

## **Senate Democratic Policy Committee Hearing**

### **“Do Deficits Matter?”**

### **The Impact of Long-Term Deficits on Economic Growth and Job Creation”**

**Tuesday, January 20, 2004**

**10:00 a.m. - Noon**

**Dirksen 138**

### **HEARING TRANSCRIPT**

**DORGAN:** We're going to begin the hearing. A number of our colleagues are yet to arrive. But we want to, in the interest of time, begin. Let me apologize for my being delayed just a few minutes. I was at a meeting in the Capitol building. This is a hearing, a Democratic Policy Committee hearing on the issue of deficits and jobs. The issue of deficits and jobs, no doubt, will be something that'll be widely discussed in the coming days and weeks following the president's State of the Union address this evening.

I am fresh from an airplane last evening reading the new book that was written about Secretary O'Neill's stewardship here in Washington, D.C. It was one of the more interesting books I have read in some long while. And Mr. O'Neill recounts that most of the fiscal policy that we are now either blessed or cursed with is a result of Mr. Rove and others deep in the bowels of the White House sharpening their pencils to try to determine what works politically as opposed to what good policy might be. And he describes discussions in the administration about deficits and the prospect of ballooning federal deficits and it affecting the economy and it affecting jobs and has the vice president retorting that deficits really don't matter.

Deficits do matter. Deficits have a profound impact on this economy, on its ability to spend and on its ability to create jobs. And we will hear from the president tonight about the state of the union. We will hear today from some witnesses with varying views on the State of the Union with respect to deficits and jobs.

My own view is that we have a fiscal policy that is completely out of balance. We cannot as a government decide to increase defense spending, increase homeland security spending, observe substantial increases in health care spending, cut taxes again and again and possibly again and believe that there's any school in the country that teaches mathematics suggesting that all adds up. It does not add up.

This fiscal policy is dangerously out of balance and it needs leadership from the president and from the Congress. And one of the leaders on this issue is my colleague from my home state of North Dakota, Senator Conrad, who is the ranking Democrat on the Senate Budget Committee. No one, in my judgment, in this country knows more about the budget, has a better handle on fiscal policy and has better sense about these things than

my colleague, Senator Conrad.

I'm pleased that he's joined us today. And I know that, as is always the case and as is his habit, he will have brought some charts. So for Senator Conrad's presentation, including charts, let me call on him.

Senator Conrad, thanks for being with us.

CONRAD: Well, thank you, Senator **Dorgan**. Thank you for convening this hearing on the first day of our return. I think it's most appropriate, given the importance of the subject. I have been reading excerpts of the book that you referenced about Secretary O'Neill.

And it reminded me vividly of some of the events of 2001 when Chairman Greenspan came to my office and told me what he intended to testify to the next day. And I urged him to think again. And I urged him not to unleash what I described at the time as the deficit dogs.

Because I told him that if he testified as he intended to, that he would unleash all of those who want to continue tax cuts beyond what was prudent and to unleash those who wanted to spend in an unrestrained way. And unfortunately, all of that has come to pass. And we now see deficits that are truly out of control.

I think it's very important for people to understand it's not just deficits in the short-term that is the great concern. Obviously we're a powerful nation. We're a wealthy nation. We can afford to run deficits in the short-term. We could even afford to run modest deficits for a longer period of time.

What we can't have is deficits that are growing dramatically in comparison to the growth of the economy. That's what puts all of this at risk. And most of the econometric models that I have seen show very clearly if we continue on this course, the course the president has recommended, that it will put upward pressure on interest rates, that it will slow economic growth and, in fact, retard all that we hope for in terms of job development.

And, Mr. Chairman, I do have a few charts. And I think it may be as useful just to go back to the history and see what President Bush inherited and what his policy has provided. We see that when he came to office, we had the biggest budget surplus in the history of the country. And he has now turned that into the biggest budget deficit in the history of the country and by a wide margin.

Let's go to the next chart that shows the historic trend of deficits since 1969.

CONRAD: And you can see the deficit that we are now anticipating for 2004, according to various administration spokesmen, will approach \$500 billion, maybe something less than that. But his spokesmen are saying now that it will approach \$500 billion. We see the previous record in 1992 before last year's new record, the previous record went all the

way back to 1992 and the previous Bush administration.

Let's go to the next chart, because some have been telling us, "Don't worry, these deficits are small in relationship to the size of our economy." I've tried to do a reality test on that. And this chart shows if you exclude Social Security -- in other words, if you don't jackpot all the funds of the federal government, if you treat Social Security separately as it should be treated, in my judgment, what you see is that even as a share of our national income, even as a share of the size of our economy, these deficits are at near-record levels. The only one higher as a percentage of gross domestic product was back in 1983.

In 1983, there was virtually no Social Security surplus. This year, the Social Security surplus will be about \$160 billion. And under the president's plan, every dime of Social Security surplus will be taken, not to pay down debt, not to prepay the liability. Every dime will be taken to pay for tax cuts and other expenses of government.

Let's go to the next one. Perhaps the most alarming thing is where all this is headed in the long-term, and not according to my projections, but according to the president's own projections. These are the numbers that come right out of his budget document of last year. This is his projection of what happens if we adopt his policies, his spending plan, his tax plan.

And what it shows is that we're in the budget sweet spot now, even though we're having record budget deficits. We see in the next few years there'll be modest improvement. But then as the baby boomers begin to retire and the tax cuts, which the president recommends be made permanent explode, what we have is an exploding deficit as well, and deficits that are much larger than anything we have ever seen before in this country.

Now that is an untenable circumstance for the country. We simply can't have budget deficits of the magnitude the president is projecting.

Let's go to the next one. One of the things that's most alarming about what the president proposes is that it's coming at the worst possible time, right before the baby boomers begin to retire. The baby boom generation, the leading edge, begins retiring in 2008. And you can see the green part of these bars is the Social Security Trust Fund. The blue part is the Medicare Trust Fund. The red is the cost of the tax cuts.

And just at the time the trust funds go cash negative in the next decade, at that very time, the cost of the tax cuts explode. And as a result, we are driven right off the fiscal cliff.

Let's go to the next chart. You know, some in analyzing the deficit say it's simply a spending problem. Well, it is in part a spending problem, because deficits arise from the imbalance between spending and revenue. But we also have a revenue problem.

This chart shows that revenue as a percent of gross domestic product will be the lowest since 1950 in 2004. So we not only have a spending problem, we've got a revenue problem.

Let's go to the next one. The results of these fiscal imbalances are always hard to see in the near-term, because the affect of deficits and the buildup of debt -- that reveals itself over time. But there are warning signals. And the first warning signal is the drop in the value of the dollar.

The dollar has dropped nearly 30 percent over the last 18 months in relationship to the euro. That's a warning signal. That's the world markets telling us that they have less confidence in the dollar, less confidence in the U.S. economy.

Let's go to the next chart, which is what Federal Chairman Greenspan has warned us. He said the relatively optimistic short-term outlook for the U.S. economy is playing out against a backdrop of growing, longer-term concern in financial markets about our federal budget. And I think unfortunately we will see that play out through this year and into next year and the following year, because the concern about our financial markets and their stability can only grow when we have fiscal imbalances of these magnitudes.

Finally, not only is Chairman Greenspan warning us, not only are others warning us, but now the international monetary fund is warning us. And they're warning us that the buildup of deficits and debt, not only threaten our own economic security, but threaten global economic security. And their concern is that these massive deficits, both the budget deficit and the trade deficit, are going to put upward pressure on interest rates and choke off economic growth and economic opportunity and job creation, not only here, but around the rest of the world as well.

That is a serious warning, one that we ought to listen to. And as a party, I think it once again will fall to the Democratic party to be the party of fiscal responsibility to bring back some sanity to our long-term fiscal condition.

Thank you.

**DORGAN:** Senator Conrad, thank you very much.

Let me call on Congressman Scott. Congressman, just in terms of order of appearance.

But, Congressman Scott, why don't you proceed? And then I'll call on Congressman Spratt.

**SCOTT:** OK. Thank you very much. And it's certainly a pleasure to be here. And I thank you, Senator, for your leadership and Senator Conrad and particularly want to give credit to Representative Spratt for his hard work over the years in leading us in the budget.

Mr. Chairman, we're dealing with a situation where fiscal responsibility is, in fact, important. In 1993, the members of this committee participated in a historic vote in 1993 which turned the corner on fiscal responsibility and created on that chart the green, which started with a record deficit and ended up with a record surplus. During that period of

time, 20 million jobs were created.

As soon as this administration came in, they passed tax cuts, and the president signed tax cuts, same tax cuts that had been vetoed by President Clinton because they were fiscally irresponsible. And we see why it was good that he vetoed those tax cuts. And you see the exploding deficit on the red.

We now pay -- and at the same time, we've not gained 20 million jobs, we've lost jobs. We are now spending -- the federal spending -- a higher percentage is paid for with borrowed money than any year since World War II. You can talk about comparisons to the gross domestic product and all that. The fiscal responsibility measure, I think, is how much of your budget is paid for with borrowed money. And we're at a level higher than anywhere since World War II.

We're also getting close to the baby boomers' retirement. Social Security and Medicare, as has been pointed out, will be quite a challenge. And we have to wonder. And we have our expert witnesses here who will tell us the impact this fiscal irresponsibility will have on our ability to meet our basic responsibilities, our ability to pay Social Security and Medicare in the future and our national security interests.

If we need money quickly, if we're this far in the hole, we'll not be able to respond. And furthermore, with this kind of deficit, a substantial portion of that deficit is money borrowed from overseas. What kind of leverage will this countries who are borrowing our notes have over us if we get into a crisis and have to deal with those countries?

And so, Mr. Chairman, I thank you for bringing the expert witnesses and for your leadership on this important issue.

**DORGAN:** Congressman Scott, thank you very much. We're waiting for Mr. Greenstein. We will have four witnesses today, but I know the witnesses who are all veterans of hearings here in the Senate understand that we are very interested in hearing from you. But first, you must hear from us in opening statements. Let me continue asking Congressman Spratt to make his opening statement.

**SPRATT:** Thank you, Mr. Chairman. Mr. Chairman, three years ago, President Bush came to the White House with an advantage that no president in recent times has enjoyed, a budget in surplus, in surplus that year by \$126 billion. His office of management and budget looked out over the next 10 years and saw nothing but surpluses, surpluses in all of \$5.6 trillion between 2002 and 2011.

We warned that these forecasts were nothing more than that, forecasts, economists' constructs, estimates of what would happen to the economy and blue-sky estimates at that. But the Bush administration didn't heed our warnings. It pushed ahead with tax cuts of \$1.7 trillion over 10 years which it trimmed to \$1.35 trillion to get the bill passed in the Senate with an artifice that it would come back to rely upon false, phony expiration dates.

Three years later, we know that the surpluses foreseen in 2001 were a mirage. If we adjust the \$5.6 trillion for political reality, if we assume, for example, that popular tax concessions like the research and experimentation tax credit will be renewed when they expire then the baseline surplus wasn't \$5.6 trillion to start with. It was closer to \$5 trillion, according to the Concord Coalition and the Center on Budget Policy Priorities.

If we then applied to this adjusted surplus the adjustments that the Congressional Budget Office made in its estimate of the budget last August, another \$3.345 trillion is washed out of that baseline surplus, \$700 billion comes out due to a slower growing economy. \$2.6 trillion comes out due to technical misestimates. At current growth levels, the economy is simply not generating the tax revenues that CBO's technical rules and OMB's technical rules predicted based on past experience.

These adjustments leave a surplus of about \$1.6 trillion, \$1.7 trillion between 2002 and 2011. Now this radical reduction in the bottom line is not due to tax cuts or terrorism or war. This is the baseline estimate. Those events are costly, but they have to be factored in later.

Only a small portion, as I indicated, is due to the economy, around \$700 billion. What's happened is that the foundation on which the Bush administration rested its fiscal policies has shifted and shifted radically. The projections that may have warranted to some their fiscal policies in 2001 and 2002 no longer pertain. We don't have a surplus of \$5.6 trillion anymore. It's more like \$1.6 trillion baseline surplus. And that's before the tax cuts, before the defense increases and before all of the other adjustments that have to be made for reality of what's happened.

When you consider that \$1.6 trillion is less than the administration's 2001 tax cuts with associated interest added, you begin to see why the Bush administration still engages in this sort of fiscal denial. Still won't quite acknowledge that the foundation on which its fiscal policies has been based has shifted radically. Why won't they? Because the current projections simply will not accommodate their tax cuts.

And yet, they're proposing more. It won't accommodate their steep increase in defense, \$1 trillion at least over and above current services, \$1 trillion over and above the CBO projection of defense costs in 2001. And truly the \$1 trillion is a conservative estimate.

That doesn't include much in the way of estimation for Iran, for Iraq, Afghanistan and those expeditions. It doesn't include much for further tax cuts. It doesn't include much for homeland security. And it's still \$1 trillion in additional spending.

The Bush administration, when fiscal denial doesn't work, drops back and dismisses these deficits effectively saying that deficits don't matter or deficits like this are, quote, "manageable," their words, not mine. Well, there's one authority to whom they frequently refer and rely upon who has said otherwise. And that's Alan Greenspan. And some months ago, he said history suggests that an abandonment of fiscal discipline will push

up interest rates, crowd out capital spending, lower productivity, force harder choices in the future.

Deficits are consequential, Mr. Chairman. And I look forward to hearing from all of our witnesses and elaborating further on this problem. And I thank each one of them for taking the time and making the effort that they have to come to testify today. Thank you very much.

**DORGAN:** Congressman Spratt, thank you for your leadership, along with Senator Conrad's leadership as the ranking members on the two budget committees.

Congresswoman DeLauro?

DELAURO: (OFF-MIKE) and I appreciate the opportunity to be able to be here this morning and to have some opening remarks. To you and Senator Conrad and John Spratt and my colleague, Representative Scott, all leaders on issues relating to the budget and the deficits we see before us, your work is critical to our efforts to address the real concerns that nearly everyone in every state in the nation are experiencing.

Historically the federal budget has reflected our priorities as a people. It has reflected our values as a nation, our shared values. But in the last three years, our budget reflects a government out of control, undermining our long-term well-being and contradicting our values.

DELAURO: We have witnessed the sharpest budget turnaround in history. What was once a \$5.6 billion surplus projected through 2011 is now a \$2.3 trillion deficit, largely due to the series of massive tax cuts the administration passed over the past three years, tax cuts that had benefit almost exclusively large corporations and wealthy individuals. States have been left with providing services that the federal government is now underfunding, even as the states face their own deficits.

In my state in Connecticut, we face a three-year budget gap of \$3.6 billion. Almost 30,000 people have already been eliminated from the HUSKY Program, which is Connecticut's SCHIP program. Six social service offices have been closed, and adult job training programs have been cut.

The administration and the majority in the Congress are intent on so debasing the quality of public services that citizens give up and turn out of necessity to the private market. Their long-range plan is to destroy the capacity and the obligation of the federal government to provide key social support.

But we could face this challenge if the White House approached these budget issues honestly. Consider what they did with "No Child Left Behind". After passing the historic education bill, the president's budget shorted it by \$8 billion. Medicaid -- the administration has proposed to turn it into a block grant but with progressively less funding, leaving the states with the enormous responsibility of providing health care for

the nation's poorest citizens.

In 2002 alone, more than 1.2 million additional people who lost their jobs and their insurance turned to Medicaid for assistance as their only option open for health care for their families. The same is true of their proposal to reform Head Start, the most effective early-learning program ever developed. Their plan offers governors choice and so-called flexibility, but with starvation funding.

In the case of child care, Republicans propose a welfare reform bill that created an \$11 billion unfunded mandate for the states. The list goes on, cuts to HOPE Six (ph), public housing programs, cuts in immunization grants, which have been effective in preventing a variety of illnesses.

By passing unaffordable tax cuts for the wealthiest Americans, Republicans are not only merely sapping government resources, they destroy the idea that our society can act with a shared sense of purpose and responsibility to address the tasks that are before our country. As we look ahead to the coming year's budget prospects, Democrats will need to be bold in their thinking and resolute in their principles. We have a very difficult fight ahead of us.

I would like to again say thanks to the chairman for inviting me to speak this morning. I look forward to the comments of our guests and the opportunity for questions and answers.

Thank you, Mr. Chairman.

**DORGAN:** Congresswoman DeLauro, thank you very much.

We have invited four witnesses today to talk about this issue of the economy and jobs. And this is not just a theoretical debate. Obviously our economy at this point is facing some challenges. We have a fair number of people and families in this country who have lost their jobs and their sources of income. And the question is what kind of policies can we employ to put this economy back on track in a way that really does produce good-paying jobs.

Gene Sperling is at the Center for American Progress. He's a Senior Fellow there and a Senior Fellow for Economic Policy at the Council on Foreign Relations. Mr. Sperling was the national economic adviser to President Clinton and Director of the National Economic Council from 1997 to 2001. In President Clinton's first term, he served as Deputy National Advisor. There is much, much more to say about his background, but for brevity, let me leave it at that. He is, I think, a remarkable thinker and a contributor to an economic policy that strengthened this country.

And, Mr. Sperling, thank you very much for joining us today. Why don't you proceed?

SPERLING: Thank you. Thank you, Senators Conrad and **Dorgan** and Congressmen



Spratt, Scott and DeLauro, not only for being at this hearing, but for your leadership on this issue for many years.

Let me thank my co-panelists as well, particularly Chris Edwards, for coming into the lion's den. Chris, I've been in your situation more often than I've been in this situation in the last few years.

I have submitted testimony which I will try to summarize rather briefly, I hope.

The basic point that I want to make is that our country has always had a fundamental belief in generational responsibility, a fundamental belief in the notion that each generation takes the steps and sacrifices necessary to leave the next generation better off. In the fiscal context, the sense of generational responsibility has very specific meaning. We have known for many years that we face a demographic crisis.

We know that we have 39 million Social Security retirees today and that we will have as many, over 70 million in 2030. We know that we face a demographic challenge. And generational responsibility in the fiscal context has meant for many years to people in both parties the sense that we, this generation, ought to take steps to save more now to not only make us more productive, but to not leave the next generation with the painful options of either higher debt, higher taxes or less investment in their children.

What has been very distressing about the policies of this administration is that they have consistently employed, I believe, two policies, overall themes. One has been actually reversed generational responsibility, the reverse and actual policies that seem to explicitly make it easier to do easy, politically easy policies now at the expense of dramatically increasing the burdens and debt on the next generation. And two, at every turn, there has been an effort to design those policies to explicitly hide that reverse generational responsibility. Every policy is explicitly designed to hide the tradeoffs that we are imposing on the next generation.

Now as to the issue of the, kind of, hidden tradeoffs, we can look right at the 2001 tax cut and what I call their Cinderella tax accounting. The tax cut was billed as \$1.35 trillion. I think we could have had a reasonable discussion if we had truly had a tax cut that was \$1.35 trillion. But we all knew that that did not count interest savings, that it assumed that it would not be accelerated, that it assumed that it would not be permanent. And it assumed that people wouldn't actually get their tax cuts, because the alternative minimum tax would take it away.

When the IMF looked at us, our policies, they said, "Well, the real cost of this is closer to \$2.4 trillion." But these policies were designed with the impression that, like Cinderella, the tax cuts would disappear at midnight, never to reappear again. And yet, what we see from the comments that I put in my testimony and others is the administration explicitly knew, did not believe this, explicitly meant for them to be permanent, explicitly was already campaigning for them, even as they were selling these tax cuts as having lower costs.

I do not know what the difference between that is and the kind of corporate behavior we speak disapprovingly of when a company knows that their shareholders and their board will not approve of their level of debt and they go out of their way to design gimmicks and accounting devices to hide from their shareholders and board what the true nature of their debt is. This tactic again was used in 2002 and 2003.

When you look at the actual cost of the tax cuts in 2013, the cost in a single year in 2013 is by any estimate over \$400 billion. And with lost interest, anywhere from five to \$600 billion. This is one of the most stunning facts and it points to my -- it goes to my second way in which there's been a constant hiding of their tax agenda.

They have constantly referred to everything we're doing as designed to get us out of short-term fiscal problems. And yet, all of these policies have been designed to have an extremely long-term impact. So the country thinks we are debating how to improve the economy in 2003. And yet, with virtually no discussion, we are adding nearly five to \$600 billion of debt deficits every year just towards the tax cuts, not including spending, not including a diminishment of economic growth, four to \$600 billion per year just through their tax cut policies.

This would be the -- so what does this mean in terms of the generational tradeoffs, the reverse generational responsibility? In the prior administration, there was a commitment to saving surpluses to ensure that we had enough to deal first with what we needed for Social Security and Medicare solvency. There was for a short period of time even a bipartisan commitment towards this goal.

Indeed, the tax cuts alone would be anywhere from two and-a-half to 3 percent of GDP, the tax cuts alone. While the amount that we would need to solve Social Security over 75 years would be .73 percent and for Medicare, 1.1 percent.

Simply put, these tax cuts over 75 years will cost more than it would have taken for our nation to save to do both Social Security and Medicare solvency. That is a fundamental tradeoff that we made, tax cuts versus solvency for Medicare and Social Security that was never honestly debated in this country because the costs were hidden, and everything was designed as if it were short-term.

The other tradeoff we see, which other people will talk about and I will not go into as much is the affect on confidence, confidence in terms of savings, confidence in terms of increasing the risk of investing in our country, confidence in terms of avoiding a potential hard landing from such a large current account deficit. The one point I will simply make is in the current economy, we are seeing more and more that job creation is not just about a return to the business cycle, but about the confidence that makes companies and entrepreneurs and venture capital put money into long-term investment. A confident fiscal environment is critical to that kind of confidence for job creation.

The third tradeoff is just our preparation for dealing with the unknown, for the unknown

crisis. If there was anything this period should have taught us it is the importance of saving for a rainy day. Indeed, in 2003, the projections when President Clinton left office were that there would be a \$350 billion surplus. Instead, we're having a \$350 billion deficit.

But, you know, \$350 billion for a single year is completely manageable to help get us out of deficit and pay for war. But imagine if the past administration had taken this administration's view. Imagine if they had left us with a \$370 billion deficit. Then this swing would have driven us to a \$1 trillion deficit, or over 10 percent of GDP.

This period should have been our greatest lesson of the importance for saving to ensure that our nation can always respond to crisis with strength, with fiscal strength. Instead, we have completely missed that lesson.

I want to leave with the following, which is that even after all of this has happened, we should not just be looking backwards and analyzing what has happened in the past. As the president goes forward on the State of the Union, we will see more of the exact same pattern, reverse generational responsibility and hiding the tradeoffs.

The lifetime savings account and retirement savings accounts that we see today perfectly fit that pattern. Because they ask for after tax, because they encourage people to go out of tax deferred savings to savings where you pay after tax income now, it will lead us to take savings, tax revenues that are expected in the future and bring them this year at the cost to the future. So all the bad charts that Senator Conrad and Senator **Dorgan** show all assume that we're going to be getting money from 401(k) and IRA distributions in the future. We're simply now robbing that future revenues to make this lifetime savings account and retirement savings accounts look positive right now.

We used to have a joke when we were in the White House that we knew how to solve the deficit. We'll just tell everybody they can pay next year's taxes this year at a 50 percent discount. Well, of course, that's a joke because you're making things look better right now by robbing the future. This LSA and RSA proposal are stunningly close to implementing that joke for our policies.

We should also keep our eye on the same for Social Security, whether we are now looking for policies that turn Social Security on its head by literally solving Social Security, not by saving more for the future as was with generational responsibility, but borrowing from the future hundreds of billions of dollars so that we can implement a pain-free transition to individual accounts, as many in the administration and their allies are proposing.

I believe we need to move forward with broad, shared sacrifice. We will never make progress if we do not have everybody at the table. It is impossible, I would believe, for any of the Democratic members of Congress to possibly go home to their constituents and ask for sacrifice in Medicare or Social Security or anything else for fiscal discipline when they have just seen hundreds of billions of dollars go to the very top 1 percent.

So it is not just the cost of those tax cuts, it is the cost of what it means in getting shared sacrifice.

SPERLING: How can other people be asked to make tough decisions when we have just given away so much to so few who are so fortunate?

Secondly, we do need new savings incentives. It should be a universal 401(k) that gives increased incentives to those who have the hardest time saving, not the 5 percent who are maxing out.

And finally, we should not forget that when we let huge deficits come, the most likely thing is that there will be a battle between how you solve Social Security and how you prevent taxes from being increased. The one loser we know will be the poor, the disadvantaged, children who don't possess the political power to compete in that type of political debate in the future. Thank you very much.

**DORGAN:** Mr. Sperling, once again you have given us a lot to think about. And thank you for your service to President Clinton as his chief economic adviser for a number of years. Thank you for your testimony today.

Next we will hear from Chris Edwards. Chris is the Director of Fiscal Policy Studies at the Cato Institute. He has over a decade of experience in tax and budget policy. Before joining Cato, he was a senior economist on the joint economic committee covering tax, Social Security and entrepreneurship issues. He has worked at PricewaterhouseCoopers, served as an economist with the Tax Foundation, holds a masters degree in economics from George Mason University.

Mr. Edwards, thank you very much for accepting our invitation to be here. And you may proceed.

EDWARDS: Thank you very much, Mr. Chairman and members of the committee. Thank you for inviting me to testify today.

Budget projections, as has been already mentioned a number of times, show red ink as far as the eye can see with the continuation of current fiscal policies. The Bush administration certainly is downplaying the importance of the deficit and has no plans to balance the budget. The high deficits will not be a serious problem if the budget could be expected to balance naturally as the economy grew over the following few years.

But today is, of course, different from the 1980s and the 1990s because the baby boom generation begins retiring in 2008, putting enormous costs on the budget. I agree with many of the comments of Gene that deficits do impose large costs on the next generation. And this is very much a serious problem.

Consider that combined Medicare, Medicaid, Social Security spending is now rising by

about \$50 billion every year, a decade from now, spending in those three entitlement programs will be rising by about \$100 billion every year. Regardless of when the various trust funds run out, the budget squeeze from entitlements will begin later this decade. So the problem is much closer than is often represented.

Unfortunately, the White House has shown no leadership in proposing budget cuts to get the deficit under control. While I support the president's tax cuts, his tax and spending policies have been hugely inconsistent. He supports small government on taxes and big government on spending.

Bush has presided over three of the five largest increases in real discretionary outlays in the last 40 years. President Bush rarely even talks about the need to restrain spending. Yet when a \$200 billion deficit, President Clinton argued in his 1995 budget message that, quote, "Except in emergencies, we cannot spend an additional dime on any program unless we cut it from another part of the budget," unquote. And that was President Clinton.

By contrast, President Bush is ignoring today's fiscal realities. Just last week he announced plans to launch an expensive mission to go the moon and Mars over the next couple of decades, possibly costing hundreds of billions of dollars. And I agree with the chairman. In this case, this certainly is putting politics above policy.

Total federal outlays have risen 24 percent in the last three years. If you exclude interest costs, which have been falling in the last few years, outlays have actually risen 30 percent. I think the administration and Congress need to focus on identifying low priority domestic programs to cut and it should be reforming the huge defense budget.

Defense outlays have risen \$150 billion just in three years. That has sucked a huge amount of resources out of the private sector economy. Defense spending is big government just like every other type of spending. The Pentagon wastes billions of dollars.

For example, the GAO says, quote, "That the Pentagon has serious financial management problems. They are pervasive, complex, long-standing and deeply rooted in virtually all business operations of the department," unquote. I don't think we can afford to have such waste in DOD and other government departments with today's huge budget deficit.

The administration is arguing that none-entitlement, non-defense, non-homeland security spending has been restrained. But that's less than one fifth of the budget. We can't leave out the other four fifths of the budget for savings. Aside from Pentagon reforms, for example, Medicaid needs reform. Medicaid spending has been rising by about 10 percent annually the last few years.

Looking ahead, some argue that the Bush tax cuts should be repealed to balance the budget. But even with the Bush tax cuts (inaudible) permanence and with a fix to the AMT, federal revenues will rise from 16.2 percent of the GDP today to about 18 percent

by 2013. That's about the average for the last 30 years, so I don't think that there's a shortage of revenue going forward.

The trouble is on the spending side. Looking ahead to 2040, outlays will rise from today's 20.5 percent of GDP to about 28 percent of GDP, given CBO's entitlement projections. That means without spending reforms, the government will be claiming about 37 percent greater share of Americans' income by 2040 than today.

Regarding the coming entitlement crunch, the current comptroller general, David Walker, I think, got it exactly right. He recently testified, quote, "Government cannot accept all the givens of its existing programs, policies and operations. A fundamental review of what the government does, how it does it should be required because of the coming demographic tidal wave on our fiscal horizon," unquote.

I think that's exactly right. A good first step would be to consider some of the spending cuts that were suggested in a new Brookings Institute study last week. Brookings introduced a number of plans to balance the budget by 2013. One of them was called the smaller government plan. In my testimony, I've cited a Cato list of possible budget cuts to build on the Brookings smaller government plan that would be large enough to balance the budget by 2013 with the Bush tax cuts in place.

Let me close by quoting President Clinton from his 1995 State of the Union as we await President Bush's State of the Union tonight. President Clinton said, quote, "Let's change government, let's make it smaller, less costly and smarter," unquote. I wholeheartedly agree.

Thank you very much for holding the hearings on this important topic.

**DORGAN:** Mr. Edwards, thank you very much for being with us today.

We've been joined by Senator Sarbanes and Senator Lautenberg. And I think with their permission, I'll continue with the two remaining witnesses. But if there comes a time when you are going to have to leave, I would like to recognize you for a statement before you do that. So if you'll just signal me, we will do that.

Mr. Greenstein, Robert Greenstein is the founder and the Executive Director of the Center on Budget and Policy Priorities where he focuses on the federal budget and more specifically, the impact of tax and budget proposals on middle and lower income people. He's written many reports, analyses, op-ed pieces, worked with many of us in the Congress on these important issues.

In 1996, he was awarded a MacArthur Fellowship. The MacArthur Foundation cited Mr. Greenstein for making the center, quote, "The center a model for a non-partisan research and policy organization."

Mr. Greenstein, thank you again for accepting our invitation and coming today to talk

about deficits and jobs. You may proceed.

GREENSTEIN: Thank you very much, Senator. We've provided a few documents, but the one that I'm really going to be talking from that's in the packet...

**DORGAN:** Can you pull the microphone a bit closer?

GREENSTEIN: I didn't have it on, that's why. I'm going to be talking from a series of overheads that are in the packet.

In September, our center, the Committee for Economic Development and the Concord Coalition did a joint analysis of how serious the deficit problems are. We found that if we continued on the current policy course, if the tax cuts are extended and made permanent, including relief from the alternative minimum tax, we view the administration's multi-year defense buildup plans and a prescription drug benefit is enacted as it was, the deficits over the coming 10 years would total \$5 trillion and then get to much higher levels after the decade.

Since we issued that estimate, three other institutions have done a similar estimate. And all of their projections are actually even higher than ours by a small amount. Brookings, in its new study, estimates \$5.1 trillion in deficits over the coming decade. And two Wall Street firms estimate \$5.4 trillion or \$5.5 trillion over the coming decade.

One of the implications of this is seen on this board behind me. Three years ago when President Bush took office, the Congressional Budget Office estimated that the cost of interest payments on the debt over the next 10 years would be \$622 billion. Now interest payments on the debt over that same 10-year period are likely to total at least \$2.5 trillion.

That's nearly an additional \$2 trillion in interest payments, for which, as you know, we get no schools, no health care, no military hardware, no roads or bridges. We get nothing in return for the interest payments. Two trillion dollars more than we anticipated three years ago.

As you know, in the last couple of weeks, the international monetary fund has strongly scolded the United States' budgetary policies in terms usually reserved for third world countries and banana republics. The IMF questioned the wisdom of the tax cuts and warned that the budget deficits we face pose significant risks, not just for the U.S. economy, but for the world economy. And they specifically referred to what the implications would be if the tax cuts are made permanent, a call that we're likely to hear tonight.

We should make no mistake about how large an impact the revenue changes have had. Last year in fiscal 2003, federal revenues as a share of the economy, the standard way we measure trends in spending and revenue over time, federal revenues as a share of the economy were at their lowest level since 1959. Federal income tax revenues were at their

lowest level as a share of the economy since 1942.

Now in 1959, we had no Medicare program at all or Medicaid, little federal aid to education. We had a very different kind of government. Yet we're back to 1959 levels in revenues. To be sure, as we pull out of the economy, the revenues will come back some.

But estimates that include the expectation of continuing relief from the alternative minimum tax so we don't have 30 million filers subject to the AMT by the end of the decade -- I think it's fair to assume that Congress is going to continue AMT relief. Once you factor that in, we find that even after the economy has recovered, federal revenues will be lower as a share of GDP than in the '70s, the '80s or the '90s despite the fact that the retirement of the baby boomers is coming. And no matter what changes we make in Social Security and Medicare, we know that their costs will necessarily rise significantly due to the aging of the population.

Recently we have heard some claims, particularly from the right part of the political spectrum, implying that the problem in rising deficits is not reduced taxes in recent years, but increased spending. As this chart shows, that's really not accurate. Federal spending as a share of the economy has risen in the last few years, but it remains lower than in every year from 1975 through 1996.

Nor is it surprising that domestic spending has risen more quickly in the last few years than in the preceding years. It always rises faster in times of economic downturn than in times of economic boom. The growth in domestic spending in the last few years has been exactly the same percentage rate as it was in the early '90s.

Now if one uses the CBO figures, the Congressional Budget Office figures, on the cost of all legislation enacted since the start of 2001, tax cuts and spending increases, we find that increases in domestic discretionary spending outside homeland security account for only 5 percent of the cost of legislation enacted in the last three years. Entitlement increases, another 12 percent. These are the costs in 2003.

They're dwarfed by the defense homeland security and international increases. And all increases in defense, anti-terrorism and domestic spending combined are smaller than the cost of the tax cuts, which account for 55 percent of the total costs during this period.

David?

**DORGAN:** Mr. Greenstein, you said during this period. Is that chart measuring the year 2003?

**GREENSTEIN:** Yes. This shows you the cost in fiscal year 2003 of all legislation enacted since 2001.

**DORGAN:** Thank you.



GREENSTEIN: The tax cut figure of 55 percent, Senator, actually rises to a higher percentage level in 2004 and 2005 as more of the tax cuts take affect and as this entitlement figure for a year or two actually goes down because some of this was temporary increases and (ph) unemployment spending. Now eventually, the entitlement figure goes back up because of the Medicare drug benefit.

GREENSTEIN: The next chart is, if anything, even more illuminating. We often hear -- Gene noted how we often hear these low estimates of the cost of the tax cut. We're used to hearing big figures on the Social Security shortfall measured over 75 years. So here working with Peter Orszag at Brookings, we simply measured the cost over 75 years of both the tax cuts, if made permanent, and the Social Security shortfall. We find that the cost of the tax cuts, if made permanent, is triple the Social Security shortfall, larger than the Social Security and Medicare hospital insurance shortfall combined.

David?

Another way to get a sense of the magnitude -- what the magnitude of the tax cuts will be if they are made permanent is shown in the next chart which shows you that when they're in full affect, if made permanent -- this would be after a state tax repeal, among other things, is in affect -- that the annual cost of the tax cut would be nearly five times everything the federal government spends on education at elementary, secondary and post-secondary levels combined, nearly five times everything we spend for our veterans, 34 times what we spend on the environment. In fact, just the tax cut for the top 1 percent of the population would be one and-a-half times everything we spend on education.

So the moral of the story here is that we need to stop digging the hole deeper, as we said in the joint statement with the Committee for Economic Development and Concord. And that means, among other things, stop digging the hole deeper on the tax cut side.

We all know that sooner or later -- and sooner is better -- we need to make changes in Social Security and Medicare so that the rise in cost isn't as large as it will be in current law. But there is no way that that will remotely come close to being sufficient to doing what we need to do. The notion that we can continue on the current tax cut course without danger for the economy, I think, is mistaken.

The final point that I would like to make is just a response to something Chris Edwards said. In his testimony, he says Medicaid spending is out of control. It's risen 10 percent per year in the last few years.

Well, the fact of the matter is that Medicaid spending rises more quickly in economic downturns because people lose their jobs and they become eligible for health care. It's also the fact that Medicaid spending is not rising more quickly than health care spending in the private sector. We have a problem in health care costs generally, not in Medicaid in particular.

What's happened in Medicaid in the last two years is that states facing budget crises have

instituted severe cuts. Between 1.2 and 1.6 million low-income children, seniors, disabled people and working parents have been made ineligible for Medicaid by these cuts. There are low-income children with cancer who are put on waiting lists. There are pregnant women who need prenatal care and are low-income who have been thrown off of Medicaid programs.

I find it difficult to contemplate that as a nation in the last two years we have allowed about 1.5 million people in need to fail to get health insurance while providing tax cuts that in 2003 averaged \$113,000 each for people that make over \$1 million a year. There's a priorities problem there. Thank you.

**DORGAN:** Mr. Greenstein, again thank you for your contributions. As always, you raise a great many questions and provide thoughtful analysis.

Charles Kolb is our last presenter. Mr. Kolb is the president of the Committee for Economic Development founded in 1942. The CED is an independent, non-partisan research and policy organization of 250 businesses and education leaders dedicated to economic and social policy and the implementation of its recommendations by public and private sectors.

Prior to joining the CED, Mr. Kolb served as general counsel and Secretary of the United Way in America from 1992 to 1997. He has 10 years of government service at senior level positions. At the White House, he served as Deputy Assistant to the President from 1990 to '92 for domestic policy. And he has an undergraduate degree at Princeton, graduate of Oxford, masters degree in philosophy, politics, economics, a law degree at the University of Virginia Law School.

## **Senate Democratic Policy Committee Hearing**

**“Do Deficits Matter?”**

**The Impact of Long-Term Deficits on Economic Growth and Job Creation”**

**Tuesday, January 20, 2004**

**10:00 a.m. - Noon**

**Dirksen 138**Mr. Kolb, thank you for joining us, and thank you for accepting our invitation. You may proceed.

**KOLB:** Thank you, Mr. Chairman, members of the committee. Thank you very much for this opportunity to present the views of the Committee for Economic Development on the federal budget deficit, its potential impact on the nation's economic future and the possible impact on the private sector.

For more than 60 years, CED has been the voice of the American business community in supporting sound economic and fiscal policy. Several of our trustees became increasingly worried in late 1992 by the reemergence of what appeared to be a serious, sustained, long-term structural federal budget deficit. Through CED's history, our trustees have

consistently believed that the U.S. economy will be strongest if over the long run it enjoys a modest budget surplus.

A surplus will help ensure the necessary capital to fund investment that is essential to both economic productivity and growth. While budget deficits are not inherently a problem if they are employed to generate a short-term macro-economic stimulus, they will undermine economic growth and productivity if they become too large and last too long.

CED's trustees decided to establish a sub-committee on the budget demographics and economic growth. And in March 2002, we released the sub-committee's report which was entitled, "Exploding Deficits, Declining Growth: The Federal Budget and the Aging of America."

We are deeply concerned that these new deficits unlike those which emerged in the early 1980s pose an even greater economic threat to the country because of the nation's current demographic profile, namely, the aging of the U.S. population, which vastly compounds the problem.

The baby boom generation is now but one presidential election cycle away from retirement. We have a relatively low fertility rate which will mean an economy with many more retirees and proportionately far fewer workers. The growing demands of our aging population for health services will therefore expand dramatically and entail escalating costs. And the result will be less public and private national savings and fewer resources available for economic growth. As we warned last March, we face a situation eventually where for the first time in our history Americans may be less well off than their predecessors.

As stronger economic growth kicks in, the demand for capital by the private sector will increase, and interest rates will begin to rise. This affect will lead to a crowding out phenomenon by which government's needs to borrow funds to finance the deficit will compete with private sector needs for capital. The growth of our overall capital stock will be reduced, which, in turn, will lower productivity growth. And at some point in our future, American workers will experience lower real wages and incomes.

As we continue with our reckless gamble of lost fiscal discipline, there is also some danger that we will see a negative impact on both consumer and business confidence. To date, that has not yet occurred, in large part because the economic recovery is still young and strong.

However, should we continue a situation of annual budget deficits of \$500 billion coupled with a record current account trade deficit exceeding 5 percent of GDP and requiring the annual importation of some 500 to \$600 billion in foreign capital, we may find both domestic financial markets and international currency markets concluding that our government lacks the political will to restore fiscal discipline and that it might indeed resort to inflation as a way out of the problem.

Other consequences of this situation could include a rise in household and corporate borrowing rates, an increase in interest payments on the national debt, as has already been pointed out, a loss in investor confidence, a shift out of dollar-based assets and the fall in stock prices and national wealth. If this scenario emerges, then higher interest rates are a foregone conclusion most dangerously as part of a possible crisis scenario.

There is also an additional negative consequence to the large federal budget deficits. They have the affect of crowding out other public expenditures, which could have positive benefits for the private sector. Federal government investments in areas such as basic research, transportation, education, maybe even manned space exploration to the moon or Mars are areas where government investment can also be a net plus for the American private sector.

The Congressional Budget Office acknowledged last year that substantial federal budget deficits could produce an economic crisis in which overseas investors stopped buying our equities, the dollar would plummet and interest rates and consumer prices would spike as part of an overall economic contraction. I sincerely hope that the issue of the structural budget deficit, our fiscal priorities and the related demographic challenges we face as a nation will become the centerpiece of the debate in this year's presidential election.

All of the candidates owe the American people explanations as to how they would address the current fiscal imbalance. What mix of spending cuts, revenue increases and budget process reforms would they propose to solve this issue to prevent a crisis and the adverse impact it would have on domestic markets and international markets?

Our track record in establishing fiscal discipline is not terribly promising. But every member of Congress shares a responsibility to put national interests ahead of political self- interest and to work with the Bush administration to establish the political consensus necessary to restore fiscal responsibility. Thank you very much.

**DORGAN:** Mr. Kolb, thank you very much for that statement. I was interested in the point you made about the value of our currency as made by Senator Conrad in the chart that was showed earlier.

Let me call on Senator Sarbanes for a statement and then Senator Lautenberg, who has also joined us.

Senator Sarbanes?

**SARBANES:** Well, thank you very much, Mr. Chairman. First I want to commend you for calling this very timely hearing to review the nation's deteriorating fiscal situation, the impact of long-term deficits on America's future economic growth and job creation. And we very much appreciate this panel coming and being with us this morning.

This hearing is timely because this very evening the president will be outlining his budget

priorities for the coming year, which will give us some insight into whether the administration indeed plans to address the very serious economic problems we are now facing or whether the administration will squander an opportunity yet again to invest in America and prepare for the future. Regrettably, based on the reports that have been released thus far about the president's speech tonight, I am very concerned that we're just going to pass by the opportunity to start putting our fiscal house into order.

This administration appears to have only one economic goal, to cut taxes for the very wealthy regardless of the consequences for America's future. This policy became evident just as soon as President Bush came into office. One of his very first initiatives was to propose a \$1.6 trillion tax cut skewed very heavily to benefit the wealthiest of Americans.

That tax cut and the two that followed have been markedly responsible for a dramatic decline in our fiscal position. The president actually asserted when he came in with respect to the tax cuts. And I quote him. "Tax relief is central to my plan to encourage economic growth. And we can proceed with tax relief without fear of budget deficits even if the economy softens."

Let me repeat that. This is the president. "We can proceed with tax relief without fear of budget deficits even if the economy softens."

The Congressional Budget Office now estimates that if the tax cuts that have been placed on the books remain in affect, the federal deficit will exceed \$400 billion per year for the next decade and beyond, \$400 billion. Federal debt will rise commensurately. Meaning trillions more in debt and interest costs that our children and our children's children will have to bear.

When he proposed this first tax cut in 2001, President Bush made three promises. He claimed that this plan is good for the long-term health of our economy. He claimed it was good for the businesses that create jobs. And he claimed it is good for America and for the American families that make our country so unique and strong.

SARBANES: Now, each of these statements turned out to be an empty promise. In fact, the long-term health of our economy is in jeopardy as a result of the structural deficits created by these inordinately large tax cuts. Former Treasury Secretary Reuben and several other economists recently released a paper which described the adverse affects of long-term deficits, including higher interest rates and greater dependence on foreign capital.

The International Monetary Fund, the IMF, has also warned of the consequences of sustained budget deficits which they said could lead to, quote, "upward pressure on interest rates, crowding out of private investment and an erosion of long-term U.S. productivity growth," end of quote. Actually you read that IMF report and you're reminded of their warnings to, sort of, third world countries about the breakdown in fiscal discipline and handling of their economic affairs. Now they're applying that very, sort of, warning to the United States.

Secondly, the president talked that it would create jobs, a job creation record of this administration is abysmal. The economy actually has lost 2.9 million private sector jobs since President Bush came into office. In no administration, in no administration since Herbert Hoover has the economy failed to have a net job creation. First administration since Hoover where we're minus on the job front.

There are 8.4 million unemployed Americans looking for work today who cannot find it. That is 2.5 million more than when President Bush took office. Of those who are unemployed, 22.3 percent are long-term unemployed. They have been unable to find work for more than 26 weeks.

The level of long-term unemployment has been above 20 percent now for 15 consecutive months. This is the worst performance since 1983 in terms of long-term unemployment. So you not only have the unemployed, but you have this problem within the unemployed the problem of the long-term unemployed, which is at its worst in more than two decades.

It is worth placing the weakness of this labor in a historical context. We've been keeping this monthly job statistics since the end of the Depression in 1939. Never before have job losses persisted for so long beyond the recession. We've had 11 recessions since 1939.

For the first 10 recessions, all the lost jobs were fully recovered within 31 months of the start of the recession. In other words, we came back up to the pre-recession level within 31 months, usually much sooner. And we then went on to set new records in terms of the number of jobs.

This time, 33 months now and counting after the last recession began, we haven't simply failed to recover the number of jobs we had in March 2001, but we remain below the figure by an extraordinary 2.4 million jobs. We'd have to pick up 2.4 million jobs to get back to the pre-recession level. And we're now at 33 months beyond. Never before did we go beyond 31 months. And most times, we did much better than that. It's an extraordinarily dismal unemployment record.

Nor has President Bush kept the promise he made that I quoted earlier to American families. The president has not supported continuing extended unemployment insurance benefits to the long-term unemployed. And I gave earlier the percentages that show that they're at record levels.

As a result, many families are now without benefits. Between 2000 and 2002, the most recent data available, the typical American family has seen their household income fall by almost \$1,500. Over that same period, 3 million more Americans are living in poverty, almost 4 million more Americans have lost their health insurance.

I think the evidence is clear. This administration's single-minded focus on cutting taxes has left us with millions of unemployed Americans today and massive deficits and debt tomorrow. The three promises President Bush made when he announced his first set of

tax cuts are still unfulfilled. And yet by all reports, the president is poised tonight to announce even more tax cuts targeted to the wealthy.

In my view, the president's continued adherence to this failed fiscal policy shows just how far out of touch this administration is with the needs of the American people.

Thank you, Mr. Chairman.

**DORGAN:** Senator Sarbanes, thank you very much.

Next let me call on Senator Lautenberg who is a former chairman of the Senate Budget Committee.

Senator Lautenberg?

LAUTENBERG: That's a wishful thought. I was the ranking member. The chairmanship constantly was outside of my grasp. I wish we could change that now. Yes. I want to thank you, Mr. Chairman and my colleagues.

**DORGAN:** Well, Senator Lautenberg, you would have liked to have been chairman of the Budget Committee. Would you at least concede that?

LAUTENBERG: I would have loved it.

**DORGAN:** OK.

LAUTENBERG: I had lusted for it.

SARBANES: Thank you for correcting my error. And had he been, we wouldn't be having these problems, Chairman **Dorgan**, I hasten to add.

**DORGAN:** In any event, Senator Lautenberg was the ranking member of the Senate Budget Committee for some long while and was a very distinguished leader on these issues.

LAUTENBERG: And Gene Sperling was often on the other side of the table, but definitely in step with what we were trying to accomplish then. I'll say a word or two about that.

And I welcome all of you, and I thank you for the testimony that you've given. I apologize for having missed part of it. I am still in the throes of celebrating the birth of a 10th grandchild. And that was very nice. And so, at this stage in life, I had to drink a Pellegrino or a seltzer and that was it.

Anyway, thank you for holding this hearing on the federal budget deficits. Back in '97, I was the ranking member of the Senate Budget Committee. And we worked diligently

with the leadership of President Clinton to negotiate the Balanced Budget Amendment.

And that agreement put our government on the path to fiscal solvency after so many years of deficit spending. And it was a proud accomplishment for government. And I worked with Congressman Spratt at that time. And we shared lots of productive moments together.

I left the Senate in 2002 for my sabbatical and thinking that the federal government would be in good shape, fiscally speaking, for lots of years to come. It was crucial to get our house in order because of the arrival soon of the first group of baby boomers. When President Bush took office in January 2001, the CBO was projecting a 10-year cumulative surplus totaling \$5.6 billion.

That surplus could have been used for lots of excellent, excellent programs, pay down the national debt by 2008, which looked like it was a reality, the public debt, extend the solvency of Social Security and Medicare, increase federal investments and transportation, other infrastructure necessities, education, find cures that we seem to be on the verge of with the possibility of some stem cell research and some of the advances that have already been made. Not only would we improve our health, our physical health radically, but we also would improve our economic health as well.

And the other thing that we needed to do was to provide some critical tax relief for working-class Americans. Now using CBO data, three highly regarded groups, the Center on Budget and Policy Priorities, the Committee for Economic Development from which we heard today and the Concord Coalition project that we're going to have a cumulative deficit between fiscal years 2002 and 2011 totaling \$3.4 trillion.

The shocking reality is that we've suffered a \$9 trillion reversal of fortune in little less than three years. The president and his allies in and out of Congress are quick to blame the recession on the terrorist attacks of 9-11 as the chief culprit. But we noted with interest the chart that was presented that showed the position of the various principle expense centers and tax cuts dwarfs them all.

Mr. Greenstein, you showed that chart.

That's part of the problem because three rounds of tax cuts have had the biggest impact on the federal budget. Now according to these groups that I mentioned, more than one-third of the \$9 trillion reversal of fortune can be attributed to not only the careless but reckless and deliberate tax cuts that this administration and its allies have ran through Congress.

It fulfills a mission that they've set out for themselves. One-third can be attributed to increased spending, almost all of which has been for defense and homeland security as well as some counter-cyclical programs, some unemployment insurance to kick in automatically. But finally, a bit less than one-third can be attributed to the recession that started on this president's watch in March of 2001 and the slower than anticipated



economic growth since the recession officially ended in November 2001.

So we've gone from projections of a \$5.6 trillion surplus over 10 years to a \$3.4 trillion deficit, all of that within a matter of months. And I say that you can't foul things up that much by accident. It has to be by design. And the design is something that the Republicans planned as their mission to starve the beast.

They've pushed the tax cuts through in large part to create budget deficits that'll force Congress to cut spending. Republican activist, Grover Norquist, president of The Americans for Tax Reform, said -- and he speaks loudly for this administration. I simply want to reduce it -- of course, that means the government -- to the size where I can drag it into the bathroom and drown it in the bathtub. Conservative economist Milton Friedman had an op-ed piece in the Wall Street Journal last January stating that the budget deficits serve the useful purpose of disciplining the Congress.

What an outrageous thing that is to say. The cynicism and recklessness of this policy cannot be overstated. And the thinking of it, with the first baby boomers on the verge of retiring, is catastrophic, the timing of it. So much so that the International Monetary Fund recently warned us that the policy threatened Social Security, Medicare and our voracious appetite for the credit necessary to sustain these huge budget deficits.

It could precipitate a currency crisis, snuff out the economic recovery. And not just in the United States. But we have countries around the world worried about how it might dramatically affect the economies of countries around the globe. And future generations are going to look back at what's happening now with bewilderment and rage.

So some might say this is an exaggeration. I don't think so. And the fact that they're so committed to extending this reduction -- I have to be very careful in my words because I get very angry about this -- this reduction in our resources incapacitating us from taking care of the programs that are necessary for a sustained Democratic society is outrageous.

And I thank the witnesses for their excellent statements and for the credibility that they lend to the concerns that we all have about the precarious condition of our economy and ultimately our way of life. Thanks very much.

**DORGAN:** Senator Lautenberg, thank you very much.

**DORGAN:** I'm going to call on my other colleagues to question. But one question that follows on something Senator Lautenberg just said, two mornings ago, I was watching a morning show on television. And the chairman of the Republican Party told the interviewer on NBC, "Look, President Bush inherited a recession. What do you expect?"

Senator Lautenberg just referred to the question of when the recession began. Mr. Spurling, could you tell us did President Bush inherit a recession?

**SPURLING:** The recession, according to the organization the NBER, started in March.

So I think it is fair to say that President Bush inherited an economy that had a mixture of economic trends. I think there's no question that the record expansion, the longest expansion in history was no question at that point, particularly in manufacturing, starting to decline.

On the other hand, we also -- he also was inheriting the strongest fiscal situation probably in the history of the country, unemployment rate at around 4.1, 4.2, a productivity rate that had doubled over the previous five years. I think that, you know, presidents both get too much credit and too much blame for the economy. I think the right thing to do is to look and say, "Given the hand that a president inherits, did they do everything in their power?"

President Clinton inherited a first quarter that was actually negative. I think it was just changed. But people forget that the first quarter of 1993 was negative. There was nearly 10 percent unemployment in California, over 11 percent unemployment in West Virginia. It was a very difficult period.

I think that the commitment that really surprised the world-wide markets that a Democratic president, Democratic Congress would implement fiscal discipline and that they might be able to get it done provided a bit of a tipping point in confidence and led to a fall in interest rates. I think many people will disagree with this, but I think the president's commitment to open markets and competition, all of those sent a sense that there was going to be renewed focus on the domestic economy.

I could go over -- and I think that -- what I just want to say is that that continued for all eight years while we battled over how to balance the budget in '95. People forget that Newt Gingrich and President Clinton were both agreed to the concept of fiscal discipline and that it should be paid for. And that the debate that led to the shutdown was due to how to do it, not whether fiscal discipline mattered or whether new proposals should be paid for.

And then the 1997 bipartisan balanced budget agreement and the commitment to save Social Security first -- which was a commitment really to tell both parties that their larger spending initiatives had to be on hold until we completed the task of knowing how to finance our long-term Social Security and Medicare challenges. I think when you look at what President Clinton inherited, those were the type of steps a president could take that could help lay a foundation for things that were happening in the private sector.

I think President Bush inherited a situation where we needed a few things desperately. We needed very strong fiscal stimulus right away. And I was one who called for that and called for short-term tax cuts for that, number one. Number two, we needed to show the world that while we were going to do long-term, we were going to do fiscal stimulus, that we were going to retain a commitment to long-term fiscal discipline.

In other words, we needed to maximize the amount of demand to stimulate job growth while at the same time showing that we were still going to keep long-term fiscal

discipline and give people confidence in our long-term economic prospect. I believe what this president did was flip those -- was get that upside down. They did the least amount of fiscal stimulus possible at the largest impact towards our long-term fiscal discipline.

So we got the smallest bang for the buck in the short-term with the worst harm to our long-term fiscal situation. And so, I think the way we should judge the president is not simply by, you know, the numbers, but by looking at whether he had truly done everything in his power. And I think a record going back from 2001, 2002, 2003 shows a president who inherited some slowing in the economy but many strong fundamentals.

And I think that had the president done everything in his power to maintain long-term fiscal discipline and stimulate job growth in the short-term, that even if we didn't have great economic performance now, the public and even those of us on the other party would have to recognize that effort. Unfortunately I cannot. I think that he has hurt our long-term confidence.

In the economy, when you talk about job growth here, Senator, I think it's very important to recognize what's happening in this economy right now. We are not being killed by an excess of job loss. We are being killed by a lack of job creation. The focus is on outsourcing and all the ways we're losing jobs. But the real impact is that we're not creating new jobs.

Why are people so hesitant to invest in this economy? Why is venture capital so hesitant to put more money behind new companies and new firms and new ideas in the way there was in the '90s? Certainly there is a higher risk premium on investment in the United States. Certainly it is a riskier prospect.

Certainly we are seeing hesitancy across the board. And I think the sense that we have a long-term fiscal ticking time bomb with no sense of fiscal leadership to deal with it is certainly at least a component in that higher sense of risk in the U.S. economy.

**DORGAN:** Mr. Sperling, for the first time in my memory, we actually have a blueprint of what has happened in the last two and-a-half years with fiscal policy. The secretary of the treasury has participated in the writing of a book. I've just finished reading that book, as I indicated, last evening. It describes in some significant detail the construction of this policy. And what it says, by the person who was the secretary of the treasury at the time, is that this had nothing to do with the kind of discussion you've just had this morning at the witness table, economic theory and this whole series of considerations about the impact of various economic strategies.

It had to do with respect to the political shop in the White House deciding what they wanted to say to their political base and what kind of policies were necessary to communicate with their political base. I have not in my lifetime seen a book of this type. It is a book giving us a direct road map on exactly what transpired to construct this -- not fiscal policy, but political policy, masquerading as fiscal policy.

SPERLING: Just one thing I would just highlight in that book was I learned about (ph) that in March of 2001 at the very beginning. And my message was that whether you were Chris Edwards and supported private accounts for Social Security reform or you were Gene Sperling and didn't support a carve-out private account -- but whatever Social Security plan you supported, it needed fundamental new savings for the transition costs to new Social Security.

**DORGAN:** Correct.

SPERLING: So that whatever side you were on, the one thing you should agree on is that need and that this tax cut would deplete in any ability to use the surplus to help formulate any Social Security reform. And I was interested to see Secretary O'Neill say, not just in the book, since those of us in the Clinton administration are understandably a little hesitant to believe everything we read in books -- but what he said personally on 60 Minutes was that he made exactly that argument to the administration that this would hurt the president's own vision for Social Security reform and that that was completely dismissed.

**DORGAN:** Well, former Secretary O'Neill will pay dearly, I'm sure, for the transgression of being candid about what happened in the construct of that fiscal policy. But my own view is that Secretary O'Neill has given great service to this country. And I, for one, appreciated reading the book and understanding what had happened then.

Congressman Spratt?

SPRATT: Thank you very much, Mr. Chairman. Here we go.

Mr. Greenstein, your organization, the Center on Budget and Policy Priorities, combined with Mr. Kolb's -- in South Carolina, we say Kolb -- Committee for Economic Development and with the Concord Coalition and came up with a study and analysis of the budget last fall shortly after the Congressional Budget Office had issued their fall summary of the budget. And in the document you put forth, mid-term and long-term deficit projections, you undertook to use the CBO analysis to restate the budget over a 10-year period of time using the original timeframe for the Bush administration, 2002 through 2011.

I'd like to walk through that analysis. On page 12 of your study -- Mr. Cogan (ph) is sitting in the back of the room. I think he's the author of this -- you might even want to -- do you have a copy of it, Richard? It just so happens?

RICHARD COGAN (ph): I didn't think of bringing it here. I'm very sorry. But I may have memorized page 12. So,...

SPRATT: No, I don't think so. No. In any event, I'll give you the numbers. We start out with \$5.61 trillion. That was the amount that was estimated as cumulative surpluses between 2002 and 2011 by the Office of Management and Budget, Bush's budget shop

when he took office, January 2001.

As I said earlier, no president in my recollection has had that kind of fiscal advantage at the beginning of his administration. However, you first suggest that the \$5.61 trillion needs to be whittled down with some political reality. For example, the assumption that CBO has to use or that OMB sometimes uses that certain tax concessions when they expire, deductions, credits, what have you, will actually expire and disappear and therefore, revenues will go up.

In truth, they almost always, particularly the popular concessions, they're almost always renewed and therefore, you have a continued level of revenues and not an uptick in revenues. In addition, there is something looming over all this problem called the alternative minimum tax, which we've been able to defer and put off with one and two-year fixes.

But ultimately the treasury, the Bush Department of Treasury tells us that 30 million Americans by 2010, tax filers, will be faced with the alternative minimum tax, paying taxes at a higher rate than they otherwise would pay. And that, I think, will make the so-called marital penalty look like a tempest in a teapot if it hits us with that full fiscal impact.

So you made a few adjustments and whittled the \$5.6 trillion cumulative surplus down to \$4.975 trillion. And that was the baseline, the adjusted baseline, around \$5 trillion. Then you went to CBO and looked at their restatements of the budget over the time period 2002 through 2011. And with respect to the economy, a slower, more stagnant economy, CBO said that \$800 billion, \$700 billion had to be taken out of the surplus to account for the slower economy.

So when the question was put earlier what impact has the economy had on the budget, CBO at least, who tend to be honest brokers, CBO said about \$700 billion to \$800 billion. In addition, however, there are technical estimating rules based on past experience that have not produced the same results as we would have expected based upon previous experience.

For example, in the 1990s, we had a phenomenon where every year for seven or eight years, tax revenues grew faster than taxable incomes. And as a result, tax revenues per dollar of GDP were higher than they had traditionally been, and CBO kept assuming that. OMB kept assuming that that phenomenon would largely continue. And it hasn't continued.

They made a substantial adjustment in the surplus projection for technical reestimates, \$2.621 trillion. So I'm getting down now to the nub. If you add the \$674 billion for economic reestimates and the \$2.621 trillion for technical reestimates, the reapplication of technical estimating rules, you get about 2.3, \$2.4 trillion. No, excuse me, \$3.3 trillion or \$3.4 trillion to be subtracted from the \$5 trillion or from the \$5.6 trillion. Which means we really didn't have, according to the current construct, we really didn't have between

'02 and '11 a \$5.6 trillion surplus. That construct is now more like \$1.6 trillion to \$2.3 trillion. Is that correct?

GREENSTEIN: Yes.

SPRATT: And consequently, how much of the remaining restated surplus has already been taken up, wiped out by tax cuts enacted to date in addition to the debt service or the interest increment that has to be added on due to the fact that you have less revenues?

GREENSTEIN: More than 100 percent of it. In other words, if you take the tax cuts that were enacted and you assume that they're extended, as the administration has proposed, and you also factor in the additional cost that the 2001 tax cut created with regards to addressing the alternative minimum tax, I believe the combined affect exceeds the \$1.6 trillion or \$1.7 trillion that would remain after you adjust for the economic and technical estimates.

A key point on the alternative minimum tax, when President Bush took office, we already had a serious problem there. It was projected that at the end of the next decade 20 million Americans would be subject to the AMT as compared to 2 million that were currently subject. And everyone understood that wouldn't be allowed to occur, and therefore, there was a big expenditure out there not reflected in the baseline.

The Bush tax cut was constructed in a way that to make it fit within the official amount allotted for it in the budget resolution in 2001. It was designed in a way where we violated what we'd always done in the past. In the past, it was understood that if you lowered tax rates, you had to make corresponding changes in the AMT. And if you had X amount of money available for a tax cut, some of that had to be used for the AMT adjustments that went with whatever tax cut you were making.

Instead, the designers of the 2001 tax cut decided to adopt what can only be described as a massive budget gimmick which was not to address the AMT to allow millions of additional people to be thrown on the AMT so that at the end of the decade, instead of 20 million filers being subject to the AMT, 35 million filers would be subject to the AMT.

In other words, they made the almost inevitable cost of addressing the explosion of the AMT hundreds of billions dollars greater than it otherwise would have been. And we will pay those costs. So factoring all those in, the combined cost would exceed 100 percent of what remained.

SPRATT: Mr. Kolb, your organization participated in this study. Do you essentially agree with this table on page 12?

KOLB: Yes, sir, we would agree with that.

SPRATT: That we didn't have to start with this \$5.6 trillion surplus, or at least it now appears in retrospect?

KOLB: I think that's correct. Yes, sir.

SPERLING (?): Actually, Richard is pointing out to me that on page 12, as you noted, the total cost of the tax cuts if you extend them -- and including the AMT relief -- is \$3.4 trillion. That's double the \$1.7 trillion that would remain from the \$5 trillion after you adjust...

SPRATT: Some of that has been enacted. Some of that is expected to be enacted, particularly the alternative minimum tax. And the rest is an adjustment for debt service, interest on the national debt due to the fact that you have less surplus, and therefore, you have to pay -- I mean, more deficit, and therefore, you have to pay more debt service.

SPERLING (?): That's precisely correct.

SPRATT: Yes. And then you make some other adjustments, defense, international homeland security. Homeland security, of course, was a rubric that didn't even exist in the budget a couple of years ago. Now it's a whole new account. Some of it is reclassified costs, but some of it is genuinely new spending. How about national defense?

By our calculation, national defense per the Bush administration's current program, leaving out for the most part any expeditionary costs for Iraq and Afghanistan after '04, easily comes to \$1 trillion over and above current services as projected in 2001. Do you concur with that?

GREENSTEIN (?): Well, we did the analysis a slightly different way so it would also include Iraq and Afghanistan. And our total was \$1.8 trillion. But I think the figure you mentioned is consistent with (inaudible).

SPRATT: Well, you tried to estimate some out-year costs beyond 2004 for the expeditions in Iraq and Afghanistan.

GREENSTEIN (?): Not exactly. What we looked at was, as you know, the administration has a multi-year defense plan. It's called the future year defense plan.

SPRATT: Yes.

GREENSTEIN (?): And the Congressional Budget Office issued a study last summer that found that in the president's budget that was issued a year ago, the outer costs for the future year defense plan were understated. The numbers in the budget didn't correspond to the actual costs. So we included the costs of funding the administration's own future year defense plan.

SPRATT: All of those added up to \$1.8 trillion over 10 years in your estimation. And once again, the Committee for Economic Development basically concurs in those estimates?

GREENSTEIN (?): Yes. Yes. What Richard is explaining is we used the CBO assumptions in that report from last summer about Iraq and Afghanistan costs, which showed some costs after 2004, but showed them dropping.

SPRATT: Well, CBO baselined the costs, and you recognize that that probably overstates the cost. Let's hope it does. So you, I think, back the number out of the baseline but then adjusted it.

GREENSTEIN (?): Well, we backed out of the baseline the assumption that the supplemental is reenacted every year. And then we added in some figures based on CBO's assumptions that there would be some costs after '04, but that they would scale out pretty quickly. So I think we were quite conservative. We did not add large amounts for the out-years for Iraq or Afghanistan.

SPRATT: Now then you made a few other adjustments for Medicare. Prescription drugs, of course, was not in the 2001 baseline. You added that at \$328 billion, which was the number, I believe, in the Republican budget resolution.

GREENSTEIN (?): Yes.

SPRATT: And it turns out to be on the low side of what that's likely to cost. You've got a few other adjustments for domestic spending and for entitlement spending. You quibble about those, but they aren't big numbers. The bottom line is you, by making these adjustments, take the \$5.6 trillion surplus and convert it to a \$4.371 trillion deficit, a swing of \$10 trillion just about.

GREENSTEIN (?): A swing of \$9 trillion, because we're starting at \$5.0. And so, it's a swing of about \$9.3 trillion, to be precise.

SPRATT: Yes. And, Mr. Kolb, your organization agrees with that and so, I take it, did the Concord Coalition?

KOLB: We did this jointly, yes, sir.

GREENSTEIN (?): These are all joint estimates.

SPRATT: Thank you very much.

**DORGAN:** Congressman Spratt, thank you very much.

I've asked Congressman Spratt if he would take the chair. I have to be on a 12 o'clock live broadcast over in the Russell Building. And I do want Congressman Scott and Congresswoman DeLauro to be able to ask questions.

This, I think, has been an excellent panel. And as we wrap up with these questions, let me



again say that I don't think there is a much greater priority anywhere in the landscape here in federal policy than to begin to straighten out this fiscal policy because it will have profound implications for years and for decades to come. I think several of you mentioned that this is kind of a time bomb that faces us.

The largest group of babies ever born in American history were born when the second World War ended. And as our troops came home, there was this outpouring of love and support, and we had the largest crop of babies produced in the history of our country. That crop of babies, when it hits the retirement rolls, creates maximum strain on Social Security and Medicare.

And my colleague, Senator Conrad, keeps talking about we don't have the luxury that we had a decade ago dealing with these deficits. We have to get it right now. We have to set this back on track because we have some significant challenges in front of us.

Congressman Spratt, thank you for being willing to take the chair as we complete.

And let me recognize Congressman Scott.

SCOTT: Thank you. And I want to express our appreciation, Senator, for your leadership in calling us together and getting this good information.

Mr. Spratt, we're tight, so let me ask some quick questions so that both Rosa and I can get questions in, some specific questions.

Mr. Greenstein, did you indicate that the Medicaid inflation was greater than or less than the health care inflation?

GREENSTEIN: Well, you know, some years it's a little more, some years it's a little less. In general, Medicare inflation, Medicaid inflation, general health inflation in the private sector, they've all been rising at a substantial rate. You generally do not see a substantially faster rate of growth in recent years in Medicare or Medicaid than in the private sector. There have been some years where the private sector health care costs rose more rapidly than the Medicaid and Medicare costs.

Now we do have one situation where Medicaid costs tend to rise a little more rapidly from year to year when the economy goes down and a little more slowly from year to year when the economy is booming. For the obvious reason that during economic downturns, more people lose their jobs and become eligible for Medicaid. When the jobs come back, they go back to work. They get employer-based health insurance, and the number of people eligible for Medicaid goes down a bit.

So we have seen some affect there. We also have in the federal Medicaid figures for the current year \$10 billion because the Congress last May provided \$10 billion in temporary, one-time only fiscal relief to the states. They provided \$20 billion in fiscal relief, \$10 billion of it in the Medicaid program. That \$10 billion is very important.

The study that we issued a few weeks ago found that that \$10 billion prevented some hundreds of thousands of additional low-income elderly and disabled people, children and working poor parents from losing their health insurance coverage.

But as a general rule, I would just say Senator **Dorgan** said a minute ago that in the long-term, we have a problem as a result of the retirement of the baby boomers. Budget analysts tend to sort of see two joint problems on the spending side in the long-term because of the retirement of the baby boomers.

And there's the fact that health care costs system-wide, private sector just as much as public sector, are rising at a very rapid rate, primarily because we keep making these medical breakthroughs and advancing medical technology in ways that improve health and prolong life and save lives. And we all want them, and they're expensive. And they tend to be more expensive than the older technologies they replaced.

And when you put together the combination of an aging population -- because older people have higher health care costs -- and continued breakthroughs in medical technology, it's kind of the combination of those two that when we did our joint statement, we found the combination of the two is very powerful. It's not just one or the other, but both together.

But it would be a mistake to say that it's just Medicaid or just Medicare. If one were to try to sharply slow the rate of growth in Medicaid and Medicare costs without doing anything about the rate of growth in private sector health care costs, then the only way to achieve that would really be by having a two-tier health care system where poorer people are denied basic services or made to pay amounts they can't afford compared to higher-income people or where we were going to cut Medicaid back and increase the ranks of the uninsured way above the 44 million who are already uninsured.

So we have got to find ways to slow the rate of health care costs system-wide, not just in Medicare or Medicaid, but system-wide in the private as well as the public sector. And unfortunately, we don't know very well how to do it.

SPERLING (?): Could I underscore just one point that Bob said? That is the real difference between the structural budget deficits that we see now and what we experienced 20 years ago. It is that combination of demographic challenges with the tax problem that creates really new terrain for all of us. And that's why it's such a serious problem that we just can't, with all due respect, grow our way out of.

SCOTT: Mr. Kolb, let me ask you a question. You indicated that we're obviously issuing a lot of debt. Who's buying the debt?

KOLB: Well, right now it's still being purchased by overseas investors, including governments as well as private investors.

SCOTT: Like which governments?

KOLB: Well, China has been one major...

SCOTT: Any national security implications in that?

KOLB: Well, that's been discussed. I think at this point, it's a hypothetical. I do think it's nonetheless worth considering.

SCOTT: If we had an international disagreement with China, would they not be at a significant advantage because they're buying our debt?

KOLB: I don't know how significant it would be. There would certainly be an advantage, and it's something we should definitely take into consideration.

SCOTT: What happens if they stop buying it or, in fact, started dumping it?

KOLB: Well, that would have an adverse impact on our economy, certainly on the dollar. And we also -- I think the other thing to bear in mind is we have assumed now for many, many years, really since the Bretton Woods system, that the dollar would be the unofficial reserve currency, if you will. And I don't think you can rule out the possibility of competition from the euro, which, as noted earlier this morning, is strengthening or even possibly the yen.

So we just assume that we'll be able to print all these dollars and someone will buy them. I'm not so sure that that's something we can project out into the future all that long.

SCOTT: Thank you.

I had another question for Mr. Sperling.

SCOTT: And I'm going to ask it and then defer -- before he gets to answer it, defer to Representative DeLauro so that she can get her questions in. And that is just simply whether or not if there is no profound change in direction, can we realistically pay for Medicare and Social Security on a long-term basis, particularly after 2017 when it starts running a deficit. But before you get to answer, let me defer to Ms. DeLauro.

DELAURO: I'll try to be very quick because we have a vote at noon.

And I have a question for Gene. And I'll just leave it about what should comprise a stimulus program, but we'll get to it at another point. When President Clinton came to office, if I understood John Spratt's comments a couple of days ago, he had a \$290 billion deficit. As we were paying that deficit down, we also dealt with making some very serious real investments in education, health care, et cetera.

I was struck by the difference of views between Mr. Edwards and Mr. Greenstein about

runaway spending and the lowest share of spending since, you know, '75 through '96. So, Mr. Edwards, where do you cut? Homeland security, foreign affairs? What are you proposing with what you're saying and what direction we go in with regard to spending?

EDWARDS: Well, I think the federal government will simply not be able to do a lot of the things it has in past decades because of the entitlement squeeze. I mean, education is an area, for example, we spend about \$60 billion a year on now. That's gone up from \$35 billion just in about three years. That is traditionally, of course, a state and local responsibility. And it strikes me that because of the entitlement squeeze, the federal government will not be able to do that sort of spending when it's traditionally state spending in the future.

There's many federal programs that I think have become long obsolete, rural programs. Transportation spending is primarily a state responsibility and I think should be moved back to the states. I think some of the ideas -- and I've cited in my testimony a list of about \$500 billion in cuts. That sounds really radical today. But I honestly believe 10 years from now some of the cuts that, you know, the Cato Institute and I are proposing will not seem radical 10 years from now.

Again, the crisis starts later in this decade. You see by 2013 Social Security, Medicare and Medicaid start rising as a share of GDP forever and ever and ever for decade after decade. And so, the cash crunch starts in less than 10 years. And so, I think a lot of these spending cuts will not seem radical 10 years from now.

DELAURO: A quick rebuttal here or response.

GREENSTEIN (?): I think there's two things. If we look at how we had this \$9 trillion swing over the past few years, increases in domestic spending have been a small part of it. They're dwarfed by the defense, anti-terrorism and particularly by the tax cuts. If you look long-term out several decades, a very large development there will be substantial increases in spending. Social Security and Medicare costs go up because of the aging of the population and the increase in health care costs.

To me, Chris' proposal which he's published -- Cato has published and he's referred to here -- on how to balance the budget while leaving all of the Bush tax cuts in place is to me a perfect illustration of why we, MCEd and Concord and ended up saying you have to do stuff on both the tax and spending side. And what I mean by that is Chris' proposal -- and, you know, I give him credit for -- there are no smoke and mirrors. He puts it right out there.

But his proposal -- he'll correct me if I'm wrong -- if I understand it correctly, it essentially calls for eliminating virtually all federal spending on education, transportation, housing, eliminating a big part of the Agriculture Department, terminating food stamps, school lunches, the WIC program, major cuts in veterans' programs.

Now whether you think that's wise or not -- I happen to think it's not. It's not going to

happen. Not to say there won't be any cuts in some of those areas at all. But we're not going to eliminate all that stuff. It isn't going to happen. And the only way he gets to balance in 10 years is, without any revenue changes, is to eliminate all that stuff. And I think this is kind of why when we all looked at it, our three groups, we said we're going to have to do tough things on the revenue side as well as on the spending side.

I happen to focus on the revenue stuff here today because my concern is that over the coming year we could make changes that dig the hole even deeper on the revenue side. In the long-term, we have some tough decisions, both on the revenue side and in terms of areas like Social Security.

DELAURO: Gene?

SPERLING: Yes. I want to go back to a point I was making in terms of the sense of shared sacrifice. I mean, I would probably disagree with many of the cuts that Chris proposes. But one has to be open to the idea that we could have national security challenges in the future or we could truly face emerging deficits that would force us to do things that we would prefer not to.

But right now, you look in the year 2013, 10 years from now, and you see that there are about \$400 billion in that one year, \$400 billion. Imagine going to a constituency and saying for the sake of your nation, patriotism so that we can prepare for terrorism or to get our economic house in order, you've got to make this painful \$10 billion cut in education or transportation and health care.

How could one possibly make that case to the American people when you've been able to afford, as Bob shows, about \$90 billion a year just to the top 1 percent and as many as just over \$400 billion, as much as \$500 billion, \$600 billion with interest costs in that year? In 1993, there were Medicare and Medicaid savings in the plan that you had. There were also increases in Head Start and the EITC.

DELAURO: Yes.

SPERLING: You can't -- to me, the problem with this kind of argument is you can only make the case for this type of spending cuts if you're showing that it's across the board. You will never get a political consensus nor should you when you're saying you can afford luxurious tax cuts for the most well off, but you're going to ask for this kind of sacrifice. I think in the future we are only going to get fiscal discipline if we have some kind of leadership that puts everybody's priorities on the table in the sense of shared sacrifice again.

SPRATT: Mr. Scott, any further questions?

EDWARDS: Can I just touch on the issue of tax cuts? A lot of the panelists have talked about the tax cuts as if they were, sort of, the idea of them was just to transfer money from the government sector to wealthy, private folks. But the way I look at the tax cuts is

the U.S. tax system operates now within the global economy.

We have to compete with other countries on the tax side. One of the future fiscal realities is certainly the entitlement spending crisis. But the other one is that every country in Europe is cutting taxes on capital income, dividends, capital gains, corporate tax rates. President Bush this last year cut the tax rate on dividends. We are only one of three OECD countries -- and there's 30 of them -- that did not provide relief for the double taxation of dividends.

In the future, the U.S. economy will be competing for capital flows. And we need an efficient tax system in order to attract those capital flows. So the tax cuts were not just about giving money to people. They were about responding to real problems in the tax code that I think we need to face.

SPRATT: Mr. Greenstein?

GREENSTEIN: Well, a couple of points, of course, most Western European countries actually have significantly higher tax collections as a share of the economy than we do. And as I read recent studies like the joint study by former Secretary Reuben, Peter Orszag of Brookings and Alan Sinai, who is a Wall Street economist who, I think, in 2001 largely supported the tax cuts at that point -- their new joint study warns, among other concerns, that our long-term deficits are now so large, the projections are so big that we run the risk that foreign capital will be less willing to come in because it will be nervous about the future of the U.S. economy and whether we'll just inflate our way out of the debt and things of this sort.

You know, when you look at a series of recent studies, the CBO study last year that commented on the affect of the tax cuts, various Brookings studies, a study by two of the leading economists at the federal reserve, the conclusion they all came to is that while certain changes in the tax system, particularly regarding marginal tax rates, by themselves, had they been fully paid for, could have an economic gain. But you have to weigh that against the economic drag, the negative economic affect from larger deficits.

And the finding of most of those studies is that the long-term affect on our economy is likely to be -- in terms of economic growth, will either be very small or negative. A quick quote from the CBO study last year that said, quote, "Tax legislation will probably have a net negative affect on saving investment and capital accumulation over the next 10 years."

So you could have made -- I think the case Chris is making -- although I would disagree with regard to the dividends and capital gains to some degree because of the differential between that and the regular rate creating more opportunities for tax shelters. But in any event, you could have made the case for certain of the tax cuts if they hadn't resulted, contributed to these big, additional deficits.

If we either really had had those surpluses or if we had paid for the tax cuts. But we've

done neither. So the long-term affect is more likely to be negative on the economy in terms of future economic growth than positive.

SPRATT: Mr. Kolb, do you care to join in this fray?

KOLB: I would just add one thing, which really has not come up in the discussion much this morning. And that is I think in addition to the suggestions with regard to spending and revenue raising, there's a third issue. And that is the reinstatement of serious, effective budget process reform.

And, you know, quite frankly sometimes both the Congress and the administration can't help themselves. And I think we have in the past seen some tough decisions made, but they came about through the forging of a political consensus that was accompanied by significant self-restraint, if you will.

My first boss in government...

SARBANES: Mr. Spratt, I think we have about three minutes left on the vote.

SPRATT: I beg your pardon.

KOLB: David Stockman talked about the triumph of politics, and I would urge you not to let that continue and to enact the type of reforms that will protect all of us.

SPRATT: Your point is extremely well taken. We agree with it.

KOLB: Thank you.

SPRATT: And we're sorry to rush off. We very much appreciate your participation.