tax Association.

*Address Service Requested*

---

For more information,  
call Public Affairs:  
202-261-5709  
or visit our web site,  
<http://www.urban.org>.  
To order additional copies  
of this publication, call  
202-261-5687  
or visit our online bookstore,  
<http://www.uipress.org>.

*National Budget Issues* analyzes wide-ranging budgetary matters that cut across all Urban Institute research areas. This series reveals the tough choices that the nation must grapple with through the budget, ideally balancing the costs and benefits of government, while also considering society's needs and taxpayers' burdens. Urban Institute's budget researchers—senior fellows and experts—include former high-ranking officials at the Congressional Budget Office and the U.S. Department of the Treasury.

**THE URBAN INSTITUTE**

2100 M Street, NW  
Washington, DC 20037

Copyright © 2003

Phone: 202-833-7200

Fax: 202-293-1918

E-mail: [pubs@ui.urban.org](mailto:pubs@ui.urban.org)

The views expressed are those of the authors and do not necessarily reflect those of the Urban Institute, its board, its sponsors, or other authors in the series.

Permission is granted for reproduction of this document, with attribution to the Urban Institute.