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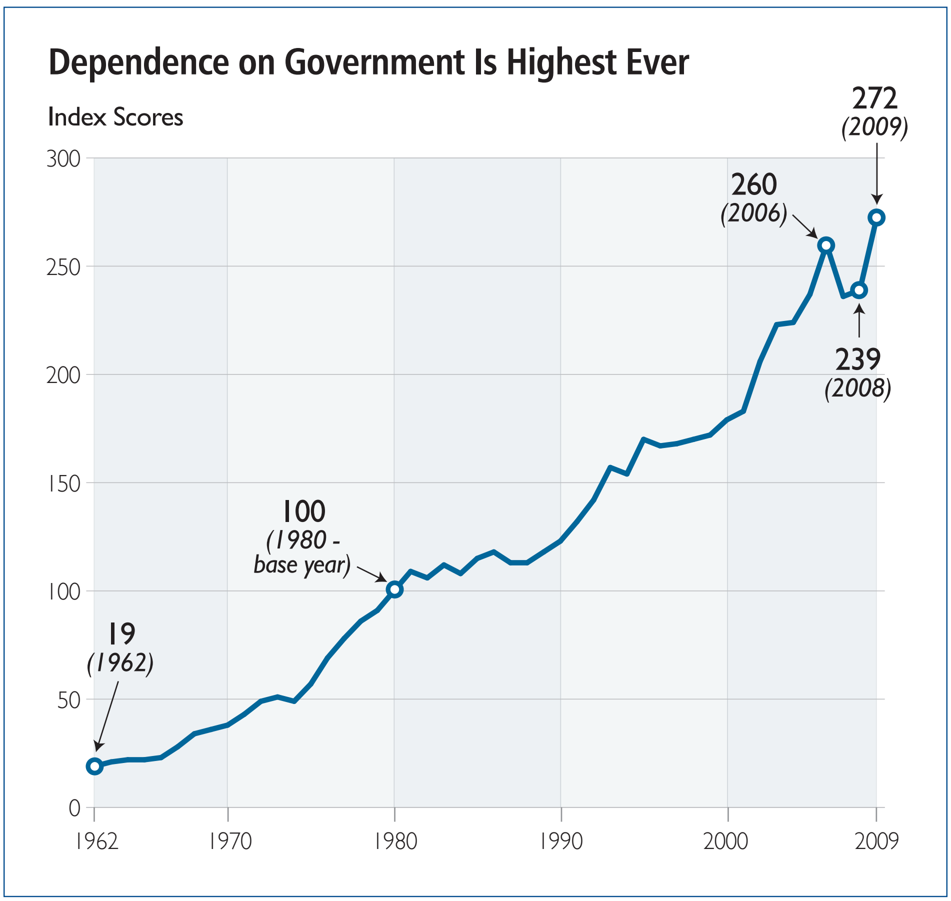
The 2010 Index of Dependence on Government

William W. Beach and Patrick D. Tyrrell

CDA10-08 October 14, 2010



The Heritage Foundation
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A Report of The Heritage Center for Data Analysis

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Abstract: *The number of Americans who pay taxes continues to shrink—and the United States is close to the point at which half of the population will not pay taxes for government benefits they receive. In 2009, 64.3 million Americans depended on the government (read: their fellow citizens) for their daily housing, food, and health care. Starting in 2015, the Social Security program will not receive enough taxes to pay all the promised benefits—which will be hard for all job-holders, but devastating for roughly half the American workforce that has no other retirement program. Add in last year's preposterously named American Recovery and Reinvestment Act, spiraling academic grants, flat-out farm socialism, the swelling ranks of Americans who believe themselves entitled to "free" government benefits—and now the government takeover of the nation's health care system—and the very nature of this country's republican form of government is called into question. Like they have been doing since 2002, Heritage Foundation policy experts lay out the increasingly gloomy facts. Can Americans pull back from the brink of complete dependence on government?*

This year's publication of the Index of Dependence on Government marks the eighth consecutive year that The Heritage Foundation has flashed warning lights about Americans' growing dependence on government payments and programs. For eight years, the Index has signaled troubling and rapid increases in the growth of dependence-creating federal programs, and for each of these years Heritage has raised concerns about the challenges that rapidly growing dependence poses to this country's republican form of government and for the broader civil society.

The 2010 Index results dramatically underscore Heritage's concerns of years past. According to The Heritage Foundation's Center for Data Analysis (CDA):

- The Index of Dependence on Government grew by 13.6 percent in 2009;
- The Index variables that moved the most over that past year were
  - Health care and welfare at 22 percent,
  - Rural and agricultural services at 20 percent, and
  - Housing at 15 percent;
- The increase from last year means that the Index has grown by 49 percent just since 2001;
- The Index begins in 1962 and has increased by more than 14 times over the intervening 47 years through 2009;
- This rapid growth of the Index has been accompanied by a rapid increase in the percentage of people who do not pay taxes. The percentage of people who do not pay federal income taxes themselves, and who are not claimed as dependents by someone who pays federal income taxes, jumped from 14.8 percent in 1984 to 43.6 percent in 2008. Counted this way, in 1984, 34.8 million tax filers paid no taxes; in 2008, 132.5 million paid nothing.[1]

It is the conjunction of these two trends—higher spending on dependence-creating programs and an

1. IRS data found in "Individual Income Tax Returns," Publication 1304, 2008 and 1984, Table 1.4; Heritage Foundation calculations.

ever-shrinking number of taxpayers who pay for these programs—that worries those interested in the fate of the American form of government. Americans have always expressed concern about becoming dependent on government, even while understanding that life's challenges cause most people, at one time or another, to depend on aid from someone else. Americans' concern stems partly from deeply held views that life's blessings are more readily obtained by independent people and that growing dependence on government erodes the spirit of self-reliance and self-improvement. These views help explain the broad public support for welfare reform in the 1990s.

This ethic of self-reliance combined with a commitment to the brotherly care of those in need appears threatened in a much greater way today than when this Index first appeared in 2002. This year, 2010, marks the first year that the Index contains significant retirements by baby boomers. Over the next 25 years, more than 77 million boomers will begin collecting Social Security checks, drawing Medicare benefits, and relying on long-term care under Medicaid. No event will financially challenge these important programs over the next two decades more than this shift into retirement of the largest generation in American history.

It is not only financial tests that these programs will face. Certainly, financial challenges will be great over the next several decades, given that none of these "entitlement" programs can easily meet their obligations even now. Doubling the number of people in retirement will constitute a massive growth of the dependent population in the United States and a potentially ruinous drain on federal finances. Perhaps the most important aspect of the boomer retirement is its dramatic reminder of the rapid growth of dependence on government in the United States.

There was such a rapid growth in dependence in 2009 that the twin concerns—how much damage this growth has done to the republican form of government, and how harmful it has been to the country's financial situation—have deepened significantly. Not only did the federal government effectively take over half of the U.S. economy and expand public-sector debt by more than all previous governments combined, it also oversaw the largest single-year expansion in total government debt in U.S. history. Much of that growth in new debt can be traced to dependence-creating government programs.

U.S. government spending and debt are now worrying the International Monetary Fund (IMF). On May 14, 2010, the IMF ranked the U.S. in second place among countries that must reduce their structural deficit (caused in part by spending on dependence-creating programs) or risk financial calamity. The IMF predicts that U.S. public-sector debt will equal 100 percent of its gross domestic product (GDP) by 2015 unless immediate actions are taken to cut the deficits by an amount equal to 12 percent of GDP. Even woeful Greece need only cut its deficits by 9 percent of its national output.

The IMF and many watchful citizens are right to be concerned about the growing debt and growing dependence. Dependence-creating programs quickly morph into political assets that policymakers readily embrace. Voters tend to support politicians or political parties that give them higher incomes or subsidies for the essentials of life. No matter how well-meaning policymakers are when they create such aid programs, these same programs quickly grow beyond their mission and become severe liabilities.

Many countries have already passed the fiscal tipping point where reckless growth in dependence programs has produced domestic debt crises. How far along the path to crisis is the United States? Are Americans closing in on a tipping point that endangers the workings of their democracy? Have Americans, perhaps, already passed that point? Can this republican form of government withstand the political weight of a massively growing population of Americans who believe themselves entitled to government benefits, and who contribute little or nothing for them?

To explore these questions, one must measure how much federal social programs have grown. How much have such programs "crowded out" what were once social obligations and services carried out by community groups, family networks, and even local governments? In other words, has the civil society yielded significant ground to the federal public sector?

The Index of Dependence on Government is an attempt to measure these patterns and provide data to help ponder the implications of these trends. Table 1 contains the Index scores from 1962 to 2009, with 1980 as the base year. As this table indicates, in recent decades, dependence on government has grown steadily at an alarming rate.

Index of Dependence on Government, 1962–2009

Year	Housing	Health and Welfare	Retirement	Education	Rural and Agricultural Services	Index Value	Annual Percentage Change in Index Value
1962	1	6	5	2	5	19	
1963	1	6	5	2	6	21	11.75
1964	1	6	5	2	7	22	2.75
1965	2	6	6	2	6	22	–0.49
1966	2	7	6	4	4	23	6.06
1967	2	8	7	7	5	28	22.30
1968	2	9	8	9	6	34	21.35
1969	2	10	9	7	7	36	4.97
1970	3	11	9	8	7	38	7.49
1971	4	14	11	7	7	43	12.14
1972	6	17	11	7	8	49	13.76
1973	9	15	13	7	8	51	4.84
1974	9	16	14	5	5	49	–5.16
1975	9	21	15	7	5	57	17.07
1976	14	24	16	8	6	69	20.87
1977	20	23	18	9	9	78	13.44
1978	22	22	18	10	13	86	10.01
1979	26	22	19	12	12	91	5.12
1980*	30	25	20	15	10	100	10.48
1981	34	26	22	18	10	109	9.22
1982	34	25	23	14	10	106	–3.34
1983	36	26	24	13	12	112	6.12
1984	38	24	25	13	8	108	–3.43
1985	38	25	26	14	13	115	6.23
1986	38	26	27	14	14	118	3.01
1987	36	26	27	12	11	113	–4.35
1988	38	27	28	13	8	113	0.22
1989	38	28	29	16	7	118	4.13
1990	39	31	30	16	7	123	3.79
1991	40	37	31	17	7	132	7.30
1992	42	44	33	16	7	142	8.19
1993	47	47	34	20	9	157	10.32
1994	51	48	36	11	8	154	–1.86
1995	58	50	38	19	6	170	10.17
1996	56	50	39	16	6	167	–1.82
1997	56	49	41	15	6	168	0.58
1998	57	50	41	15	6	170	1.63
1999	55	52	41	13	10	172	1.06
2000	56	55	42	12	13	179	3.80
2001	57	59	44	12	11	183	2.20
2002	62	68	46	20	10	206	12.61
2003	64	73	48	26	12	223	8.42
2004	64	74	49	28	8	224	0.40
2005	63	75	51	34	15	237	5.91
2006	62	73	52	52	21	260	9.81
2007	70	74	56	25	12	236	–9.23
2008	67	81	58	23	10	239	1.12
2009	77	99	63	22	12	272	13.62

* Base year

Sources: Heritage Foundation calculations sourced throughout the Index of Dependence on Government.

Table 1 • CDA 10-08 heritage.org

THE FISCAL CHALLENGES OF GROWING DEPENDENCE

Entitlements. The issue of dependence is particularly salient today when more and more Americans are about to begin their reliance on government for their retirement. At age 65, retirees are eligible to collect Social Security income, as well as health care benefits from Medicare or Medicaid.[2] Currently, these programs make up 41 percent of all non-interest federal program spending. Over the next two decades, that spending will increase to nearly 62 percent of non-interest spending as 10,000 baby boomers retire *per day* and begin to collect benefits. Jointly, these programs will enable the government dependence of nearly 80 million baby boomers.

This is particularly troubling because most of the soon-to-be users of these programs are middle-class to upper-class Americans who do not need government support. Because eligibility for these programs is linked to age, not financial need, multi-millionaires and billionaires collect the same benefits, such as subsidized prescription drugs through Medicare Part D, as do low-income retirees.

Paying for these middle-class and upper-class entitlements in the coming years will require unprecedented levels of deficit spending. According to the Financial Report of the United States, the amount of debt Americans expect to pay for these commitments is $56.4 trillion—$184,000 per American citizen.[3] This is an unsustainable level of debt sure to slow the economy and could force even higher rates of taxation in the future. The high costs of these programs, which will be shouldered by the children and grandchildren of baby boomers, could easily lead to further increases in dependence of future generations who would be more likely to depend on welfare during a slow economy, for instance. This snowballing of dependence—caused by reliance on Social Security, Medicare, and Medicaid—could send the country past a tipping point of sustainable dependence that could endanger the functioning of democracy itself.

Additionally, the growing cost illustrates the budgetary problem of allowing dependence to grow unchecked. One reason this growth will be so significant is that these programs grow on autopilot, which, in turn, perpetuates dependence since these programs are not subject to regular debate and evaluation. Unlike nearly all other program spending, Social Security, Medicare, and Medicaid are mandatory spending programs that operate outside of the annual budget process. This exemption entitles these programs to call on all federal revenues first, regardless of other budgetary priorities. Substantive policy reform is required if this automatic dependence is to be halted. The solution is to turn these programs into 30-year budgeted programs, subjecting the budgets to debate every five years.

Other policy reforms that emphasize independence and self-reliance must also be part of addressing the problems inherent in these and other programs. The concept of a safety net ought to be restored to gear Social Security, Medicare, and Medicaid toward those who truly need these programs. This can be accomplished by relating benefits to retirees' income and encouraging personal savings during working years.

Growth in the Non-Taxpaying Population. The challenges that Congress faces in reforming these entitlement programs are heightened by the rapid growth of other dependence-creating programs, such as subsidies for food and housing and college financial aid, and by the growing number of Americans who pay nothing for them. How likely is Congress to reform entitlements as quickly as it should when so many voters pay little or nothing for the other dependence-creating programs contained in this Index? Can Congress rein in the massive middle-class entitlements in an environment of fast-growing dependence programs?

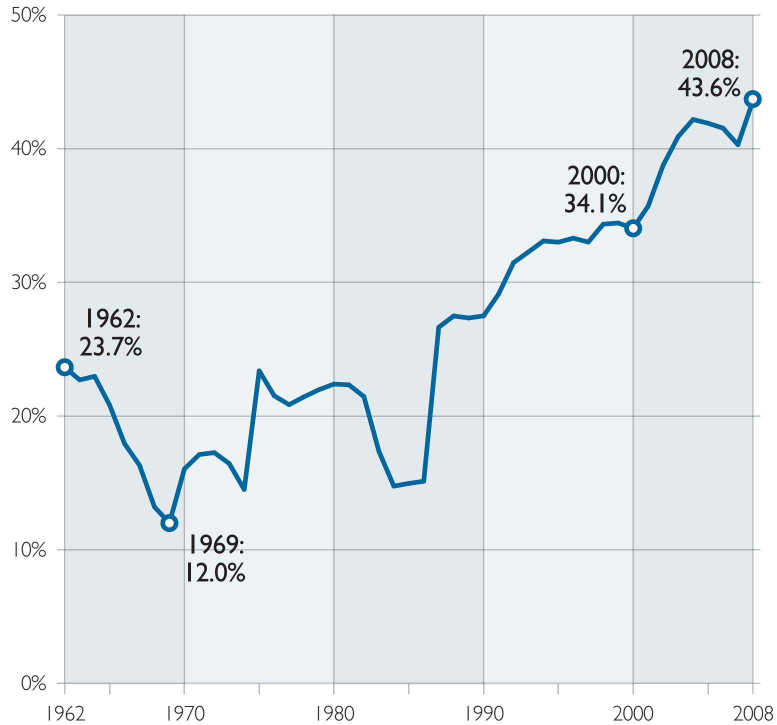
In 1962, the first year measured in the Index of Dependence on Government, the percentage of people who do not pay federal income taxes themselves and who are not claimed as dependents by someone who pays federal income taxes stood at 23.7 percent; it fell to 12 percent by 1969 before beginning a ragged but ultimately steady increase. By 2000, the percentage was 34.1 percent, and 43.6 percent in 2008.[4] In short, the country may be rapidly approaching a point where one-half of "taxpay-

2. Medicaid also provides health care for low-income, non-retired families.

3. This total reflects the debt associated with all federal government commitments, which includes, but is not limited to, the three entitlements—Social Security, Medicare, and Medicaid.

More Americans Not Represented on Tax Returns

Percentage of U.S. Population Not Represented on a Taxable Return



Note: Figures for 1977 to 1982 were extrapolated due to unavailable data.

Source: Heritage Foundation calculations based on data from the Internal Revenue Service, "Individual Income Tax Returns," Publication 1304, 1962–2008, Table 1.4, and various IRS reports.

Chart 1 • CDA 10-08 heritage.org

ers" *do not pay taxes*, while receiving generous federal benefits.

This trend should concern everyone who supports America's republican form of government. If the citizens' representatives are elected by an increasing percentage of voters who pay no income tax, how soon will it be before these representatives respond more to demands for yet more entitlements and subsidies from non-payers than to the pleas from taxpayers to exercise greater spending prudence?

1) THE PURPOSE AND THEORY OF THE INDEX

The 2010 Index of Dependence on Government is divided into four major sections: Section 1 explains the purpose and theory behind the Index; Section 2 reviews major policy changes in the five program areas; Section 3 features a methodology that describes how the Index is constructed; Section 4 discusses the Index in terms of the number of Americans who depend on government programs.

The Index of Dependence is designed to measure the pace at which federal government services and programs have grown in areas in which private or community-based services and programs exist or existed to address the same or similar needs. By compiling and condensing the data into a simple annual score (composed of the scores for the five components), the Index provides a useful tool for analyzing dependence on government. Policy analysts and political scientists can also use the Index and the patterns it reveals to develop forecasts of trends and ponder how these trends might affect the politics of the federal budget.

The Index uses data drawn from a carefully selected set of federally funded programs. The programs were chosen for their propensity to duplicate or replace support traditionally provided to needy people by local organizations, neighborhoods, communities, and families, such as shelter, food, monetary aid, education and health care, employment training, or jobs.

In calculating the Index, the expenditures for these programs are weighted to reflect the relative importance of each service (for instance, shelter, health care, or food). The degree of a person's dependence will vary with respect to the need. For example, a homeless person's first need is generally shelter, followed by nourishment, health care, and income. Center for Data Analysis analysts weighted the program expenditures based on this hierarchy of needs, which produces a weighted Index of expenditures centered on the year 1980.

4. IRS data from "Individual Income Tax Returns," Publication 1304, 1962–2008, Table 1.4 and other numbered tables from those years; Heritage Foundation calculations.

Historically, private individuals and local entities have provided more assistance to needy members of society than they do today. Particularly during the 20th century, government gradually offered more and more services that were previously provided by self-help and mutual-aid organizations.[5] Lower-cost housing is a good example. Mutual-aid, religious, and educational organizations long have aided low-income Americans with limited housing assistance, but after World War II, the federal and state governments began providing the bulk of low-cost housing. Today, the government provides nearly all housing assistance for the poor and low-income.

Health care is another example of this pattern. Before World War II, Americans of modest income typically obtained health care and health insurance through a range of community institutions, some operated by churches and social clubs. That entire health care infrastructure has since been replaced by publicly provided health care insurance, largely through Medicaid and Medicare. Regardless of whether the medical and financial results are better today, the relationship between the people who receive health care assistance and those who pay for it has changed fundamentally. Few would dispute that this change has negatively affected the total cost of health care and the politics of the relationships among patients, doctors, and hospitals.

Financial help for those in need has also changed profoundly. Local, community-based charitable organizations once provided the majority of the aid, which resulted in a personal relationship between those who receive assistance and those in the community who provide it. Today, Social Security and other government programs provide much or all of the income to indigent and modest-income households. Nearly all the income that was once provided to temporarily unemployed workers by unions, mutual-aid societies, and local charities is now provided by federal income, food, and health programs. Indeed, income assistance is quickly becoming a government program with little, if any, connection to the local civil society.

This shift from local, community-based mutual-aid assistance to anonymous government payments has clearly altered the relationship between the person in need and the service provider. In the past, a person in need depended on help from people and organizations in his or her local community. The community representatives were generally aware of the person's needs and tailored the assistance to meet those needs within the community's budgetary constraints. Today, housing and other needs are addressed by government bureaucrats who have little or no ties to the community in which the needy person lives.

Both cases involve a dependent relationship. However, the dependent relationship with elements of the civil society includes healthy *expectations* of the recipient's future civil viability and ability to aid another person in turn. The dependent relationship with the political system has *no reciprocal expectations*. The former relationship is essential to the existence of civil society itself. The latter is usually based on unilateral aid where the recipient's return to civil viability (or lack thereof) is not a factor. Indeed, the "success" of such government programs is frequently measured by the program's growth rather than the outcomes it produces. While the dependent relationship with civil society leads to a *balance* between the interests of the needy person and the community, the dependent relationship with the government runs the risk of generating political pressure from interest groups—such as health care organizations, local communities, and the aid recipients themselves—to expand and cement federal support.

The Index of Dependence on Government provides a way of assessing the magnitude and implications of the change in government dependence in American society. The steps to prepare this year's Index are described in the methodological section near the end of this paper, and the Index is based principally on historical data from the President's fiscal year (FY) 2011 annual budget proposal.[6] The last year measured in the 2010 Index

5. Mutual-aid societies consist of individuals who pledge to help each other with financial, employment, and health challenges, setting up a low-cost mutual insurance arrangement. Today, very few mutual-aid societies exist in the United States. Perhaps the best known is the Security Benefit Association in Topeka, Kansas. See David Beito, *From Mutual Aid to the Welfare State: Fraternal Societies and Social Services, 1890–1967* (Chapel Hill, N.C.: University of North Carolina Press, 2000).

6. Office of Management and Budget, *Historical Tables: Budget of the U.S. Government, Fiscal Year 2011*, at *http://www.gpoaccess.gov/usbudget/fy11/pdf/hist.pdf* (September 24, 2010).

was FY 2009. The Center for Data Analysis used a simple weighting scheme and inflation adjustment to restate these publicly available data. CDA analysts encourage replication of their work and will gladly provide the data that support this year's Index upon request.

2) THE FIVE INDEX COMPONENTS

CDA analysts began by reviewing the federal budget to identify federal programs and state activities supported by federal appropriations that fit the definition of dependence—which means that a reasonable argument can be made that the program or activity provides goods or services that have crowded out or constrained private or local government alternatives. Furthermore, the immediate beneficiary of the program or activity must be an individual.

This definition generally excludes state programs that could foster dependence. However, federally funded programs in which the states act as intermediaries are included.

Elementary and secondary education is the principal state-based program excluded under this stipulation. Post-secondary education is the only part of government-provided education included in the Index.[7] Military and federal employees are also excluded because national defense is a primary function of the federal government and thus does not promote dependence as measured by the Index.

CDA analysts then divided the qualifying programs into five broad components:

1. Housing
2. (a) Health care and (b) Welfare
3. Retirement
4. Higher education
5. Rural and agricultural services

The following sections discuss the pace and content of policy changes in these five components.

1. Housing.[8] The Department of Housing and Urban Development (HUD) was created in 1965 by consolidating several independent federal housing agencies into a single presidential cabinet department. The purpose of the consolidation was to elevate the importance of government housing assistance within the constellation of federal spending programs. At that time it was believed that the destructive urban riots that broke out in many cities in the early 1960s were a consequence of poor housing conditions and that these conditions were contributing to urban decay. Two initiatives—housing assistance and urban revitalization—were combined into a single federal department.

HUD spending still largely reflects that dual mission. In any given year, about 80 percent of HUD's budget is targeted at housing assistance, and the other 20 percent is focused on urban issues by way of the Community Development Block Grant (CDBG) program. Given the nature of these programmatic allocations, HUD budgetary and staff resources are concentrated on low-income households to an extent unmatched by any other federal department.

Within the 80 percent of the HUD budget spent on housing assistance are a series of means-tested housing programs, some of which date back to the Great Depression. Typically, these programs provide low-income people, including the elderly and disabled, with apartments at monthly rents scaled to their incomes. The lower the income, the lower the rent. Traditionally, HUD and the local housing agencies provide eligible low-income households with "project-based" assistance, an apartment unit that is owned and operated by the government.

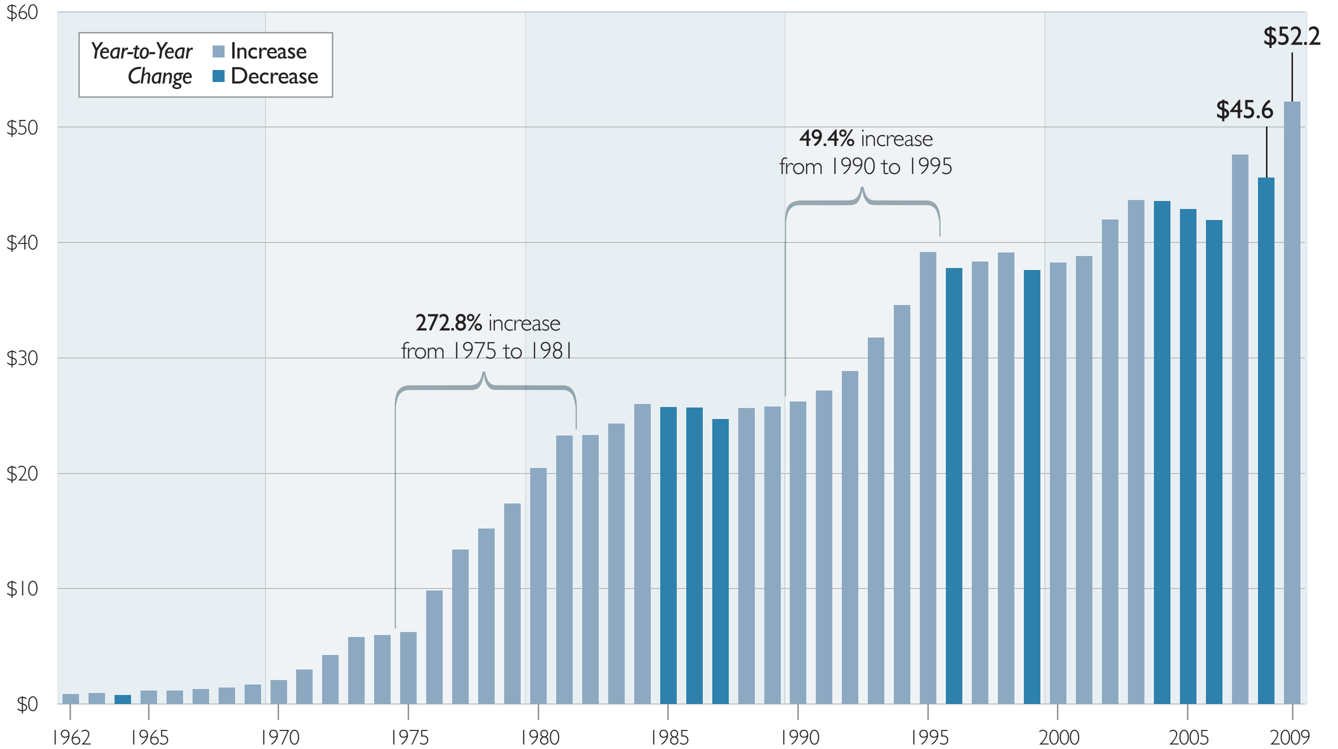
Public housing projects have historically been the most common form of such assistance, but they began to fall out of favor in the 1960s because of the rampant decay and deterioration that followed from concentrating too many troubled, low-income families in a single complex or neighborhood. Periodically, a new form of project-based program is adopted as "reform," but the new program tends to fall out of favor after several years of disappointing results. HOPE VI is the most recent form of project-

7. The exclusion of elementary and secondary education from the Index reflects the CDA determination that when it comes to elementary and high schools, aid historically provided by government probably has *not* crowded out aid once generally provided by civil society. However, federally funded and guaranteed financial aid for post-secondary education *does* compete with privately provided financial assistance.

8. This section was written by Ronald D. Utt, Herbert and Joyce Morgan Senior Research Fellow in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation.

Housing Assistance Highest in History of Index

Expenditures in Billions of 2005 Dollars



Source: Office of Management and Budget, *Historical Tables: Budget of the United States Government, Fiscal Year 2011*, 2010, Table 3.2, pp. 56, 63, and Table 12.3, pp. 267, 278.

Chart 2 • CDA 10-08 heritage.org

based assistance, but high costs and low benefits led the George W. Bush Administration to attempt, unsuccessfully, to terminate the program in 2006. Efforts are now underway by some in the Obama Administration to increase the program's funding.

HUD also provides "tenant-based" housing assistance to low-income households in the form of rent vouchers and certificates. These certificates help low-income people rent apartments in the private sector by covering a portion of the rent. The lower the person's or family's income, the greater the share of rent covered by the voucher or certificate. Vouchers were implemented in the early 1970s as a cost-effective replacement for public housing and other forms of expensive project-based assistance; but vouchers still account for only a portion of housing assistance because of industry resistance to terminating the lucrative project-based programs.

Finally, HUD provides block grants to cities and communities through the CDBG program according to a needs-based formula. Grant money can be spent at a community's discretion among a series of permissible options. Among the allowable spending options is additional housing assistance, which many communities use to provide assistance to a greater number of low-income households. In 2005, President Bush proposed transferring CDBG from HUD to the Department of Commerce and reducing funding for the program.

Although HUD programs are means-tested to determine eligibility, they are not entitlements. As a result, many eligible households do not receive any housing assistance because of funding limitations. In many communities, the waiting lists for housing assistance are long—up to several years—and in some cases local housing authorities no longer add new families to the list because there is simply no prospect of newer families receiving an apartment in the foreseeable future.

Recognizing that HUD housing assistance can create dependence among those who receive its benefits, some Members of Congress have attempted to extend the work requirements of the 1996 Personal Responsibility and Work Opportunity Reconciliation Act to HUD programs. Advocates for the poor have thwarted these efforts. To date, the most that can be required of a HUD program beneficiary is eight hours per month of volunteer service to the community or housing project in which he or she lives.

The complexity of HUD's changing mix of project-based housing assistance can make measuring dependence levels difficult, especially over time. For example, trends in inflation-adjusted HUD spending suggest that dependence has been rising for many years.[9] Alternative measures, however, such as periodic tabulations of the share of renters receiving some form of housing assistance, indicate no change over the same period. For example, inflation-adjusted HUD spending increased by 11.6 percent from 1993 to 1999, but the share of renters who received some form of rent subsidy fell from 18.4 percent to 17.8 percent during that same time, perhaps reflecting the shift to the more costly HOPE VI program. Census estimates are available only for 1993 and 1999, so it is difficult to determine the extent to which these numbers characterize the entire period.

After a mid-decade jump reflecting spending to rebuild infrastructure destroyed by Hurricanes Katrina and Rita, the housing component of the Dependence Index jumped significantly, and it will likely jump even more in subsequent years as mortgage bailout programs continue, and as the Obama Administration shifts federal housing policy from encouraging homeownership to creating more affordable rental units.

2(a) Health Care.[10] Increasing enrollment in public health care programs, particularly Medicare, Medicaid, and the Children's Health Insurance Program (CHIP), is leading to greater dependence on government. These three programs enrolled approximately 98.2 million individuals in 2009—amounting to 32 percent of the American population. Combined, these programs accounted for $886 billion in federal spending in 2009, which represents 35.8 percent of national health expenditures and 6.2 percent of GDP. Government spending in 2009 on Medicare, Medicaid, and CHIP was 122 percent greater than the $399.1 billion spent on these programs in 1999, just a decade before.

In its yearly survey of health insurance coverage, the U.S. Census Bureau published figures in 2009 that underscore the current trend toward greater government dependence.[11] The percentage of Americans with private health insurance is on the decline, mostly as a result of the steady erosion of employer-based coverage, while the percentage of Americans on government programs is rising even faster, in large part due to Medicaid and CHIP expansions and an aging population that is increasing Medicare enrollment.

Medicare. Congress established Medicare in 1965 through Title XVIII of the Social Security Act. Medicare pays for health care for individuals ages 65 and over and for those with certain disabilities. Medicare enrollment has increased steadily since its enactment in 1965 due to increases in both population and life expectancy. In 1970, an estimated 20.4 million individuals were enrolled in Medicare. By 2009, the number of enrollees had more than doubled to 46.3 million.[12]

Over the next 10 years, the number of individuals enrolled in Medicare will increase drastically. There are more than 77 million baby boomers set to turn 65 starting in 2011. This will dramatically increase the number of individuals who pay for their health care using taxpayer dollars. Furthermore, the heavily subsidized coverage will increase overall demand for health care and place upward pressure on health care prices.

9. "Inflation-adjusted HUD spending" means that growth in spending due solely to inflation has been subtracted from the amounts referenced in this section.

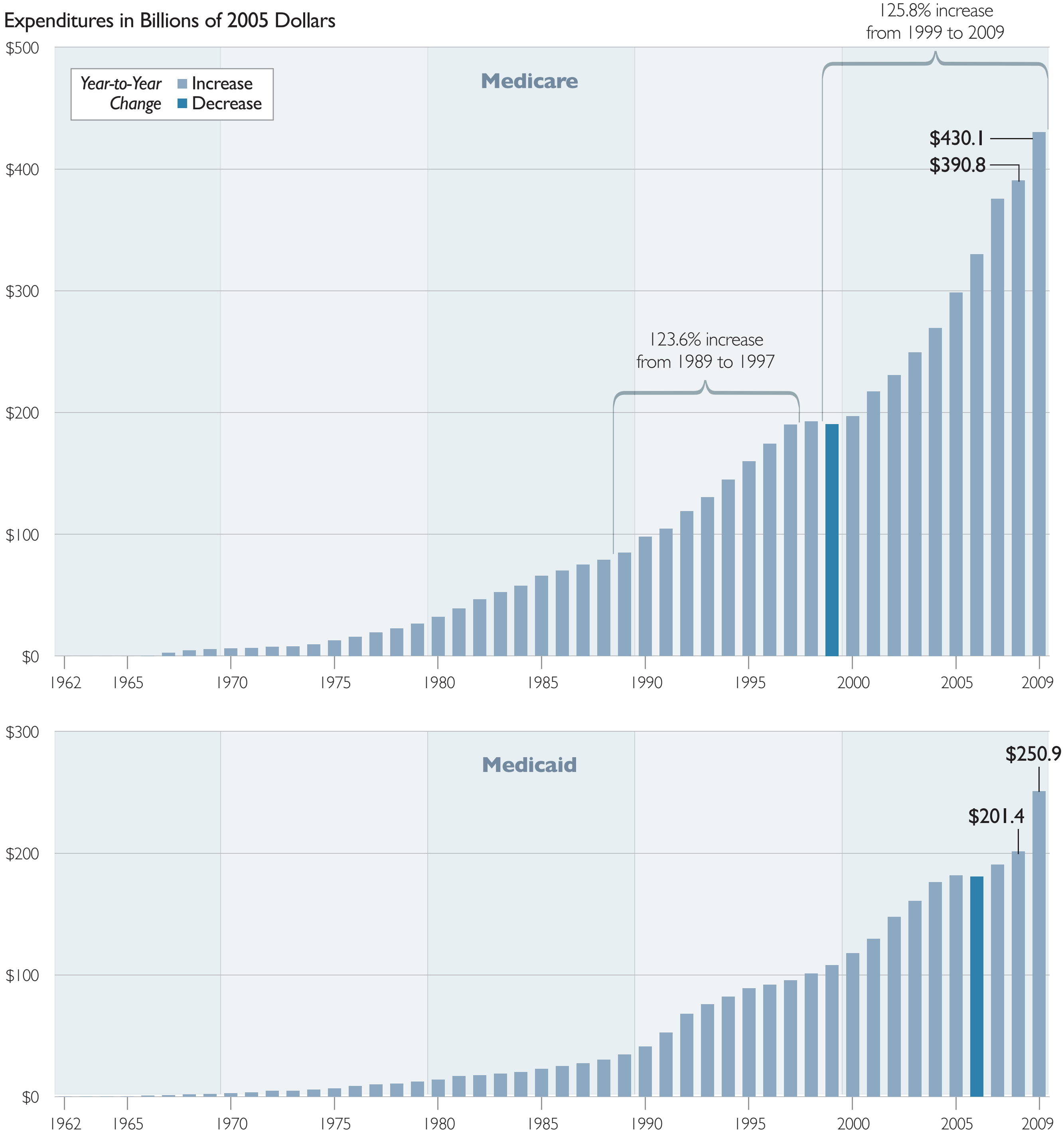
10. This section was written by Brian Blase, Policy Analyst in the Center for Health Policy Studies at The Heritage Foundation.

11. U.S. Census Bureau, "Income, Poverty, and Health Insurance Coverage in the United States: 2008," September 2009, at *http://www.census.gov/prod/2009pubs/p60-236.pdf* (September 24, 2010).

12. Centers for Medicare and Medicaid Services (CMS), "2010 Annual Report of the Boards of Trustees of the Federal Hospital Insurance and Federal Supplementary Medical Insurance Trust Funds," at *https://www.cms.gov/ReportsTrustFunds/downloads/tr2010.pdf* (September 24, 2010), and CMS, "Medicare Enrollment: National Trends, 1966–2008," at *http://www.cms.gov/MedicareEnRpts/Downloads/HISMI08.pdf* (September 24, 2010).

While Medicare is the primary source of health insurance for this population, many enrollees have supplemental private sources of coverage, such as employer-provided retiree coverage. However, subsidized public coverage—such as the addition of a universal prescription-drug benefit in 2003—crowds out private coverage alternatives. For instance, two-thirds of all Medicare enrollees had

Medicaid and Medicare Costs—Growing Fast



Source: Office of Management and Budget, *Historical Tables: Budget of the United States Government, Fiscal Year 2011*, 2010, Table 3.2, p. 63, and Table 12.3, p. 266.

Chart 3 • CDA 10-08 heritage.org

prescription-drug coverage from another source before the new Medicare drug benefit was enacted.[13] According to an analysis by Frank Lichtenberg and Shawn Sun, the new drug benefit resulted in a 72 percent crowd-out of private coverage. For every seven prescriptions paid for by the government, five would have otherwise been financed privately.[14] Additionally, Medicare provides disincentives for people to work beyond age 65, which further increases dependence. Today, less than 30 percent of men ages 65 to 69 remain employed, down from 46 percent in 1960, when people died much younger.

Medicaid and CHIP. Medicaid, the joint federal–state health care program for certain categories of the poor, was also established in 1965 through Title XIX of the Social Security Act. In 2009, 46.9 million Americans were enrolled in Medicaid, an increase of 3.3 million individuals in just one year and an increase of 16.1 million people since 1999. Medicaid serves a diverse population of the poor, including children, mothers, the elderly, and the disabled. In 2009, 53 percent of Medicaid enrollees were children,[15] although roughly two-thirds of Medicaid spending went to the elderly and the disabled, who are much more likely to have long-term care needs. The national cost of Medicaid in 2009 was estimated at $378 billion.[16]

The structure of the Medicaid program varies from state to state because states can determine their own eligibility and benefit levels, provided they meet a minimum federal standard. States have used this flexibility to expand eligibility further up the income scale and to offer generous benefit packages. Indeed, a majority of both Medicaid enrollees and spending are for optional groups or services. The generous federal reimbursement that states receive for Medicaid spending encourages states to expand their Medicaid programs far beyond the point they would if state taxpayers absorbed the full cost.

These incremental Medicaid expansions and the addition of the Children's Health Insurance Program[17] have increased the number of individuals eligible for government health programs. CHIP has led many working families who would otherwise enroll their children in private coverage to opt for public coverage instead. The Congressional Budget Office (CBO) concluded that private coverage crowd-out from CHIP expansions ranges from 25 percent to 50 percent.[18] In June 2009, 5 million children were enrolled in CHIP—an increase of 130,000 children from June 2008 and an increase of 3.6 million children from a decade earlier.

Legislative Changes in 2009. The passage of the economic stimulus package and the expansion of CHIP in early 2009 led to a greater government role in health care provision. The stimulus bill consisted of an $87 billion bailout for state Medicaid programs that relieved many states—at least temporarily—of the responsibility of cutting Medicaid programs down to affordable size. The bailout increased the national debt and will thus be paid for by future taxpayers. In addition, the Maintenance of Effort (MOE) requirement in the stimulus bill prohibited states from reducing their Medicaid eligibility requirements below those in place on July 1, 2008. The result: States that cannot afford their Medicaid programs are unable to reduce their size and are instead relying on tax increases or cutbacks in other state spending. Medicaid needs to be fundamentally restructured: The enormous amount of fraud must be reduced and states must rely less on

13. Joint Economic Committee, U.S. Congress, "Medicare Beneficiaries' Link to Drug Coverage," April 10, 2003.

14. Frank R. Lichtenberg and Shawn X. Sun, "The Impact of Medicare Part D on Prescription Drug Use by the Elderly," *Health Affairs*, Vol. 26, No. 6 (2007), pp. 1735–1744.

15. Kaiser Commission on Medicaid and the Uninsured, "Medicaid Enrollment: June 2009 Data Snapshot," February 2010, at *http://www.kff.org/medicaid/upload/8050.pdf* (September 24, 2010).

16. U.S. Department of Health and Human Services, Centers for Medicare and Medicaid Services, "National Health Expenditure Projections 2009–2019," forecast summary and selected tables, at *http://www.cms.gov/NationalHealthExpendData/downloads/proj2009.pdf* (September 24, 2010).

17. The State Children's Health Insurance Program (SCHIP) was enacted in 1997 to provide federal assistance to the state for providing health insurance to uninsured children in low-income working families whose parents' income was not low enough to qualify for Medicaid. The name has subsequently been changed by deleting the word "State."

18. Congressional Budget Office, "The State Children's Health Insurance Program," May 2007, p. 12, at *http://www.cbo.gov/ftpdocs/80xx/doc8092/05-10-SCHIP.pdf* (September 24, 2010).

taxpayer bailouts. In 2009, federal policy moved in the opposite direction.

The federal CHIP expansion passed by Congress also increased government dependence by expanding the program to include children of families whose income is three times the federal poverty level and higher. The expansion also increased government control by forcing federal mandates on state operations of the program. The new Congress has, in effect, begun to turn CHIP into another entitlement program like Medicaid.

Impact of Obamacare. Passage of the Patient Protection and Affordable Care Act in March 2010 will result in a massive increase in Medicaid enrollment and further government intervention in the form of generous subsidies for individuals to buy insurance in the government-designed health insurance exchanges. According to the CBO, by 2019, Obamacare will add 16 million individuals to Medicaid and 19 million people will receive government subsidies—at an average of $6,000—to purchase coverage through the state health insurance exchanges.[19] Obamacare, therefore, will cause a massive increase in dependence on government.

This growing dependence has a direct effect on those who pay taxes. Medicare and Medicaid are the two largest entitlement programs, and spending for both is expected to rocket upwards from already sky-high levels. By 2019, Medicare is projected to cost $978 billion and federal spending for Medicaid and CHIP is expected to reach $802 billion. Actuaries at the Centers for Medicare and Medicaid Services at the Department of Health and Human Services predict that by 2019 the government (federal and state) will fund 52 percent of all health care spending.[20] The CBO anticipates that these government health care programs will consume more than 12 percent of GDP by 2050.[21]

2(b) Welfare.[22] The 1996 Welfare Reform Act, or the Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA), replaced the decades-long Aid to Families with Dependent Children (AFDC), through which recipients were entitled to unconditional benefits, with the Temporary Assistance for Needy Families (TANF), a block grant program. Enacted during the Great Depression, AFDC, an old cash welfare program, was intended to provide financial assistance to needy dependent children. Over the decades, however, the program swelled and added adults, such as unemployed parents of enrolled children. Welfare rolls peaked in 1994, reaching more than 5 million cases, or 14.2 million individual recipients. Before welfare reform, one child in seven received AFDC.

An open-ended assistance program, AFDC granted states more money as their welfare rolls continued to increase. At the individual level, AFDC handed out benefits without any expectations from the recipients. That is, recipients were entitled to cash aid as long as they fell below the need standards set by the states. The entitlement created perverse incentives—discouraging work among able-bodied adult recipients and discouraging marriage.

Welfare reform effectively altered the fundamental premise of receiving public aid and ended it as an entitlement. Receiving assistance became temporary and tied to demonstrable efforts by the recipients to find work or take part in work-related activities. Self-sufficiency of the recipients became the focus. The successes of welfare reform are undeniable. Between August 1996 and September 2009, welfare caseloads declined by 57.5 percent, from 4.4 million families to 1.9 million families. The legislation was also successful in reducing child poverty, by 1.6 million children.[23]

The initial years after welfare reform brought significant progress, but by the late 1990s, most states

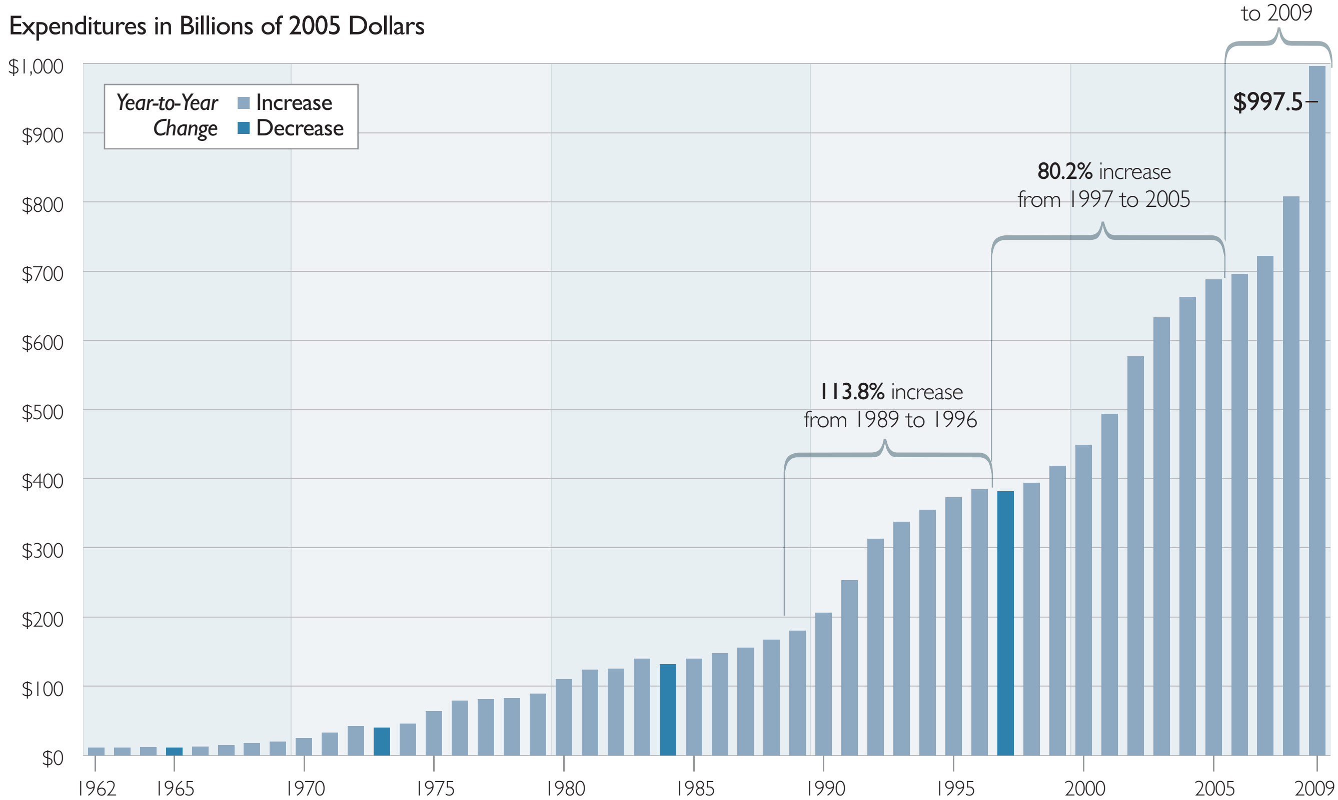
19. Congressional Budget Office, "H.R. 4872, Reconciliation Act of 2010," March 18, 2010, at *http://www.cbo.gov/doc.cfm?index=11355* (September 24, 2010).

20. Andrea M. Sisko *et al.*,"National Health Spending Projections: The Estimated Impact of Reform Through 2019," *Health Affairs*, Vol. 29, No. 10 (2010), at *http://content.healthaffairs.org/cgi/reprint/hlthaff.2010.0788v1* (October 4, 2010).

21. Congressional Budget Office, "The Long-Term Budget Outlook," June 2009, pg. 6, at *http://www.cbo.gov/ftpdocs/102xx/doc10297/06-25-LTBO.pdf* (September 24, 2010). See also, Congressional Budget Office, "The Budget and Economic Outlook: An Update," August 2009, at *http://www.cbo.gov/ftpdocs/105xx/doc10521/08-25-BudgetUpdate.pdf* (September 24, 2010).

22. This section was written by Christine Kim, Policy Analyst in the Domestic Policy Studies Department at The Heritage Foundation.

Welfare and Low-Income Health Care Assistance Jumps



Source: Office of Management and Budget, *Historical Tables: Budget of the United States Government, Fiscal Year 2011*, 2010, Table 3.2, p. 63, and Table 12.3, p. 267.

Chart 4 • CDA 10-08 heritage.org

had met the PRWORA's work goals, and the motivation to further reduce dependence and encourage work among recipients began to wane. The national TANF caseload has flatlined in recent years, and the percentage of TANF families who worked at least 30 hours per week (20 hours for those with young children) never rose above 38.3 percent, attained in FY 1999, and has hovered near 30 percent in more recent years.

In February 2006, after four years of debate, Congress reauthorized TANF under the Deficit Reduction Act. The new legislation reiterated the need to engage recipients in acceptable work activities, moving them to self-sufficiency. Once again, states are required to increase work participation and to reduce their welfare caseloads using the lower 2005 caseload levels as the new baseline, which essentially restarts the 1996 reform. As required by Congress, the Department of Health and Human Services also issued new regulations to strengthen work participation standards.

The 2006 reauthorization also contained a notable measure that began to rectify the inattention to the other two 1996 welfare reform goals: reducing unwed childbearing, and restoring stable family formation.[24] The erosion of marriage and family is a primary contributing factor to child poverty and welfare dependence, and it figures significantly in a host of social problems. A child born out of wedlock is seven times more likely to be poor than a child raised by married parents, and more than 80 percent of long-term child poverty occurs in broken homes or homes where the parents never married. Moreover, the absence of marriage and fathers in the

23. Original Heritage research in Christine Kim and Robert Rector, "Welfare Reform Turns Ten: Evidence Shows Reduced Dependence, Poverty," Heritage Foundation *WebMemo* No. 1183, August 1, 2006, at *http://www.heritage.org/Research/Reports/2006/08/Welfare-Reform-Turns-Ten-Evidence-Shows-Reduced-Dependence-Poverty.*

home negatively affects child development, educational achievement, psychological well-being, and propensity toward delinquency and substance abuse.[25]

For the last four decades, the unwed birth rate in America has been rising steadily, from 5.3 percent in 1960, to 40.6 percent in 2008.[26] Among blacks, 72.3 percent of all children born in 2008 were to unmarried parents, and 52.5 percent among Hispanics. Although the pace of growth in the proportions of births to unmarried women slowed in the immediate years after welfare reform, more recently, it has risen rapidly. From 2002 to 2008, the number of non-marital births increased by 26 percent.

In 2008, 1.7 million children were born to unmarried parents. Contrary to popular conception, the typical single mother is not a teen but in her twenties. Whereas in 1970, one-half of all out-of-wedlock births were to teens, in 2008, births to girls younger than 18 years of age comprise only 8 percent of such births. Sixty percent of out-of-wedlock births occur to women in their twenties.[27] Nor is the typical unwed mother a Murphy Brown type. About 43 percent are high school dropouts, and another 36 percent are high school graduates. Eighteen percent have had some college education; only 2 percent have a college degree.[28]

In the TANF reauthorization, Congress, for the first time, enacted a healthy-marriage initiative, allocating $100 million in TANF funds per year—less than 1 percent of total TANF expenditures in FY 2006—to local organizations that provide voluntary marriage-centered services and skills training to recipients. In his FY 2011 budget, President Obama proposed terminating this program and replacing it with another expensive jobs and employment scheme.[29] Funding for the program runs out on December 3, 2010, unless Congress extends it.

Furthermore, in February 2009, the Democrat-controlled Congress and the new Obama Administration enacted new legislation that essentially overturned the fiscal foundation of welfare reform and reverted to an AFDC-style funding scheme. States receive cash bonuses when they swell the welfare rolls. Moreover, covering 80 percent of the cost of new welfare caseloads, the federal government is giving states much more money than it did under the old welfare program. The new legislation clearly undercuts the incentives wrought by welfare reform to move individuals into work and self-sufficiency.

Despite the 1996 Welfare Reform Act, comprehensive welfare reform is far from achieved. Today's welfare system is a convoluted machinery of 70 programs, six federal departments, and a voluminous collection of state agencies and programs. A typical welfare recipient family could receive assistance from six or seven programs (e.g., TANF, Medicaid, food stamps, public housing, Head Start, and the Social Service Block Grant) administered by four different departments.[30]

Since President Lyndon Johnson declared the War on Poverty in 1964, the government has spent $15.9 trillion on means-tested welfare aid. The

24. In the opening section of PRWORA, Congress states the following: (1) "Marriage is the foundation of a successful society," and (2) "Marriage is an essential institution of a successful society which promotes the interests of children." Congress then states that the "increase in the number of children receiving public assistance is closely related to the increase in births to unmarried women. Between 1970 and 1991, the percentage of live births to unmarried women increased nearly threefold, from 10.7 percent to 29.5 percent." Public Law 104–193, § 101.

25. Robert Rector, "Married Fathers: America's Greatest Weapon Against Poverty," Heritage Foundation *WebMemo* No. 2934, June 16, 2010*, at http://www.heritage.org/Research/Reports/2010/06/Married-Fathers-Americas-Greatest-Weapon-Against-Child-Poverty*, and Patrick F. Fagan, Robert E. Rector, Kirk A. Johnson, and America Peterson, *The Positive Effects of Marriage: A Book of Charts* (Washington, D.C.: The Heritage Foundation, 2002), at *http://thf_media.s3.amazonaws.com/2002/pdf/positive_effects_of_marriage.pdf*.

26. Brady E. Hamilton, Joyce A. Martin, and Stephanie J. Ventura, "Births: Preliminary Data for 2008," *National Vital Statistical Reports*, Vol. 58, No. 16, April 6, 2010, at *http://www.cdc.gov/nchs/data/nvsr/nvsr58/nvsr58_16.pdf* (September 24, 2010).

27. Stephanie J. Ventura, "Changing Patterns of Nonmarital Childbearing in the United States," National Center for Health Statistics *Data Brief* No. 18, May 2009, at *http://www.cdc.gov/nchs/data/databriefs/db18.htm* (September 24, 2010).

28. Sara McLanahan *et al.*, "The Fragile Families and Child Wellbeing Study: Baseline National Report," March 2003, at *http://www.fragilefamilies.princeton.edu/documents/nationalreport.pdf* (September 24, 2010).

29. Katherine Bradley and Robert Rector, "How President Obama's Budget Will Demolish Welfare Reform," Heritage Foundation *WebMemo* No. 2819, February 25, 2010, at *http://www.heritage.org/Research/Reports/2010/02/How-President-Obamas-Budget-Will-Demolish-Welfare-Reform.*

Obama Administration has worked rapidly to expand the welfare state further. President Obama's FY 2011 budget increases spending on programs for the poor to 42 percent above levels in FY 2008, President George W. Bush's last full year in office. If Obama's budget is enacted, total welfare spending would rise to $953 billion by 2011, and over the next 10 years, it would exceed $10 trillion. In the last two decades, growth in means-tested welfare spending has outpaced that of Social Security, Medicare, education, and defense.[31]

Too many of these welfare programs operate on means-tested eligibility, and without any real mechanism to break dependence. Twelve years after the reform, the welfare system still rewards non-work. Additional reform should focus on applying TANF principles to other failing welfare programs, in particular food stamps and public housing, that subsidize idleness and foster dependence, and remove the anti-marriage bias and economic marriage penalties inherent in other means-tested welfare programs (e.g., the Earned Income Tax Credit (EITC) for married couples with children).[32]

3) Retirement.[33] Since the time of President Franklin D. Roosevelt, the American retirement system has been described as a three-legged stool consisting of Social Security, employment-based pensions, and personal savings. Yet the reality is quite different. Almost half of American workers (about 78 million) are employed by companies that do not offer any type of pension or retirement savings plan. This proportion of employer-based retirement savings coverage has remained roughly stable for many years, and experience has shown that few workers can save enough for retirement without such a payroll-deduction savings plan. For workers without a pension plan, the reality of their retirement is closer to a pogo stick consisting almost entirely of Social Security.

Since 1935, Social Security has provided a significant proportion of most Americans' retirement incomes. The program pays a monthly check to retired workers and benefits to surviving spouses and children under the age of 18.[34] Monthly benefits are based on the indexed average of a worker's monthly income over a 35-year period, with lower-income workers receiving proportionately higher payments and higher-income workers receiving proportionately less. The lowest-income workers receive about 70 percent of their pre-retirement income, average-income workers receive 40 percent to 45 percent, and upper-income workers average about 23 percent.

However, the demographic forces that once made Social Security affordable have reversed, and the program is on an inexorable course toward fiscal crisis. To break even, Social Security needs at least 2.9 workers paying taxes for each retiree who receives benefits. The current ratio is 3.3 workers per retiree and dropping because the baby boomers produced fewer children and are now nearing retirement. The ratio will reach 2.9 per retiree in around 2015 and drop to two workers per retiree in the 2030s.

Current retiree benefits are paid from the payroll taxes collected from today's workers. Due to the effects of the recent recession, Social Security will not collect enough in taxes to pay for all of its promised benefits in both 2010 and 2011, and, starting in 2015, those deficits will become permanent.

From 1983 through 2009, workers paid more in payroll taxes than the Social Security program needed. These additional taxes were supposed to accumulate to help to finance retirement benefits for baby boomers. But these excess taxes were not saved or invested for the future. Instead, the money was used to finance other government programs. In return for the diverted revenue, Social Security's

30. Robert Rector, "Means-Tested Welfare Spending: Past and Future Growth," Heritage Foundation Testimony, March 7, 2001, at *http://www.heritage.org/Research/Welfare/Test030701b.cfm*.

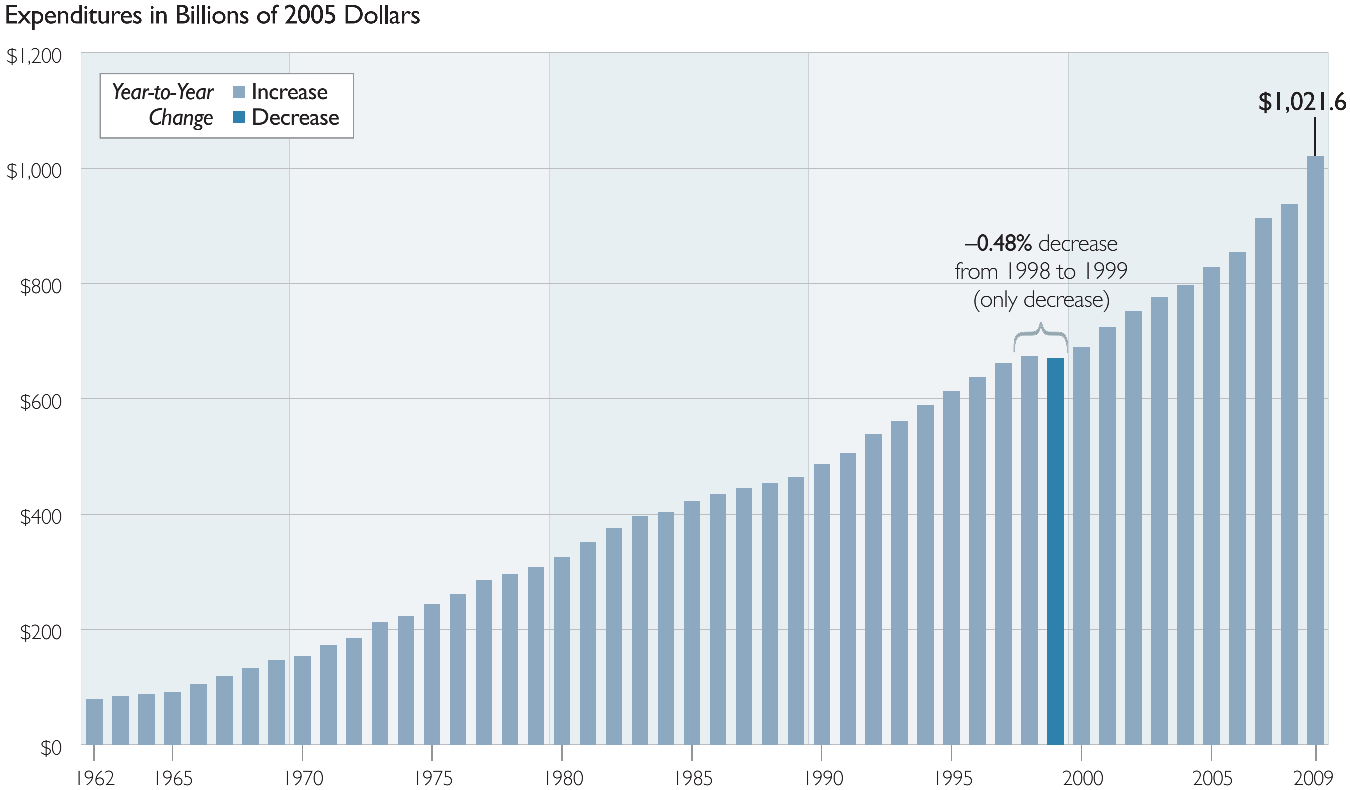
31. Katherine Bradley and Robert Rector, "Confronting the Unsustainable Growth of Welfare Entitlements: Principles of Reform and the Next Steps," Heritage Foundation *Backgrounder* No. 2427, June 24, 2010, at *http://www.heritage.org/Research/Reports/2010/06/Confronting-the-Unsustainable-Growth-of-Welfare-Entitlements-Principles-of-Reform-and-the-Next-Steps*.

32. *Ibid*.

33. This section was prepared by David C. John, Senior Research Fellow in Retirement Security and Financial Institutions in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation.

34. Social Security also has a separately financed disability program that is outside the scope of this discussion.

Baby Boomers Drive Social Security Spending



Source: Office of Management and Budget, *Historical Tables: Budget of the United States Government, Fiscal Year 2011*, 2010, Table 3.2, p. 63.

Chart 5 • CDA 10-08 heritage.org

trust fund received special issue U.S. Treasury bonds. In 2015, when Social Security starts redeeming its Treasury bonds, the federal government will be required to pay off the bonds through higher taxes or massive borrowing.

Social Security's uncertain future is a problem for all workers, but especially for roughly half of the American workforce that has no other retirement program. Few of these Americans have any significant savings, and they will depend heavily on the government for their retirement incomes.

This dependence is largely the result of government policies. By soaking up money that could otherwise be invested for the future, Social Security's high tax rate makes it much harder for lower-income and moderate-income workers to accumulate any significant savings.

Complex government regulations also discourage the expansion of occupational pensions to cover a higher proportion of the workforce. Over the last few decades, the cost of traditional pension plans has skyrocketed, and thousands of them have shut down. Efforts to develop innovative hybrid pension plans stalled when confusing laws and regulations resulted in lawsuits.

While most employers now offer defined-contribution plans, such as 401(k), these plans are subject to the Employee Retirement Income Security Act (ERISA). ERISA regulations are especially onerous to smaller employers, who usually lack the resources to hire a good funds manager and the necessary knowledge of the complex legal requirements. As a result, small businesses hesitate to offer retirement plans to their workers for fear of accidentally violating a regulation.

A simpler, less regulated account suitable to smaller businesses would go a long way toward increasing the number of workers with retirement savings. Simplified automatic enrollment procedures, automatic investment choices, procedures that allow savings to follow the worker from employer to employer, and better annuity choices would also help. The Automatic IRA, which incorporates these features and has been endorsed by such diverse publications as *National Review* and *The New York Times*, is one such simple retirement savings plan. Regrettably, until these policies move from theory to reality, Americans face increased dependence on a government-managed Social Security system that cannot possibly meet their needs. This dependence is likely to increase if millions of Americans fail to save enough for a comfortable retirement since such a development would put pressure on legislators to provide additional taxpayer-financed income programs.

4) Higher Education.[35] Federal post-secondary education spending continues to grow at a rapid pace. During the 2008–2009 school year, total federal spending on student aid programs (including tax credits and deductions, grants, and loans) was \$117 billion[36]—making total federal aid 91 percent higher than for the 1998–1999 school year (inflation-adjusted). In the 2008–2009 school year, federal grant aid increased to \$24.8 billion, an 11 percent increase over the previous year—well ahead of the inflation rate.[37]

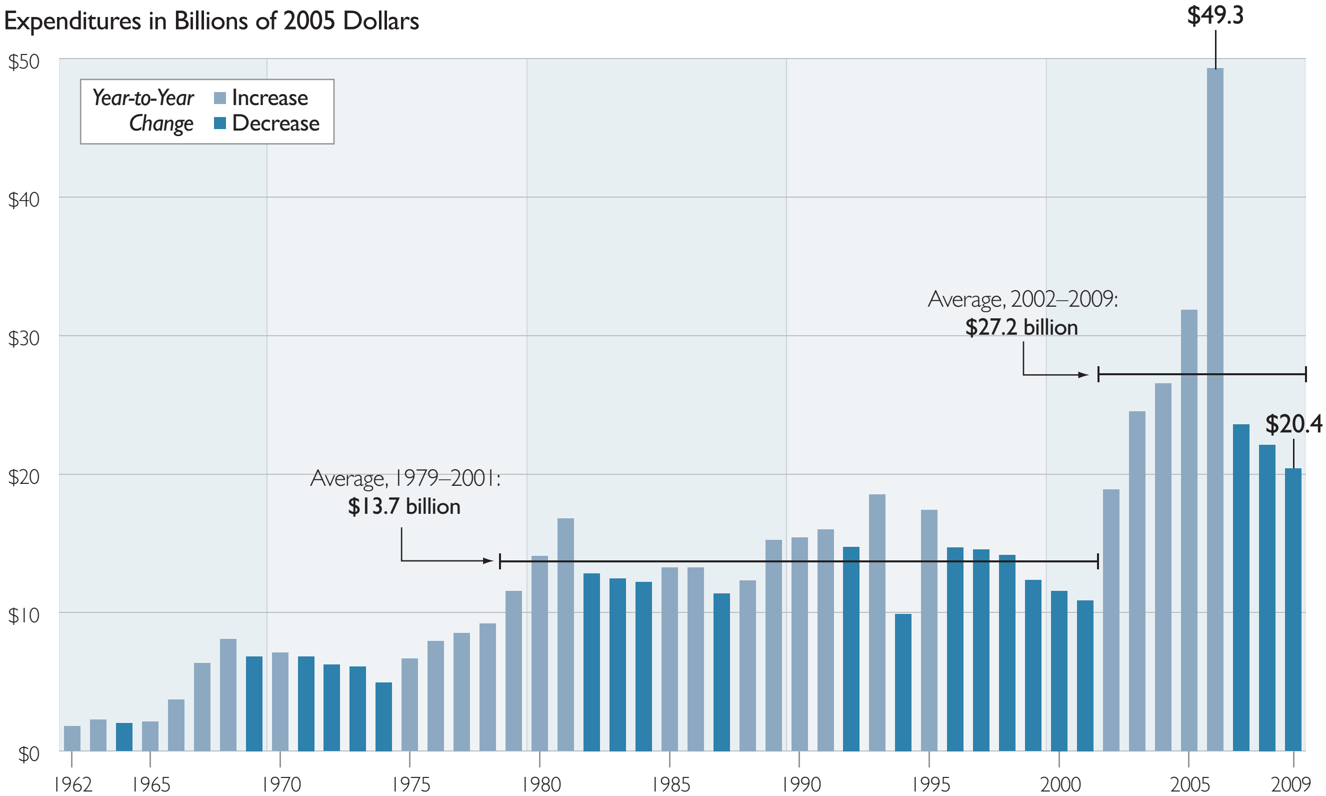
Over the last decade, increased federal higher-education subsidies have increased the number and percentage of post-secondary students who depend on government aid. In the 2008–2009 school year, 6.1 million students received Pell Grant scholarships—compared to 3.9 million in school year 1998–1999.[38] Moreover, about half of all undergraduates take out federal Stafford loans. In all, federal borrowing increased by 15 percent from 2008 to 2009.[39]

Both federal spending and students' dependence on government is likely to rise in 2010 and 2011. The American Recovery and Reinvestment Act, signed into law by President Obama in February 2009, included an additional \$17.1 billion in funding for Pell Grants, appropriating new money for Pell awards in 2010 and providing funding to cover Pell shortfalls in 2009.[40] In seeking to make the United States the country with "the highest proportion of college graduates in the world by 2020," President Obama has pushed for significant increases in federal subsidies.[41] The President's 2011 budget request increases funding for federal grants, loans, and work study to \$173 billion—a 48 percent increase over the \$117 billion spent in 2009.[42] Moreover, "the administration's budget would provide a record \$34.8 billion in Pell grants to nearly 9 million students during the 2011–2012 award year."[43]

In addition to increases in federal higher-education spending, the federal Pell grant program became mandatory in 2010, ensuring future funding and growth for the (formerly discretionary) grant program. The Patient Protection and Affordable Care Act of 2010 contained a provision eliminating the Federal Family Education Loan (FFEL) program in favor of the federal Direct Loan Program. In so doing, the Obama Administration ended government-insured private-sector student loans, meaning that all new federally subsidized loans will originate with, and be serviced by, the Department of Education. The shift crowds private

35. This section was written by Lindsey Burke, Policy Analyst in education in the Domestic Policy Studies Department at The Heritage Foundation.
36. College Board, "Trends in Student Aid: 2009," at *http://www.trends-collegeboard.com/student_aid/pdf/2009_Trends_Student_Aid.pdf* (September 24, 2010).
37. *Ibid.*, p. 6.
38. *Ibid.*
39. *Ibid.*
40. U.S. Department of Education, "American Recovery and Reinvestment Act (ARRA)," May 7, 2009, at *http://www2.ed.gov/about/overview/budget/budget10/summary/appendix1.pdf* (September 24, 2010).
41. "Remarks: Obama at Carnegie Mellon University June 2, 2010," *Time: The Page*, at *http://thepage.time.com/remarks-obama-at-carnegie-mellon-university-june-2-2010/* (September 24, 2010).
42. U.S. Department of Education, "Summary of Discretionary Funds, FY 2011 Request," January 21, 2010, at *http://www2.ed.gov/about/overview/budget/budget11/summary/appendix1.pdf* (September 24, 2010).
43. U.S. Department of Education, "Fiscal Year 2011 Budget Summary–February 1, 2010," at *http://www2.ed.gov/about/overview/budget/budget11/summary/edlite-section1.html* (September 24, 2010).

Era of Big Education Spending Continues



Source: Office of Management and Budget, *Historical Tables: Budget of the United States Government, Fiscal Year 2011*, 2010, Table 3.2, p. 63, and Table 12.3, p. 259.

Chart 6 • CDA 10-08 heritage.org

lenders out of the student loan market and increases taxpayer exposure to student defaults, likely increasing costs over time. While long-term cost increases for taxpayers are likely as a result of the elimination of the FFEL program, short-term costs are also likely, primarily from the estimated 404 new employees that will be hired by the Department of Education in 2011 to oversee the increase in Direct Loan volume.[44] Costs to taxpayers are also likely to rise significantly in the coming decades with the Obama Administration's proposal to forgive student loan debt. In his 2010 State of the Union Address, President Obama stated that he will make higher education costs manageable by "forgiving all remaining debt after 10 years of payments for those in public service work and 20 years for all others."[45]

Increases in federal student aid subsidies over the years have done nothing to mitigate ever-rising college costs. Tuition and fees at public and private four-year institutions rose 6.5 percent and 7.3 percent, respectively, after adjusting for inflation, from the 2008–2009 academic year to the 2009–2010 academic year. In the decade from 2000 to 2010, tuition and fees rose by an average annual rate of 4.9 percent at public universities.[46] Since 1982, the cost of college tuition and fees has increased 439 percent—more than four times the rate of inflation.[47]

44. *Ibid.*

45. Mike Allen, "President Obama, Vice President Biden Unveil Middle-Class Agenda," *Politico*, January 25, 2010, at *http://www.politico.com/news/stories/0110/31951_Page3.html* (September 24, 2010).

46. College Board, "Trends in College Pricing: 2009," at *http://www.trends-collegeboard.com/college_pricing/pdf/2009_Trends_College_Pricing.pdf* (September 24, 2010).

Increases in federal subsidies for college have led to the increases in college tuition and fees. Economist Richard Vedder argues that "some of these [federal] financial aid programs have contributed mightily to the explosion in tuition and fees in modern times."[48] Moreover, increases in federal higher-education subsidies have enabled universities to raise tuition and have made students less sensitive to cost increases. There is also little reason for the federal government to be in the student lending market at all. Vedder also notes that "It is not clear that higher education has major positive spillover effects that justify government subsidies in the first place, and the private loan market that can handle anything from automobile loans to billion-dollar government bond sales can handle financial assistance to students if necessary."[49]

Increasing federal subsidies for college will not solve the problem of ever-increasing college costs. Indeed, decades of increasing federal subsidies for college have enabled universities to raise tuition and fees, exacerbating the college cost problem. Instead of continuing to expand the government's role in student lending, federal subsidies should be limited to those students with the greatest financial need. Restrictions on the number of years that students can have access to federal subsidies would also likely begin to tackle the college cost problem.[50]

5) Rural and Agricultural Services.[51] Much of the rapid increase in "rural and agricultural assistance" dependence is rooted in farm subsidy programs. A multitude of farm subsidies (e.g., direct payments, countercyclical payments, market assistance loans, and non-recourse loans) generally work together to compensate farmers for low crop prices. Conservation payments pay farmers to initiate conservation projects or to simply stop farming their land. Export subsidies effectively lower the price of American products so that they can undercut international competitors.[52]

Farm subsidy supporters often describe farmers as impoverished victims of unpredictable weather and large global economic forces. In reality, American farmers are doing quite well. The average farmer has a net worth of $895,756[53] (double the national average of household wealth), an annual income of $81,670[54] (approximately 27 percent above the national average), and lives in a rural area with a significantly lower cost of living. The failure rate for farms is just one-sixth the rate of other businesses.

Yet farm subsidies have become America's largest corporate welfare program. The majority of subsidies go to commercial farms, which report average incomes of $200,000 and net worth of nearly $2 million. By contrast, the bottom 80 percent of farmers receive just one-fifth of the subsidies.

Instead of being related to need, farm subsidies are based on two factors: which crops are grown and how much is grown. Approximately 90 percent of all farm subsidies go to growers of just five crops: wheat, corn, cotton, soybeans, and rice. Growers of most other crops are ineligible for most subsidy programs, regardless of need.

Farmers who plant more crops receive larger subsidies. This is where the economic logic of farm subsidies falls apart. Subsidies are intended to compensate farmers for low prices that result from an

47. Dan Lips, "Ways to Make Higher Education More Affordable," Heritage Foundation *WebMemo* No. 2785, January 29, 2010, at *http://www.heritage.org/Research/Lecture/The-Real-Costs-of-Federal-Aid-to-Higher-Education.*

48. Richard Vedder, "The Real Costs of Federal Aid to Higher Education," Heritage Foundation *Lecture* No. 984, January 12, 2007, at *http://www.heritage.org/Research/Lecture/The-Real-Costs-of-Federal-Aid-to-Higher-Education*.

49. *Ibid.*

50. *Ibid.*

51. This section was written by Brian M. Riedl, Grover M. Hermann Fellow in Federal Budgetary Affairs in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation.

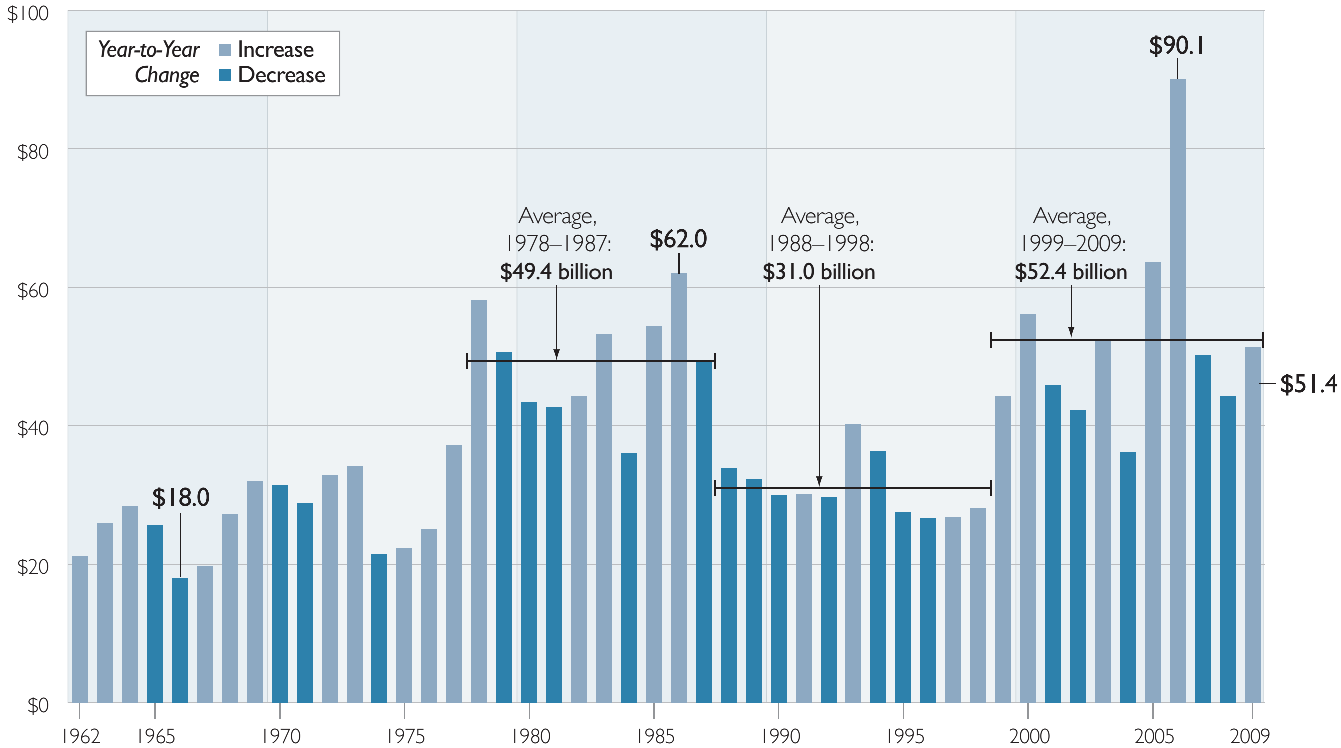
52. For more information on farm subsidies, see Brian M. Riedl, "How Farm Subsidies Harm Taxpayers, Consumers, and Farmers, Too," Heritage Foundation *Backgrounder* No. 2043, June 20, 2007, at *http://www.heritage.org/Research/Agriculture/bg2043.cfm.*

53. U.S. Department of Agriculture, Economic Research Service, "Farm Household Economics and Well-Being: Assets, Debt, and Wealth," Table 10, August 31, 2010, at *http://www.ers.usda.gov/briefing/wellbeing/farmnetworth.htm* (September 24, 2010).

54. U.S. Department of Agriculture, Economic Research Service, "Farm Household Economics and Well-Being: Farm Household Income," August 31, 2010, at *http://www.ers.usda.gov/briefing/wellbeing/ farmhouseincome.htm* (October 5, 2010).

Rural, Agricultural Programs—Spending Tops 1990s Levels

Expenditures in Billions of 2005 Dollars



Source: Office of Management and Budget, *Historical Tables: Budget of the United States Government, Fiscal Year 2011*, 2010, Table 3.2, pp. 56, 63, and Table 12.3, pp. 265, 271.

Chart 7 • CDA 10-08 heritage.org

oversupply of crops, but granting larger subsidies to farmers who plant the most crops merely encourages them to plant yet more crops, driving prices even lower and leading to calls for larger subsidies. Furthermore, while paying some farmers to plant more crops, the Conservation Reserve Program pays other farmers to plant fewer crops. One analyst accurately describes U.S. farm policy as "one foot on the break, one foot on the accelerator."[55]

Eventually, Congress acknowledged the failures of centrally planned agriculture. The 1996 Federal Agricultural Improvement and Reform Act[56] (also known as the Freedom to Farm Act) was designed to phase out farm subsidies by 2002 and allow the agricultural sector to operate as a free market. After spending just $6 billion on farm subsidies in 1996, Congress overreacted to a temporary dip in crop prices in 1998 (resulting from the Asian economic slowdown) by passing the first in a series of annual emergency bailouts for farmers.

By 2000, farm subsidies hit a record $30 billion. Farmers quickly grew accustomed to massive government subsidies, and competition for the farm vote induced a bipartisan bidding war on the eve of the 2002 elections. Lawmakers gave up on reform and enacted the largest farm bill in American history, projected to cost at least $180 billion over the following decade. Despite escalating costs and negative economic effects, farm socialism is now the overwhelming preference of Congress and the White House.

Farms' government dependence will almost certainly continue. Policymakers mistakenly see farm subsidies as the solution to, not a significant cause

55. James Bovard, "The 1995 Farm Follies," *Regulation*, Vol. 18, No. 3 (Summer 1995), at *http://www.cato.org/pubs/regulation/regv18n3/reg18n3-bovard.html* (October 5, 2010).

56. 7 U.S. Code § 7201.

of, low crop prices. Expensive disaster payments are doled out whether the weather is bad (crops destroyed) or good (oversupply lowers prices). Finally, farm subsidies have created an entitlement mentality among a class of farmers who will likely punish any elected officials who pursue reform. Currently, there are no plans to move farmers toward self-sufficiency.

Rather than fix this broken system, the 2008 farm bill made it worse.[57] Congress ignored President George W. Bush's call to subsidize only those farmers who earn less than $200,000 a year, and repealed key limits on the subsidies a farmer may receive. The bill created a permanent new disaster program, increased subsidy rates, and used gimmicks to cover up a spending increase of approximately $25 billion over 10 years. Even corn farmers, who already benefit from soaring prices resulting from federal ethanol policies, will continue to receive billions in annual subsidies. These anti-trade policies will also likely lead to retaliation by America's trading partners, harming American farmers and consumers. Congress overrode President Bush's veto of the farm bill, guaranteeing at least six more years of destructive farm policies.

Programs Used to Calculate Index Values

I. Housing
- Mortgage credit
- Housing assistance
- Community development block grants
- Urban development action grants
- Subsidized housing programs

II. Health and Welfare
- Health care services
- Health research and training
- Consumer and occupational health and safety
- Unemployment compensation
- Food and nutrition assistance
- Other income security
- Disease control (preventive health care services)
- Health resources and services
- Substance abuse and mental health services
- Grants to states for Medicaid
- Child nutrition programs
- Food stamp programs
- Family support payments to states
- Social services block grants
- Children and families service programs
- Training and employment services
- Unemployment trust fund

III. Retirement
- Medicare
- Social Security
- General retirement and disability insurance

IV. Education
- Federal higher education
- State higher education

V. Rural and Agricultural Services
- Farm income stabilization
- Agricultural research and services
- Community development
- Area and regional development
- Disaster relief and insurance
- Rural community advancement program
- Homeland Security disaster relief

Source: The Heritage Foundation

Table 2 • CDA 10-08 heritage.org

3) HOW THE INDEX OF DEPENDENCE ON GOVERNMENT IS CONSTRUCTED

After identifying the government programs that contribute to dependence, the Center for Data Analysis further examined the data to identify the components that contributed to variability. Relatively small programs that required little funding and short-term programs were excluded. The remaining expenditures were summed up on an annual basis for each of the five major categories listed in Table 2.[58] The program titles are those used by the Office of Management and Budget for budget function and sub-function in the budget accounting system.

The CDA analysts collected data for FY 1962 through FY 2009. Deflators centered on 2005 were employed to adjust for inflation.

Indices are intended to provide insight into phenomena that are either so detailed or complicated that simplification through arbitrary but reasonable rules is required for obtaining anything other than a rudimentary understanding. The Consumer Price Index (CPI) of the Bureau of Labor Statistics, for instance, is a series based on an arbitrarily selected "basket of goods" that the bureau surveys periodically for price changes. The components of this basket are weighted to reflect their relative importance to overall price change. Energy prices are weighted as more important than clothing prices. Multiplying the weight by the price produces a weighted price for each element of the CPI, and the total of the weighted prices produces the rough CPI score.

57. Brian M. Riedl, "Seven Reasons to Veto the Farm Bill," Heritage Foundation *Backgrounder* No. 2134, May 12, 2008, at *http://www.heritage.org/research/agriculture/bg2134.cfm*.

58. Office of Management and Budget, *Historical Tables: Budget of the U.S. Government, Fiscal Year 2011*, at *http://www.gpoaccess.gov/usbudget/fy11/pdf/hist.pdf* (September 24, 2010).

The Index of Dependence on Government generally works the same way. The raw (or unweighted) value for each program (i.e., the yearly expenditures for that program) is multiplied by its weight. The total of the weighted values is the Index value for that year.

The Index is calculated using the following weights:

1. Housing: 30 percent
2. Health care and welfare: 25 percent
3. Retirement: 20 percent
4. Higher education: 15 percent
5. Rural and agricultural services: 10 percent

The weights are "centered" on the year 1980. This means that the total of the weighted values for the Index components will equal 100 for 1980, which gives the Index a reference year from which all other Index values can be evaluated.

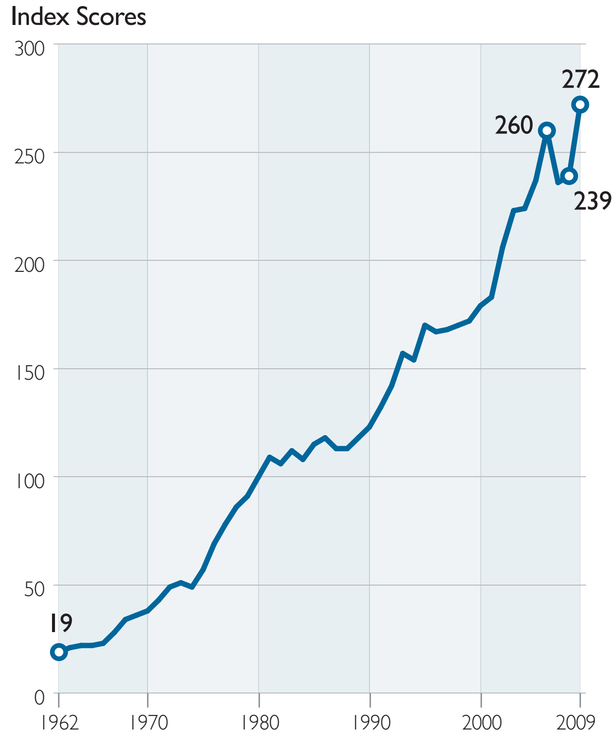
The CDA chose the year 1980 because of its apparent significance in American political philosophy. Many analysts view 1980 as a watershed year in U.S. history because it seems to mark the beginning of the decline in left-of-center public policy and the emergence of right-of-center challenges to policies based on the belief that social systems fail without the guiding hand of government.[59]

The Index certainly reflects such a watershed. Chart 8 plots the Index from 1962 to 2009. The scores have clearly drifted upward over the entire period.

There are two plateaus in the Index—the 1980s and the period from 1995 to 2001—that suggest that policy changes may significantly influence the Index growth rate. During the early 1980s, the growth of some domestic programs was slowed to pay for increased defense spending, and Congress enacted significant policy changes in welfare and public housing during the 1990s. Both of these cutbacks reduced the Index growth rate.

Chart 9 connects the Index to major public policy changes. The largest jump in the Index occurred during the Johnson Administration following the passage of the Great Society programs. The Johnson Administration not only launched Medicare and other health programs, but also vastly expanded the federal role in providing and financing low-income housing. The Index also jumped 92 percent (from 36 to 69) under the Nixon and Ford Administrations, when Republicans were funding and implementing substantial portions of the Great Society programs.

Dependence on Government Continues to Climb



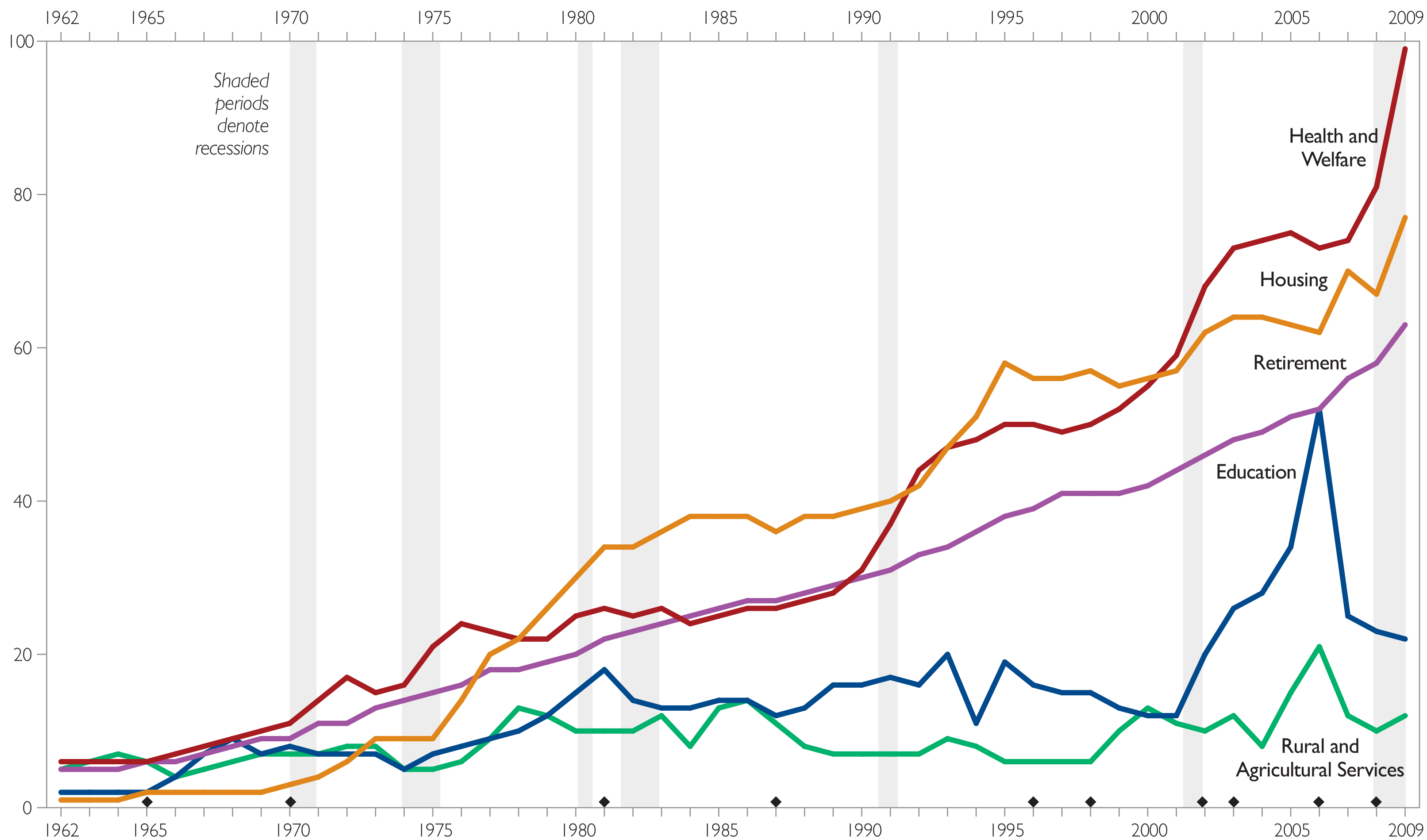
Source: Based on Heritage Foundation calculations sourced throughout the Index of Dependence on Government.

Chart 8 • CDA 10-08 heritage.org

The two periods of relatively more conservative public policy (the 1980s and 1995 to 2001) stand out clearly in Chart 9. The slowdowns in spending increases during the Reagan years and after the 1994 congressional elections produced two periods of slightly negative change in the Index. These periods saw significant retreats from the Great Society goals, particularly in the nation's approach to welfare. The return of budget surpluses during the last years of the Clinton Administration, however, led to significant spending increases for all of the components, particularly education and health care. Since then, the Index has grown at roughly the same rate as it has during the past 25 years.

59. See, for example, John Micklethwait and Adrian Wooldridge, *The Right Nation: Conservative Power in America* (New York: The Penguin Press, 2004), pp. 64–93.

Government Dependence Index Values Tied to Major Policy Changes



◆ Major Policy Changes

1965: Great Society programs: Medicare, Medicaid, Higher Education Act, Department of Housing and Urban Development

1970: Expansion of Social Security benefits

1981: First Reagan budget and tax cuts

1987: Extension of Social Security taxes to state and local government workers

1996: Welfare reform to include work requirement and Freedom to Farm Act

1998: Expansion of Medicaid to cover low-income children

2002: Expansion of agricultural subsidies, No Child Left Behind Act

2003: Passage of Medicare prescription drug benefit

2006: Hurricanes Katrina and Rita relief; Pell Grant expansion

2008: Recession-related programs

Source: Based on Heritage Foundation calculations sourced throughout the Index of Dependence.

Chart 9 • CDA 10-08 heritage.org

4) CALCULATION OF COVERED POPULATION

The Index reflects the growth of federal government programs that arguably crowd out or substitute for similar initiatives advanced by state and local governments or by organizations within civil society. Index values do not depend on the number of people who receive support through these programs, but that number nevertheless sheds additional light on what the Index illustrates.

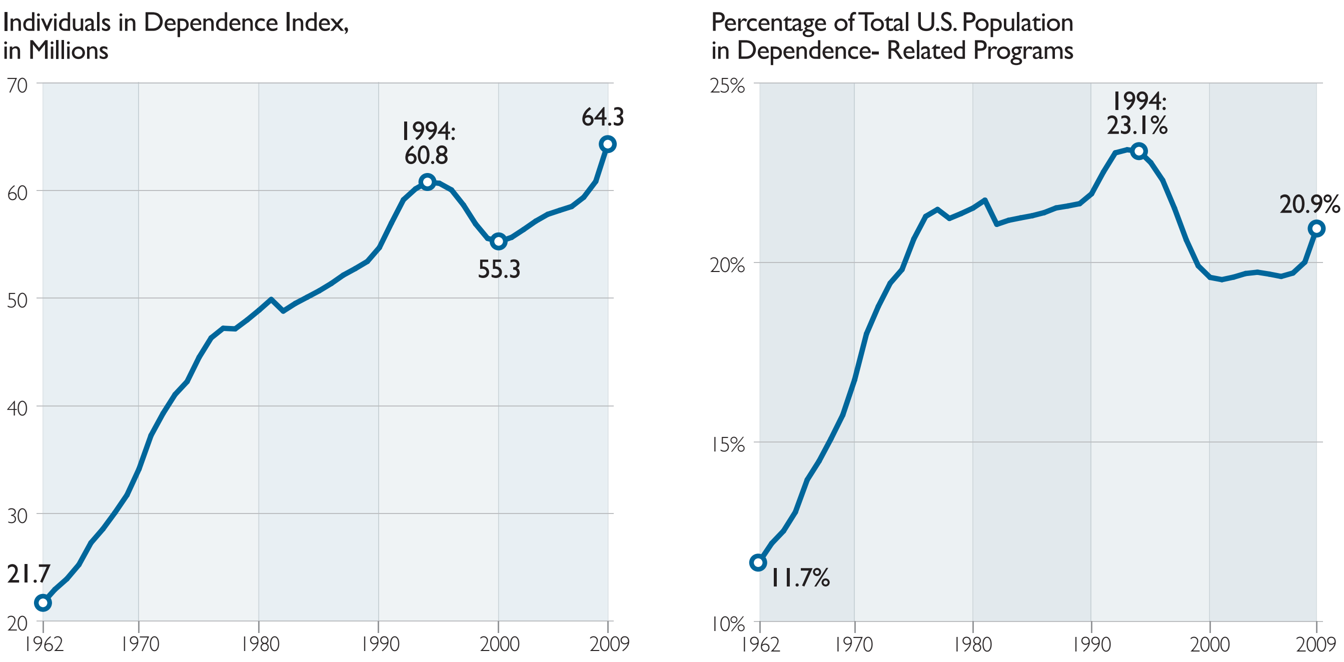
Data on the number of people enrolled or benefiting from the programs listed in Table 1 between 1962 and 2009 were drawn from a variety of public sources. A significant effort was made to eliminate duplicate enrollments. For example, many people who receive food stamps also receive medical services through Medicaid.

Chart 10 shows the annual number of program participants from 1962 through 2009. On the eve of the Great Society programs, some 21.7 million people (or 11.7 percent of the population) received assistance through the programs listed in Table 2 that existed at the time. Today, 64.3 million people (20.9 percent of the total U.S. population) receive some level of assistance through the programs included in the Index.

Growth in income and non-financial support among program participants has accompanied the increase of people who receive assistance. Per capita financial and non-financial support (after adjusting for inflation to year 2005 dollars) stood at about $7,293 in 1962. By 2009, this support had grown to about $31,950. (See Chart 11.)

Data in the Index and complementary estimates of program populations raise concerns about the ability of local governments and civil society organizations to provide aid and other assistance. They also raise traditional republican concern about the long-term viability of political institutions when a significant portion of the population becomes dependent on government for most or all of its income.[60]

Dependent Population Rising Again



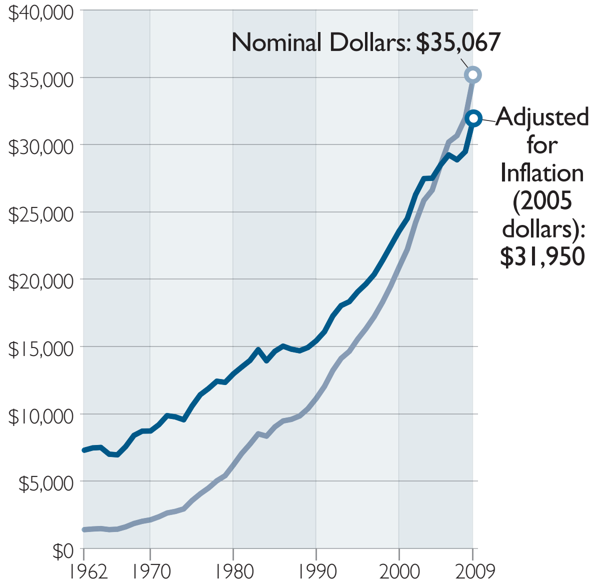
Source: Heritage Foundation calculations based on data from the Department of Education, Social Security Administration, Department of Health and Human Services, Office of Personnel Management, and the Census Bureau.

Chart 10 • CDA 10-08 heritage.org

60. For histories of this republican concern, see Bernard Bailyn, *The Ideological Origins of the American Revolution* (Cambridge, Mass.: Harvard University Press, 1967), and Gordon S. Wood, *The Creation of the American Republic, 1776–1787* (Chapel Hill, N.C.: University of North Carolina Press, 1969).

Government-Provided Income Rises

Per-Capita



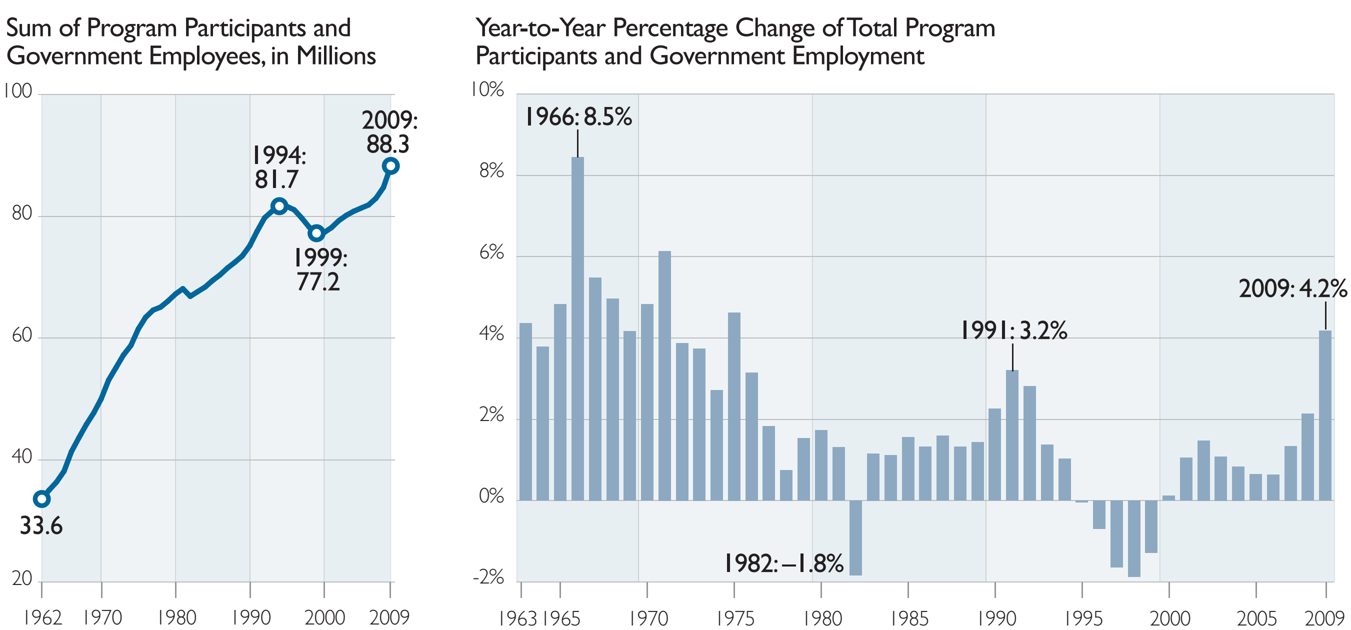
Source: Heritage Foundation calculations using data from the Office of Management and Budget, U.S. Department of Education, Social Security Administration, and Department of Health and Human Services.

Chart 11 • CDA 10-08 heritage.org

A level of slightly more than one-fifth of Americans (20.9 percent) on welfare may or may not be sufficiently high to trigger this concern. However, this percentage grows to 28.8 percent when federal and state employees are included. In 1962, the sum of these two categories (Index participants and government employees) stood at 33.6 million, or 18 percent of the total population. This total grew to 88.3 million (or 28.8 percent of the total population) by the end of 2009, an increase of 163 percent. (See Chart 12.)

The annual growth rate in federal and state government employment has generally subsided since the 1960s and 1970s. (See Chart 13.) However, the growth rate of state government employment has been positive for all but three years out of the past 48. Federal employment grew during the military buildup of the 1980s and during the military downsizing after the collapse of the Soviet Union, which led to negative change rates in federal employment throughout the 1990s. In 2009, with the economy mired in the longest recession since 1962, and the national unemployment rate jumping to 9.3 percent from 5.8 per-

Ever More Americans Dependent on Government

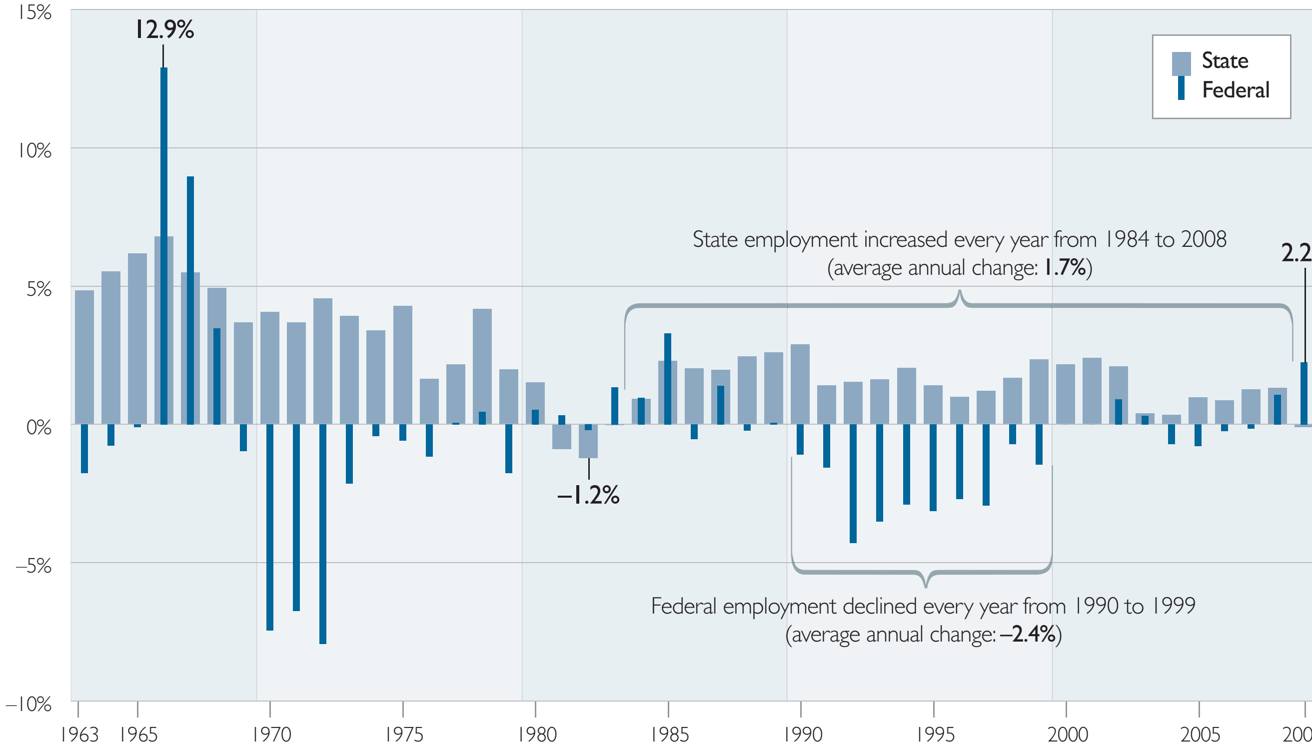


Source: Heritage Foundation calculations based on data from the Department of Education, Social Security Administration, Department of Health and Human Services, Office of Personnel Management, and Office of Management and Budget.

Chart 12 • CDA 10-08 heritage.org

Federal Employment on the Rise Again

Year-to-Year Percentage Change in Federal and State Employment



Source: Current Establishment Survey (CES) (Payroll Employment), "Employees on Nonfarm Payrolls by Industry Subsectors and Selected Detail (Table B-1)," by Haver Analytics, and "Department of Defense Active Duty Military Data," by Haver Analytics. Before 2002, federal data comes from *Historical Tables: Budget of the United States Government, Fiscal Year 2009*, Table 17.5.

Chart 13 • CDA 10-08 heritage.org

cent,[61] government employment went the opposite way, with federal the number of federal workers growing by 2.2 percent.

CONCLUSION

Public policy appears to matter in the growth of the Index of Dependence on Government. The rapid increase in the 1960s and 1970s corresponds to a new commitment by the federal government to solve local social and economic problems, which had previously been the responsibility of local governments, civil society organizations, and communities and families. The sum of government employees and the population covered by programs contained in this Index grew dramatically, even after accounting for the military buildup for the Vietnam War during the mid-1960s.

The 1980s and 1990s generally witnessed much slower growth in the Index. Indeed, if the period 1989–1993 had reflected the policies of the periods 1981–1988 and 1994–2001, the Index would have decreased in value. However, rather than fall, the Index appears to have resumed the growth rates attained during the Carter and George H. W. Bush Administrations.

Americans should be concerned about this seemingly relentless upward march in Index scores. Dependence on the federal government for life's many challenges strips civil society of its historical and necessary role in providing aid and renewal through the intimate relationships of family, community, and local institutions and governments. While the Index does not measure the decay of civil

61. Bureau of Labor Statistics, Current Population Survey, Household Data, Annual Averages, "Employment Status of the Civilian Noninstitutional Population, 1940 to Date [2009]," at *http://www.bls.gov/cps/cpsaat1.pdf* (October 4, 2010).

society, it reflects its declining role in this most important aspect of life.

Americans' concern over the growth of the Index of Dependence should be particularly high for another reason: Americans find themselves on the eve of the largest retirement of people in world history—at the same time that the number of "taxpayers" who pay no taxes is growing steadily. This country's republican form of government, with its finely balanced mixture of civil and political institutions and charitable roles probably could withstand some additional, but only very limited, increases in the dependent population as defined in this paper.

Can it stand, however, against the swelling ranks of Americans who believe themselves entitled to government benefits for which they pay few or no taxes? Are Americans completely indifferent to history's many examples of experiments in republican government collapsing under the weight of just such a population? Are Americans near a tipping point in the nature of their government and the principles that tie it to civil life?

A fair reading of these trends and the data contained in this Index leads almost inescapably to the view that, yes, Americans have reached that point.

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