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A BLUEPRINT FOR CUTTING COSTS AND BOOSTING GROWTH

Progressive Policy Institute

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Introduction

When the Progressive Policy Institute (PPI) published our plan for Funding America's Future as part of the 2019 Solutions Initiative, we urged policymakers to do two things: restore America's commitment to public investment and put the national debt on a downward trajectory so those investments could be sustained. We warned that failure to do so would result in borrowing costs crowding out public investment and reduced economic opportunity for young Americans.

In his first term as president, Joe Biden has led our country in revitalizing major public investments. The Infrastructure Investment and Jobs Act (IIJA) dedicated more than half a trillion dollars in new spending to rebuild crumbling roads and bridges, modernize our power grid, improve water safety, and so much more. The CHIPS and Science Act promised to dramatically increase spending on research and development (R&D) activities that lay the foundation for technological progress. And the Inflation Reduction Act (IRA) was the world's biggest investment in staving off a climate crisis by supercharging a green-energy revolution.

Unfortunately, similar progress was not made on debt management. Last year, the federal government spent $2 trillion more than it raised in revenue. Such massive borrowing might have made sense if it was necessary to support the economy through a recession or other unforeseen emergency, but it cannot possibly be justified given the record-low unemployment brought about by the Biden economy. This overspending exacerbated inflation in the aftermath of the COVID-19 pandemic and helped push interest rates higher than at any point since 2000.

As a result, the federal government now spends more than 3.1 percent of gross domestic product (GDP) annually just servicing the national debt—a level that's already higher than at any other point in American history and is projected to more than double over the next 30 years if current policy continues. The Fiscal Responsibility Act of 2023 made deep cuts to discretionary spending that left many CHIPS and Science Act programs unfunded, demonstrating that public investments are often the first thing to be crowded out by debt. The consequences of two decades of fiscal irresponsibility, once thought to be a problem for future generations, are a problem for Americans today.

PPI's new Blueprint for Cutting Costs and Boosting Growth proposes a better path forward that builds upon President Biden's pro-growth public investments by pairing them with the fiscal restraint necessary to prevent ballooning debt payments from crowding them out. We propose modernizing healthcare and retirement programs for our aging society by controlling costs and rewarding work with more-progressive benefit formulas. Our approach makes the federal tax code simpler and more progressive while raising the revenue necessary to adequately fund our government. Together, our policy proposals promote long-term growth and economic opportunity while reducing income inequality.

If fully enacted during the first year of the next president's administration, PPI's blueprint would put the budget on a path to balance within 20 years. But we do not see actually balancing the budget as a necessary end. Rather, PPI seeks to put the budget on a healthy trajectory so future policymakers have the fiscal freedom to address emergencies and other unforeseen needs. We know many on the right will oppose our proposed tax increases and many on the left will oppose our entitlement reforms. However, setting the ambitious goals we have ensures that enacting even half our proposed savings could stabilize the debt and secure a more prosperous future.

Spending

As our population ages, the explosive growth of healthcare and retirement spending, and interest on the debt used to finance them, is leaving lawmakers with fewer resources to invest in the next generation. Nearly three quarters of federal spending this year will be allocated based on legislation passed by previous Congresses—nearly double the share it was 50 years ago. PPI's blueprint would restore fiscal democracy by giving elected officials greater flexibility to adjust future spending priorities and revitalize public investments that support long-term growth.

Strengthen Social Security's Intergenerational Compact with Pro-Work Reforms

Despite most Americans' perception of Social Security as an earned benefit that they pay for throughout their lives, the program has been spending more on benefits than it raises in taxes for years—and the gap is only growing. As a result, benefits will be automatically cut by more than 20 percent when the trust funds are exhausted roughly a decade from now. It is vital for policymakers to protect vulnerable seniors from deep cuts without asking young Americans to foot the bill for affluent beneficiaries who did not pay enough to finance the program during their working lives.

To that end, PPI proposes transitioning to a new formula that awards benefits based on how many years an individual worked rather than their lifetime earnings. This innovative structure cements Social Security's status as an "earned benefit" but is far more progressive and affordable than the current formula. A low-income worker and their higher-earning boss would get the same benefit if they put in the same amount of work and anyone who works for at least 20 years would receive a benefit that keeps them out of poverty. Parents would also receive up to five years of credit for caregiving to better reflect their contributions to future Social Security solvency.

Our plan also increases the eligibility ages with longevity while preserving a special early retirement age for lower-earning workers because these gains have not been evenly shared. We would change cost-of-living adjustments to track inflation more accurately but boost benefits for the oldest beneficiaries most at risk of outliving their savings. And we would reform spousal and survivors benefits to better protect widow(er)s from falling into poverty.

Altogether, PPI's proposed reforms are the equivalent of fixing roughly half of the program's shortfall over the next 30 years through benefit changes and half through greater contributions from workers. Beneficiaries in the top fifth of the lifetime earnings distribution would absorb cuts relative to the current formula that are on average comparable to the ones already slated to occur under current law, but those at the bottom would be fully shielded from any cuts and many would even receive greater benefits than they could receive under the current formula.

Modernize America's Healthcare System to Expand Coverage and Reduce Costs

Medicare faces the same demographic and financing challenges as Social Security, but with the added pressure of healthcare costs growing faster than inflation. We propose to modernize Medicare by consolidating the three parts of traditional fee-for-service Medicare—Hospital Insurance (Part A), Supplemental Medical Insurance (Part B), and Prescription Drug Coverage (Part D)—into a simplified "Medicare One" benefit with one premium, one annual deductible, one set of co-insurance rates, a cap on out-of-pocket expenses, and one set of site-neutral provider reimbursement rates. Our approach leaves open the option for Medicare to also cover hearing, vision, and dental benefits but only if that benefit expansion is fully financed with income-based premiums. We would leverage competition to reduce inefficiencies and cut costs by basing the taxpayer subsidy for Medicare premiums on a weighted average of Medicare One and Medicare Advantage coverage costs. Together, these reforms would reduce government healthcare spending with no net cost increase for the average beneficiary.

PPI proposes to tackle high prices for healthcare services more broadly by setting maximum rates (based on a multiple of Medicare One reimbursement rates) for what providers can charge payers for out-of-network care. Providers would be prohibited from passing the costs of this care onto consumers through balance billing without adequate disclosure in advance. We also support breaking up anti-competitive monopolies in healthcare, which together with our other policies would pressure providers to compete more on quality and enter into contracts with insurers that reward value-based care.

We propose a partial extension of the IRA's temporary premium tax credit expansion that permanently fixes the "cash cliff" with a subsidy rate halfway between the IRA and original Affordable Care Act. We would also let individuals ages 55–64 without an employer-sponsored insurance plan use these premium subsidies to buy into Medicare at cost. Our reforms to Medicaid eliminate financing gimmicks, streamline the waiver process to support state innovation, and improve healthcare for needy populations. Finally, we propose investments in public health to tackle the opioid crisis, maternal mortality, and future pandemics like COVID-19.

Revitalize Discretionary Spending to Promote Public Investment

By controlling the growth of debt and mandatory spending programs, our plan provides fiscal space for policymakers to revitalize public investments in our future. We would raise federal spending on domestic R&D back to its historical average of 0.5 percent of GDP, which would be enough to fully fund the programs authorized by the CHIPS and Science Act and lay the groundwork for American leadership in new technologies such as artificial intelligence. Our budget then grows spending on public investments in education, infrastructure, and scientific research with GDP to ensure a consistent share of economic resources are devoted to pro-growth spending. Meanwhile, other nondefense discretionary spending is indexed to grow with our population plus inflation to maintain current service capacity.

But PPI believes that our government must not only spend more, it must spend smarter. We propose to repeal Buy America provisions (except those essential for national security) and other restrictions such as the Jones Act that prevent taxpayers from getting the most bang for their buck. Our budget includes a competitive grant program to relax zoning restrictions and seeds capital for a housing construction bank, both of which would spur new housing supply to reduce most families' greatest cost. We also propose several changes to rationalize the social safety net, such as tightening eligibility for housing choice vouchers by turning it into an entitlement.

We recommend a similar approach to defense spending. PPI supports establishing a BRAC-like commission composed of retired military and civilian leaders to identify common-sense savings from wasteful procurement practices and unnecessary personnel expenses. However, because the defense budget is already set to shrink as a percent of GDP under the baseline while authoritarian regimes such as Russia and China make our world increasingly dangerous, PPI proposes using these savings to help our allies defend democracy instead of pocketing them for deficit reduction.

Invest in the Workforce of Today and Tomorrow

PPI's budget offers a better-targeted, fiscally responsible way to advance many of the goals from the Biden administration's unsuccessful Build Back Better agenda. Our plan provides paid-leave benefits for new parents that replace 80 percent of the first $15 in hourly wages for 12 weeks and encourages employers to supplement it. We would put affordable child care within reach by making the Child Tax Credit fully refundable, expanding it to $5,000 per year for children under age three, and supporting states that expand public education to include all-day preschool for children ages three and four. These policies help new parents stay attached to the workforce and recognize the enormous social benefit parents provide by raising the next generation. We also propose to create "Child Opportunity Accounts" with annual government contributions based on family income to teach financial literacy through experience and help children from disadvantaged backgrounds access the same opportunities as their wealthier peers.

As children prepare to enter the workforce, they face an entrenched bias in federal policy that favors going to college over pursuing other skills—one which was made worse by the Biden administration's poorly targeted student-debt cancellation schemes. We would reform income-driven repayment programs to better target relief for students whose debt burdens outweigh the financial benefits of their degree and repeal regressive education-related tax breaks. PPI would use the savings to expand Pell grants and allow them to be used for more training programs, increase funding for career-technical education in high schools, and sponsor four million new apprenticeships annually. Paired with proposals to promote greater accountability of schools, these policies reduce the cost of college for those who attend while providing more accessible pathways to well-paying jobs for the majority of young Americans who do not.

We also believe now is the time for comprehensive, pro-growth immigration reform. While policymakers must strengthen border security, the United States currently has more job openings than jobless people to fill them—a problem that will worsen as our population ages. Opening our country up to more young immigrants with the skills needed to fill these jobs can help curtail inflation, reduce deficits, and strengthen the finances of Social Security and Medicare without undermining American workers.

Revenues

Congress had a unique opportunity in 2017 to make the tax code simpler and promote growth. Unfortunately, Republicans in power then chose to instead prioritize shortsighted tax cuts for the rich. When these provisions expire at the end of December 2025, PPI proposes to instead enact fiscally responsible, pro-growth tax reform. Our plan aims to raise at least 22 percent of GDP in revenue over the long run—enough to fund the government without slowing our economy or overburdening workers.

Reform the Corporate Tax Code to Promote Growth and International Competitiveness

TCJA made several positive changes to the corporate tax code, such as broadening its base and making the rate more internationally competitive. But lawmakers overshot when they slashed the rate from 35 percent to 21 percent. Our plan recoups the lost revenue by raising the federal corporate income tax rate to 25 percent, which is roughly on par with the OECD average. We also propose to equalize the tax treatment of stock buybacks with qualified dividends, tax nonprofit entities that functionally operate like corporations, and cut inefficient tax loopholes left in place by TCJA.

Importantly, we call for reversing the one "base-broadening" provision that TCJA got profoundly wrong: prohibiting investments in R&D from being fully deducted the year in which they occur. This change artificially reduced TCJA's scored cost while disincentivizing investments in technological innovation that power our economy. PPI proposes to not only restore the immediate deductibility of R&D but expand upon it by offering similar tax treatment for expensing all investments. We propose to pay for this change over the 30-year window by gradually eliminating the deductibility of interest on business loans, which encourages businesses to rack up debt regardless of whether it is used to expand productive capacity.

PPI also advocates reversing the counterproductive trade wars started by Donald Trump. The current U.S. tariff regime is needlessly complicated and raises costs for industries ranging from farming to manufacturing. Even worse, it discriminates against women and disproportionately raises the cost of products purchased by low-income people. Policymakers should dramatically simplify and scale back both the Trump-era tariffs and the ones that predated them. However, PPI does not advocate for unilateral disarmament in international tax policy: we support retaining some targeted tariffs on China and reforms that prevent other countries from collecting taxes that U.S. companies should be paying to our government instead.

Make the Individual Income Tax Code Simpler and More Progressive

While TCJA's business tax reforms were imperfect, its changes to individual income taxes were an unaffordable giveaway to the rich. PPI would not only reverse TCJA's individual rate cuts but make the tax code even more progressive than before, such as by taxing individual income over $1 million at a 45 percent rate and income over $10 million at a 50 percent rate. Furthermore, we would raise capital gains tax rates in these two tax brackets to the revenue-maximizing level.

TCJA's most egregious change was cutting the estate tax so an heir can inherit up to $26 million from their parents tax-free. It is antithetical to our nation's meritocratic ideals for the income someone earns through their own hard work or entrepreneurial risk-taking to be taxed more than a windfall they receive simply for being born to wealthy parents. PPI thus proposes to replace the estate tax with a progressive inheritance tax that taxes inherited income over $1 million at the beneficiary's top marginal income tax rate plus a surtax of up to 15 percent. However, we permit inheritance taxes on illiquid assets to be paid over several decades so nobody has to sell their family farm or small business just to pay the tax bill. We would also require heirs to pay all unpaid capital gains taxes when an asset is sold rather than "stepping up" the basis.

Despite its flaws, TCJA's individual income tax changes also included several worthy tax simplification measures that PPI would build upon. Our plan makes permanent TCJA's changes to personal exemptions and standard deductions that dramatically reduced the number of households who itemize their taxes. PPI would go even further than TCJA by repealing the state-and-local tax deduction altogether as well as the tax exemption for interest on municipal bonds. Most of the benefits from these tax breaks are captured by higher earners rather than by the state and local governments they are supposed to support, so we propose the federal government instead use half the savings from their repeal to assist state and local governments directly. Our plan would also phase out the mortgage interest deduction, giveaways to pass-through business owners, and several other increasingly regressive tax expenditures. Instead of restoring the alternative minimum tax, we favor capping the value of any remaining itemized deductions at 30 percent for each dollar deducted. Finally, we would reverse recent cuts to IRS enforcement that make it easier for wealthy tax cheats to escape paying the taxes they legally owe.

Replace Regressive Taxes on Work with Economically Efficient Taxes on Consumption

Our ambitious tax plan also goes well beyond addressing provisions related to TCJA. The payroll tax has become a highly regressive tax on workers' wages after several rate increases meant to finance previous benefit expansions. It imposes a flat rate of over 15 percent on most wages but less than 4 percent on earnings above a certain threshold. By taxing wages but not capital, the payroll tax hampers job creation and reduces earnings. Yet it doesn't raise nearly enough money to pay promised benefits for Social Security and Medicare, forcing the government to rely on general revenues and public borrowing to make up the difference.

PPI proposes to replace this regressive, anti-growth tax on labor with more progressive and efficient taxes on consumption. Specifically, we call for a 15 percent value-added tax and a border-adjusted carbon tax to reduce both our deficit and greenhouse gas emissions. To prevent these changes from harming lower-income families who spend a disproportionate share of their income on energy and necessities, PPI proposes transforming the Earned Income Tax Credit into a more generous Living Wage Tax Credit and making permanent a modified version of TCJA's Child Tax Credit that is fully refundable, indexed for inflation, and can be claimed monthly. We also call for replacing outdated gas taxes with a new vehicle-miles traveled tax piloted by IIJA that raises enough revenue from users to fully fund surface transportation infrastructure.

Conclusion

When the budget was last balanced, nobody could have predicted the need for new spending in response to the War on Terror, the 2008 financial crisis, or the COVID-19 pandemic. Because we can't know what challenges future policymakers will face, PPI's budget controls costs so they have the fiscal space needed to address those challenges without harming growth (for illustrative purposes, we assume any future surpluses are evenly split between new tax cuts and discretionary spending). In doing so, our plan restores fiscal democracy and revitalizes pro-growth public investments that lay the foundation for a more abundant and equitable America.

PPI's full Blueprint for Cutting Costs and Boosting Growth can be found at https://www.progressivepolicy.org/publication/budgetblueprint/

Percentage of GDP	2024	2034	2054
Revenues	17.5	21.6	23.0
Spending	23.2	23.7	23.0
Deficit (-) or Surplus	-5.7	-2.1	0.0
Debt Held by the Public	99.1	90.0	48.3