Testimony before the Senate Committee on the Budget
Co-Chairmen of the President's Commission on Fiscal Responsibility and Reform
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Chairman Conrad, Ranking Member Sessions, and Members of the Committee, thank you for inviting us to appear today to discuss the recommendations of the National Commission on Fiscal Responsibility and Reform. We particularly want to thank Chairman Conrad and Senator Crapo for your work on the Fiscal Commission, as well as Senator Warner for the leadership you have provided in keeping the Commission's recommendations at the forefront of the debate in Congress. We hope that the hard work and courage that you have shown will lead the way to serious action.

The need for action

As Co-Chairmen of the National Commission on Fiscal Responsibility and Reform, we spent most of 2010 studying the cold, hard facts concerning our nation's fiscal situation. Every member of our Commission came to the same unavoidable conclusions: The fiscal problems our nation faces are real. The solutions will be painful. There is no easy way out. Everything must be on the table. And Washington must lead.

Over the course of our deliberations, the urgency of our mission became all the more apparent. The contagion of debt that began in Greece and continues to sweep through Europe shows us clearly that no economy will be immune. If the U.S. does not put its fiscal house in order, the reckoning will be sure and the devastation severe.

We believe that if we do not take decisive action our nation faces the most predictable economic crisis in its history. The current fiscal path we are on is simply not sustainable. Spending is rising rapidly, and revenues are failing to keep pace. As a result, the federal government is forced to borrow huge sums each year to make up the difference. In bad economic times, such borrowing might make sense in order to soften the blow of a recession. Our concern is not so much the record deficits we face today, although they do cause us real worry. Our principle concerns are the prospects that borrowing will remain high throughout the decade, and rise substantially as time goes on. Under a reasonable set of assumptions, our national debt will surpass 90 percent of Gross Domestic Project (GDP) by the end of the decade, a level not seen since just after World War II, and a level most economists find problematic.

The demographics are not our friend. Over the long run, as the baby boomers retire and health care costs continue to grow, the situation will become far worse. By some time next decade, revenue will be able to finance only interest payments, Medicare, Medicaid, and Social Security. These mandatory payments will squeeze out funding for all other priorities. Every other federal government activity – from national defense and homeland security to transportation and education – will have to be paid for with borrowed money. Unfortunately, these pressures are no longer just long-term problems; they are increasingly becoming short- and medium-term issues. The Congressional Budget Office reported earlier this year that Social Security outlays exceeded revenues last year, and will remain in the red permanently.

In addition to our debt problems, we have a budget that focuses too much on consumption at the cost of important investments, and a tax code that is grossly inefficient in terms of encouraging work, investment, and global competitiveness. This outdated, inefficient and overly complex tax system is a drag on economic growth and competitiveness. Reforms must be made in a way that would strengthen our competitiveness.

Continued inaction and short term fixes do no represent viable, sustainable options for our country. This kind of uncertainty and avoidance is not an acceptable course of action for a responsible government. If not addressed, burgeoning deficits will eventually lead to a fiscal crisis, at which point the bond markets will force decisions upon us. If we do not act soon to reassure the markets, the risk of a crisis will increase, and the options available to avert or remedy the crisis will both narrow and become more stringent. If we wait ten years, CBO projects our economy could shrink by as much as 2 percent and spending cuts and tax increases needed to plug the hole could nearly double what is needed today.

Predicting exactly what a debt crisis would look like or the precise level of public debt that would trigger such a crisis is difficult, but the consensus of the experts we met with was that the risk will grow as our debt does – particularly if we have no plan to bring it back down, as a share of the economy, in future years.

Summary of Commission Plan

In establishing the Fiscal Commission, President Obama gave us a two-part mission: to bring the budget into primary balance (balance excluding interest costs) by 2015, and to meaningfully improve the long-run fiscal outlook. Our recommendations accomplish both of these goals through an aggressive, fair, balanced, and bipartisan proposal – a proposal as serious as the problems we face.

The Fiscal Commission put forward a comprehensive fiscal plan that included over sixty specific recommendations for reforms of spending programs and the tax code, and many other illustrative options. The plan would achieve nearly $4 trillion in deficit reduction through 2020, more than any effort in history, by going after every sacred cow, while protecting the most vulnerable and prioritizing investments in education, infrastructure, and high value-added R&D. The plan would stabilize the debt beginning in 2014, one year earlier than the President’s goal, and reduces debt to 65 percent of GDP by 2020 (and 60 percent by 2023). It cuts our deficit in half by 2015 to 2.3 percent of GDP, surpassing the goal of 3.0 percent. By 2020, our plan cuts the deficit by three-quarters to 1.2 percent of GDP. Over the long-run, the plan makes additional reforms to ensure lasting solvency for Social Security and put in place tools to control federal health care cost growth. Though long-term projections are always far less accurate than short-term ones, we estimate the commission plan would balance the budget and bring the debt down to 40 percent of GDP by 2035. To the extent our plan results in faster than projected economic growth, we could reach a balanced budget sooner.

The plan is built on six responsible, balanced, bipartisan principles:

1) We wanted to make sure we did not do anything that would adversely affect a very fragile economic recovery. Growth is essential to restoring fiscal strength and balance. That is why we delayed getting spending back to pre-crisis levels until 2013, when spending in our plan returns to 2008 levels in real terms.
2) We wanted to make sure we protected the truly disadvantaged. We must ensure that this nation has a robust, affordable, fair, and sustainable social safety net. That is why we focused benefits on those who need them the most through policies such as an increase in the minimum benefits under Social Security and a twenty year bump up in Social Security for the very old and long-term disabled. And we did not recommend any fundamental policy changes to income support programs for the most disadvantaged, such as unemployment compensation, food stamps and SSI...
3) We wanted to make sure we keep the nation secure. But both our nation's economic and national security depend on us putting our fiscal house in order. Admiral Mullen, Chairman of the Joint Chiefs of Staff, has said that our debt is our greatest national security problem. We do not believe this country can continue to spend more than the next fourteen largest countries combined on defense.
4) As President Obama said in his State of the Union Address, our nation must continue to invest in education, infrastructure and high value research if we are to compete in a knowledge based economy. We should cut red tape and unproductive spending that hinders growth and job creation, while at the same time investing in those areas that will help create jobs and keep us globally competitive. But these investments must be done in the context of a fiscally responsible plan. That is why we recommended a 15 cent a gallon increase in the gas tax to pay for transportation spending. It is also why we called for a cut and invest committee to provide resources for education and high value research.
5) The tax code must be reformed to broaden the base, lower rates for individuals and employers and reduce the deficit. We need to reform the corporate tax system to make America the best place to start and grow a business and create jobs. This can be done by eliminating or significantly reducing tax expenditures which are often nothing more than inefficient spending in the tax code. Tax reform should be done through a "zero based budgeting" approach which starts with all tax expenditures wiped out and dramatically lower rates, forcing advocates of certain tax expenditures to justify why they should be added back and how to increase rates to

pay for them. If we eliminated all tax expenditures, we could eliminate the Alternative Minimum Tax, bring individual income tax rates down to 8 percent, 14 percent, and 23 percent and the corporate rate to 26 percent while reducing the deficit by $80 billion in 2015.

6) We must end redundant, wasteful, and ineffective federal spending wherever we find it, while demanding productivity in Washington. We must cut spending we cannot afford, with no exceptions. All the talk so far has focused on domestic non-security discretionary spending. We could eliminate all non-security discretionary spending this year and still have a deficit of over $1 trillion. Clearly we must reduce all excess spending – including defense, entitlement spending, and spending in the tax code as well as domestic programs.

The above means that the plan has six major technical components:

- ❖ Discretionary spending caps to force budget discipline and impose significant cuts in both security and non-security spending by cutting low-priority programs and streamlining government operations, plus illustrative examples sufficient to save $200 billion in 2015.
- ❖ Tax reform which wipes out or restructures nearly all tax expenditures in order to dramatically lower corporate and individual tax rates and reduce the deficit at the same time.
- ❖ Concrete health care reforms which ask for greater contributions from doctors, lawyers, drug companies, and beneficiaries in the medium term, as well as a measure to put federal health spending in a global budget after 2020.
- ❖ Other savings from reforming the military and civilian retirement systems, reducing farm subsidies and other mandatory spending, along with a technical correction to provide more accurate indexing of all government programs and the tax code.
- ❖ Social Security reform which achieves 75-year sustainable solvency while reducing poverty by establishing a new minimum benefit equal to 125 percent of poverty in 2017 for a full career worker and providing a twenty year bump up in benefits for the old-old and long term disabled. We increased the eligibility age for full benefits to 68 by 2050 and 69 by 2075, with a hardship exemption for those who are in manual labor jobs who need to retire early, We also make progressive changes to the benefit formula and gradually increase the amount of wages subject to payroll taxes back to 90 percent of total wages.
- ❖ Tough budget process reforms to ensure the debt remains stable as a share of the economy.

Discretionary Spending

In order to bring down the deficit, Washington will have to rein in discretionary spending. Every aspect of the discretionary budget must be scrutinized, no agency can be off limits, and no program that spends too much or achieves too little can be spared. The federal government can and must adapt to the 21st century by transforming itself into a leaner and more efficient operation. Like its citizens, like the businesses that provide those citizens with jobs, like every state and local government, our federal government must also be willing to do more with less and live within its means.

Any serious attempt to reduce the deficit will require deliberate, planned reductions in both domestic and defense spending. The government will not be able to protect those in need or invest to achieve our nation's long-term potential growth if Washington squanders taxpayer dollars on duplicative or marginal programs with no measurable results.

The proposal we put forward would set limits for discretionary spending that would have a freeze in 2012, a 5 percent cut in 2013, followed by growth at about half inflation through 2020. We applied the same approach to security and non-security. We also required the President to propose limits on war spending consistent with the projected needs under current policies, with the spending levels in the CBO troop drawdown scenario as the starting point.

The Commission proposed locking in those savings by establishing strict, enforceable limits on all discretionary spending. In the 1990s, discretionary spending caps played a large role in bringing the budget into balance. By establishing formidable boundaries to guide spending in future years, Congress and the Administration will be forced to eliminate waste and excess in agency budgets, better target funding toward programs that demonstrate real results, and reduce duplication throughout the federal bureaucracy.

The Commission's proposal would create separate caps for security and non-security discretionary spending so that they would be treated the same. Firewalls ensure that both sides of the discretionary budget are subject to scrutiny and cuts so that neither party can avoid looking for savings in one side of the budget by cutting the other side deeper.

The spending path recommended by the Commission is more than simply numbers on a page. It is a vision for our future reflecting the values and priorities of the American people. We must continue to invest in our future, but must not undermine those investments by leaving generations yet to come with a debt they cannot repay. The Commission's spending limits will necessitate a more efficient government that invests wisely, spends Americans' precious tax dollars well, is transparent and accountable for every dime, and makes hard choices as to what government should and shouldn't do.

We put together an illustrative list of spending cuts totaling $200 billion in savings in 2015 to show how the savings required by the caps could be achieved without undermining our national security or jeopardizing investments in our future. We also recommended a "Cut and Invest" committee to identify low priority or duplicative programs that could be eliminated in order to free up funds for high priority investments. Last week the Government Accountability Office issued the report required by the Coburn Amendment identifying 34 areas of duplication, overlap or fragmented services where reforms could potentially save billions of tax dollars annually and help agencies provide more efficient and effective services. The report also identified another 47 areas where agencies or Congress could take action to either reduce the cost of government operations or enhance revenue collections for the Treasury. This report provides further evidence that Congress and agencies will be able to find cost savings in order to comply with spending limits while still meeting key priorities.

The Commission also recommended several reforms of discretionary spending to improve the transparency and accountability of spending. We proposed budgeting for disaster spending, placing greater restrictions on the use of emergency funds and establishing strict criteria for war supplementals. Finally we proposed making spending from transportation trust funds mandatory spending, limited to actual dedicated revenues collected by the trust fund in the prior year, and proposed a 15 cent increase in the gas tax to make the trust funds whole.

Comprehensive Tax Reform

America's tax code must be reformed. In the quarter century since the last comprehensive tax reform, Washington has riddled the system with countless tax expenditures, which are simply spending by another name. These tax earmarks – amounting to about $1.1 trillion a year of spending in the tax code – not only increase the deficit, but cause tax rates to be too high. Instead of promoting economic growth and competitiveness, our current code drives up health care costs and provides special treatment to special interests.

Rather than tinker around the edges of the existing tax code, the Commission proposed fundamental and comprehensive tax reform that would lower tax rates, reduce the deficit, simplify the tax code, reduce the tax gap, and make America the best place to start a business and create jobs.

The Commission proposed a "zero based budgeting" approach to tax reform of starting with a clean tax code that didn't have any tax expenditures and had much lower rates and then deciding which tax expenditures should be added back and which rates should be increase to pay for them. We estimated that if all tax expenditures were eliminated we could eliminate the Alternative Minimum Tax, bring individual income tax rates down to 8 percent, 14 percent, and 23 percent and reduce the corporate rate to 26 percent while achieving $80 billion in deficit reduction in 2015 and $160 billion in 2020

We realized that it would be impractical to completely eliminate all tax expenditures. However, we concluded that starting with a completely clean tax code and forcing advocates of various tax expenditures to justify why they should be added back and how the costs should be offset would result in a much simpler, efficient tax code than would be possible if we started with the status quo.

The Commission proposed establishing a fast track process for consideration of tax reform, with a tax expenditure haircut that would take effect beginning in 2012 if Congress failed to act. We said that tax reform must reduce the size and number of these tax expenditures, lower marginal tax rates for individuals and corporations and reduce the deficit while maintaining or increasing the progressivity of the tax code. The Commission members agreed that we need to protect the disadvantaged, so we started with the assumption that Congress would add back the EITC and the Child Tax Credit. The commission also agreed that tax reform should preserve some tax incentives to promote work, home ownership, charitable giving, retirement savings, etc. – but in a simplified and better targeted manner, while keeping the top marginal rate at or below 29 percent.

Although we decided that the precise details of tax reform and exact transition rules should be developed by the relevant congressional committees and the Treasury Department with expertise in the tax code, we produced a modified version of the “zero plan” that preserved certain tax expenditures in a modified form while still reducing rates and achieving deficit reduction. The illustrative plan developed by the commission demonstrated that it is possible both to reduce rates dramatically and to achieve significant deficit reduction if tax expenditures are eliminated or scaled back and better targeted. The illustrative plan would set rates at 12 percent, 22 percent, and 28 percent, create a 12 percent credit for mortgage interest and charitable giving, consolidates and limits the size of retirement accounts and gradually phase out the health exclusion, among other changes. The illustrative plan would preserve the EITC and child credit in their current form or an equivalent alternative. The result of this illustrative plan is a tax reform package that is more progressive than current law and achieves the deficit reduction targets in the Commission plan while dramatically reducing marginal tax rates.

The Commission also recommended corporate tax reform to make America the best place to start a business and create jobs. The current tax code saps the competitiveness of U.S. companies. Additionally, the tax code should help U.S.-based multinationals compete abroad in active foreign operations and in acquiring foreign businesses. The Commission recommended corporate tax reforms which would eliminate all tax expenditures for business, establishing a single corporate rate at the same level as the top individual tax rate (between 23 and 29 percent) and provides for a competitive territorial system, thus making America a globally competitive place to start and grow a business and attracting billions of dollars back to the country.

Health Care Cost Containment

Federal health care spending represents our single largest fiscal challenge over the long-run, and presented one of the biggest challenges for our Commission as well. There are very serious philosophical differences about the health care bill enacted last year that need to be debated, but the Commission wasn’t going to be able to resolve that debate. We decided it would be far more productive for us to discuss ways that we could build on the cost saving and cost control elements that were in the health care reform bill and look for other ways to achieve savings that were not included in the bill. Our proposal set out a few broad parameters to do that.

The Commission recommended reforming both the formula for physician payments (known as the Sustainable Growth Rate or SGR) and the Community Living and Support Services Act and finding savings throughout the health care system to offset their costs, with additional savings for deficit reduction. The Commission said that the cost of any "doc fix" – must be fully offset, and recommends enforcing this principle by eliminating its exemption in statutory PAYGO.

We proposed paying for the "doc fix" by asking doctors, other providers, lawyers and individuals to share responsibility for controlling costs. That means a doc fix that is a little less generous than what doctors have been receiving but one that provides a better system for paying doctors. It also means getting savings from drug companies and other providers beyond what was included in health reform, changing cost sharing rules to reduce overutilization of care and enacting medical malpractice reform.

We also called for repealing the CLASS Act – the Community Living And Support Services Act – unless reforms are enacted to make the program financially sustainable. Since the CLASS Act would actually bring revenues in over the next decade before starting to pay out benefits, we recommend additional health care savings of $76 billion to replace those revenues. In addition, we recommend additional reforms to reduce federal health spending and slow the growth of health care costs more broadly.

In total, the commission proposed over a dozen very specific policies to achieve savings in Medicare and Medicaid – totaling over $400 billion – in order to fully finance the "Doc Fix," pay for a potential repeal of the CLASS Act, and provide additional funds for deficit reduction.

Among the largest of these reforms is a very specific reform to Medicare cost sharing rules which calls for a "a single combined annual deductible of $550 … along with [a] 20 percent uniform coinsurance … [and] catastrophic protection for seniors by reducing the coinsurance rate to 5 percent after costs exceed $5,500 and capping total cost sharing at $7,500" and an equally specific restriction of MediGap. These two policies were estimated by CBO to save $110 billion over ten years.

In addition, the commission recommended comprehensive reforms of medical malpractice rules, extending Medicaid drug rebates to dual eligibles, reducing payments for graduate (and indirect) medical education, limiting the ability of States to manipulate their federal Medicaid matches by taxing providers, turning FEHB into a premium support program, and making a number of specific payment reforms and other changes.

The Commission also called for aggressive implementation of the demonstration projects in Medicare for new delivery systems and payment reforms that have potential for savings. In some instances CMS has the authority to expand the pilot projects if they are successful, in other areas Congress would need to act. We propose shifting the presumption toward going forward with reforms by requiring the Secretary to implement any pilot projects that have shown success in controlling costs without harming the quality of care by 2015, and we proposed expanding them to Medicaid and potentially into the exchanges. We also recommended elimination of the provider carve outs from IPAB, the Independent Payment Advisory Board to broaden the scope of payment reforms IPAB could implement.

Over the longer term (2020 and beyond), the Commission recommended setting targets for the total federal budgetary commitment to health care, limiting growth to one percent above GDP growth and requiring further structural reforms if federal health spending exceeds the program-specific and overall targets. We recognize that controlling federal health spending will be very difficult without reducing the growth of health care costs overall. To that end, the Commission's recommendations on tax reform regarding reducing and potentially eliminating the exclusion for employer-provided health insurance will help decrease growth in health care spending, according to virtually all health economists

If the recommendations made by the commission combined with the new policies enacted by Congress do not slow the rate of growth in the federal budgetary commitment to health care to the rate of GDP plus one percent, more drastic measures have to be considered, such as a premium support plan, increases in the age of eligibility for Medicare, block grants for Medicaid, a robust public option, an all payer system, or giving Medicare the authority to be a more active purchaser of health care services.

Mandatory Savings

Outside of health care and Social Security, the commission also applied scrutiny to other mandatory programs – programs which are not subject to the scrutiny of the annual appropriations process.

Our goal in this area was to reduce low priority or wasteful spending, including subsidies that are poorly targeted or create perverse incentives. We felt that income support programs for the most disadvantaged, such as unemployment compensation, food stamps, and Supplemental Security Income (SSI), should not be touched. These programs provide vital means of support for the disadvantaged, and the commission did not recommend any fundamental policy changes to these programs.

We identified approximately $225 billion in mandatory savings outside of Social Security, health care and safety net programs. Much of this came from reforms to the military and civil servant retirement systems. We heard time and time again that these defense and non-defense "entitlements" are draining money away from the fundamental priorities of government, and so recommended a number of innovations and cost-saving techniques to bring them more closely in line with similar retirement programs from the private sector.

In addition, we proposed reforms to student loan programs and the Pension Benefit Guarantee Corporation (PBGC) – both of which were included in the President's budget proposal. We also recommended reductions in agriculture subsidies, along with a large number of smaller cuts.

The Commission also recommended a technical change in indexing federal programs and tax provisions by adopting the "chain-weighted" Consumer Price Index for Urban Consumers (C-CPI-U) for all provisions that are currently indexed to CPI-U and CPI-W. The Commission did not propose a change in indexing of government programs, but simply recommended using a more accurate measure to implement current policy. This is a technical correction that experts from both sides of the aisle agree on, and the overestimation in the current CPI is something that is costing us a lot of money across the budget.

Social Security Reform

The most popular Social Security reform plan in Washington is the do-nothing plan – a plan which effectively recommends a 22 percent across-the-board benefit cut for all current and future beneficiaries in 2037. That is woefully unacceptable and easily preventable if we act now.

We wanted to make sure the system is sustainable over the long term – to make sure it can continue to provide the foundation for a secure retirement not just for old guys like us, but for our kids and our grandkids. That's why we have focused on 75-year sustainable solvency for Social Security.

Saving Social Security will require shared sacrifice. Those at the top will have to contribute the most, both through higher payroll taxes and lower-than-scheduled benefits. Middle income workers will also have to contribute, but can do so primarily by working a little longer, to the extent they are able. Those who are most vulnerable should actually receive additional protections, in order to make sure Social Security is fulfilling its fundamental mission to keep seniors out of poverty.

The plan developed by the Commission would achieve sustainable solvency – meaning we would continue to have balance in the 75th year – in a way that phases in changes quite gradually while providing greater poverty protections than current law and making the program more progressive. We did not propose reforms of Social Security to reduce the deficit; the Social Security plan would have very little impact on the budget in the near term and we did not count any of those effects in meeting our deficit reduction targets. Rather, we proposed reforms of Social Security to ensure that the program remains strong and financially viable for future generations and to meet our mandate of making recommendations to "meaningfully improv(ing) the long run fiscal outlook."

The Commission's Social Security plan had six basic elements:

First, the plan would index the retirement ages – both early and normal – to account for increases in life expectancy. Effectively, this means the retirement age (which is scheduled to reach 67 under current law in 2027) will reach 68 in about 2050 and 69 in about 2075, just after our grandchildren have retired. Even with this change, future retirees will spend more time in retirement receiving benefits than current beneficiaries. We address the concern for workers who truly can't continue to work past age 62 because of physical limitations by directing the Social Security Administration to establish a hardship exemption and setting aside money to accommodate such a provision.

Second, we made progressive changes in the benefit formula by creating an extra bendpoint at the 50^{th} percentile of wages. Under this change, by 2050, the Social Security replacement factors would go from 90 percent, 32 percent, and 15 percent under current law to 90 percent, 30 percent, 10 percent, and 5 percent. Even with our recommendations, nearly all retirees (including high earners) will receive higher benefits than retirees today do – even adjusted for inflation. So it is hard to talk about these as benefit cuts.

Third, we increased the amount of income subject to the payroll tax by gradually raising the "taxable maximum." In the 1980s, this taxable maximum was high enough to cover 90 percent of wages, but under current law it is projected to cover only 82.5 by the end of the decade. We proposed slightly speeding up the wage-indexed increases in the taxable maximum so that it would again cover 90 percent of wages by 2050.

Fourth, we also included newly hired state and local workers in the Social Security program after 2020. This would give affected workers stronger retirement security, and make the system more efficient; it also makes sense from an honest budgeting perspective, because the most likely outcome is that over time the federal government may be called on to aid ailing state systems.

We also switched the measure of inflation used to calculation cost of living adjustments (COLAs) from the CPI to the more accurate chained-CPI. This was a technical correction which we applied government-wide to a number of tax and spending provisions.

And finally, we provided new protections for vulnerable workers in two ways. First, we created a robust minimum benefit which would guarantee a base benefit equal to 125 percent of the poverty line for someone who had worked for 30 years, and would index that level to wages so it becomes more generous over time. In addition, we created a benefit bump up, equal to 5 percent of the average wage, for the very old and the long-time disabled.

Budget Enforcement

The Commission proposal included recommendations that would achieve enough savings to more than restore primary balance and stabilize the debt under current projections. However, members of the Commission thought that it is important for Congress and the President to remain vigilant to ensure the budget remains on a course to primary balance and a stable debt to GDP ratio. We therefore recommended an enforcement mechanism to ensure the budget achieves primary balance by 2015 and the debt is stabilized thereafter.

The Commission's proposal would require action by the President and Congress on budget stabilization legislation if the budget (excluding interest costs) is projected to be out of primary balance in 2015, or if the debt held by the public has not stabilized thereafter. The debt stabilization process would include fast-track procedures to facilitate changes in law necessary to protect the fiscal health of the federal budget.

Previous budget enforcement mechanisms that placed limits on the deficit failed because they attempted to use budget process as a substitute for the tough choices needed to reduce the deficit. By contrast, this proposal provides a failsafe ensuring the fiscal goals envisioned by the Commission's recommendations actually materialize in the future.

The debt stabilization process recommended by the Fiscal Commission reflects a new standard for the President and the Congress to react in a timely manner to fiscal imbalance. Requiring the President to provide detailed legislative changes in law with his budget, coupled by the enactment of the Congressional budget resolution with directives to committees of jurisdiction to act by a date certain, will provide accountability and transparency to the federal budget process

Lessons from Fiscal Commission

Our experience in the commission provided several lessons which should help policymakers grapple with the challenges they will face with their votes on the debt limit, with necessary appropriations to keep the government running, and with making the budget process work this year.

First, a fiscally responsible plan must be bold and comprehensive. It must restrain spending across the federal budget, reform the tax code, bring down health care costs, and make Social Security solvent and strong for the next 75 years and beyond.

A comprehensive approach is necessary not only to match the magnitude of the problem, but to allow for the tradeoffs and balance necessary to reach a bipartisan agreement. Our strong belief is that there would have been less support on the Commission for a less comprehensive plan that avoided making some of the politically sensitive and difficult choices we had to make to really bring the deficit down and eventually achieve balance. Commission members were willing to accept painful choices in parts of the budget that they cared about only if there were equally painful choices in other parts of the budget important to other members. Taking tax reform or Social Security off the table, for example, would have undermined prospects for agreement.

Second, Washington must lead the way. A realistic plan will require shared sacrifice by all but the most vulnerable in society. In order to ask for such sacrifices, we need to create a more efficient and cost-effective government, and root out waste wherever we find it.

Third, revenues need to be part of the solution, but as part of fundamental tax reform that moves beyond the zero sum argument about the Bush tax cuts that both parties have been fighting for and against over the last decade. The answer instead should focus on reforming revenues through a more efficient tax code that promotes economic growth. Today, we spend over $1.1 trillion a year on "tax expenditures" – credits, deductions, loopholes and exclusions which are really just spending by any other name. If we reform or eliminate these tax breaks, we can dramatically reduce personal and corporate tax rates, improve economic growth, and at the same time reduce the deficit.

Fourth, a plan to reduce the deficit must therefore promote economic growth and not undermine the economic recovery. In order to avoid shocking the fragile economy, the Commission recommended waiting until 2012 to begin enacting programmatic spending cuts, and waiting until fiscal year 2013 before making large nominal cuts. In addition, revenue changes would not begin until calendar year 2013, after spending cuts are already well underway.

A number of economists have argued that putting into place a credible plan to reduce future deficits can have a positive effect on the economy. This so-called "announcement effect" could help to prevent interest rate increases and also mitigate uncertainty among individuals and businesses. In addition, stabilizing the debt will improve the country's long-term growth prospects by reducing the "crowd out" of private investment and by forestalling a potential fiscal crisis.

Finally, and perhaps most importantly, reaching an agreement will require a serious effort on the part of the leaders in Congress and the administration to develop real trust and mutual respect. Building this trust and mutual respect is the critical first step in working together to reach a principled compromise that makes the tough, smart, fiscally responsible choices necessary to achieve real fiscal reform and responsibility. We are hopeful that the discussions being led by Vice President Biden with Congressional leaders in both parties over the appropriations for the remainder of the year will help develop that trust and can serve as a model for work on a broader fiscal package.

Conclusion

None of us likes every element of our plan, and each of us had to tolerate provisions we previously or presently oppose in order to reach a principled compromise. We were willing to put our differences aside to forge a plan because our nation will certainly be lost without one.

We surely do not pretend to have all the answers, and none of the commission members who voted for the plan supports every element of that plan. We fully expect there to be arguments that we went too far in some areas or not far enough in others. That is a debate Congress should have. All we ask is that the debate be guided by the "Becerra Rule" we followed in the Commission – "don't shoot down an idea without putting forward a better idea in its place."

In the weeks and months to come, countless advocacy groups and special interests will try mightily through expensive, dramatic, and heart-wrenching media assaults to exempt themselves from shared sacrifice and common purpose. The national interest, not special interests, must prevail. The nation desperately needs broad, bipartisan agreement based on shared sacrifice, not politics as usual. Americans are counting on us to put politics aside, pull together not pull apart, and agree on a plan to live within our means and make America strong for the long haul.

The political system, by its very nature, moves slowly and sloppily. But this country does not have a lot of time to act if it is to avert fiscal calamity. The American people must join us in demanding that the President and leaders of both parties in both Houses begin the honest negotiations needed to ensure enactment of a comprehensive bipartisan fiscal reform plan by year's end. The Fiscal Commission's plan can serve as the starting point; the ending point must be something equally ambitious, with broad support from both parties to ensure passage.

We believe neither party can fix this problem on its own, and both parties have a responsibility to do their part. The American people are a long way ahead of the political system in recognizing that now is the time to act. We believe that far from penalizing their leaders for making the tough choices, Americans will punish politicians for backing down – and well they should.

Thank you again for inviting us to appear today. We look forward to your questions.

SUMMARY OF COMMISSION RECOMMENDATIONS

Discretionary Spending Cuts

1.1: CAP DISCRETIONARY SPENDING THROUGH 2020. Hold spending in 2012 equal to or lower than spending in 2011, and return spending to pre-crisis 2008 levels in real terms in 2013. Limit future spending growth to half the projected inflation rate through 2020. *(Saves $183 billion in 2015, $1,760 billion through 2020)*

1.2: CUT BOTH SECURITY AND NON-SECURITY SPENDING. Establish firewall between the two categories through 2015, and require equal percentage cuts from both sides.

1.3: ENFORCE CAPS THROUGH TWO MECHANISMS -- POINT OF ORDER AND SEQUESTRATION. Require a separate non-amendable vote in House and 60-vote point of order in Senate to waive spending beyond the caps. Impose across-the-board sequester by the amount appropriations exceed the caps.

1.4: REQUIRE THE PRESIDENT TO PROPOSE ANNUAL LIMITS FOR WAR SPENDING. Create a separate category above the caps for Overseas Contingency Operations (OCO), proposed by the President to reflect the projected needs of war policy.

1.5: ESTABLISH A DISASTER FUND TO BUDGET HONESTLY FOR CATASTROPHES. *(Costs $11 billion per year, $99 billion through 2020)*

1.6: STOP THE ABUSE OF EMERGENCY SPENDING.

1.7: FULLY FUND THE TRANSPORTATION TRUST FUND INSTEAD OF RELYING ON DEFICIT SPENDING. Dedicate a 15-cent increase in the gas tax to transportation funding, and reduce spending to match the revenues the trust fund collects each year.

1.8: UNLEASH AGENCIES TO BEGIN IDENTIFYING SAVINGS.

1.9: ESTABLISH CUT-AND-INVEST COMMITTEE TO CUT LOW-PRIORITY SPENDING, INCREASE HIGH-PRIORITY INVESTMENT, AND CONSOLIDATE DUPLICATIVE FEDERAL PROGRAMS.

1.10: ADOPT IMMEDIATE REFORMS TO REDUCE SPENDING AND MAKE THE FEDERAL GOVERNMENT MORE EFFICIENT. *(Saves $50+ billion)*

- **1.10.1** Reduce Congressional & White House Budgets by 15 Percent ($0.8B)
- **1.10.2** Impose Three-Year Freeze on Member Pay
- **1.10.3** Impose Three-Year Pay Freeze on Federal Workers and Defense Department Civilians ($20.4B)
- **1.10.4** Reduce Size of the Federal Workforce Through Attrition ($13.2B)
- **1.10.5** Reduce Federal Travel, Printing, and Vehicle Budgets ($1.1B)
- **1.10.6** Sell Excess Federal Property ($0.1B)
- **1.10.7** Eliminate All Congressional Earmarks ($16B)

Tax Reform

2.1: ENACT FUNDAMENTAL TAX REFORM BY 2012 TO LOWER RATES, REDUCE DEFICITS, AND SIMPLIFY THE CODE. Eliminate all tax expenditures, dedicate a portion of the additional revenue to deficit reduction and use the remaining revenue to lower rates and add back necessary expenditures and credits.

> **2.1.1** Cut rates across the board, and reduce the top rate to between 25 and 29 percent.
> **2.1.2** Dedicate $80 billion to deficit reduction in 2015 and $180 billion in 2020.
> **2.1.3** Simplify key provisions to promote work, homes, health, charity, and savings while increasing or maintaining progressivity.

2.2: ENACT CORPORATE REFORM TO LOWER RATES, CLOSE LOOPHOLES, AND MOVE TO A TERRITORIAL SYSTEM.

> **2.2.1** Establish single corporate tax rate between 25% and 29%.
> **2.2.2** Eliminate all tax expenditures in the corporate code.
> **2.2.3** Move to a competitive territorial tax system.

2.3: PUT FAILSAFE IN PLACE TO ENSURE SWIFT PASSAGE OF TAX REFORM.

Health Care Savings

3.1: REFORM THE MEDICARE SUSTAINABLE GROWTH RATE. Reform Medicare Sustainable Growth Rate ("doc fix") for physicians and require the fix to be offset. *(Saves $3 billion in 2015, $22 billion through 2020, relative to a freeze)*

3.2: REFORM OR REPEAL THE CLASS ACT. *(Costs $11 billion in 2015, $76 billion through 2020)*

3.3: PAY FOR 'DOC FIX' AND CLASS ACT REFORM. Enact specific health savings to offset the costs of the Sustainable Growth Rate (SGR) fix and the lost receipts from repealing or reforming the CLASS Act.

> **3.3.1** Increase authority and funding to reduce Medicare fraud. *(Saves $1 billion in 2015, $9 billion through 2020)*
>
> **3.3.2** Reform Medicare cost-sharing rules. *(Saves $10 billion in 2015, $110 billion through 2020)*
>
> **3.3.3** Restrict first-dollar coverage in Medicare supplemental insurance. *(Medigap savings included in previous option, additional savings total $4 billion in 2015 and $38 billion through 2020)*
>
> **3.3.4** Extend Medicaid drug rebate to dual eligibles in Part D. *(Saves $7 billion in 2015, $49 billion through 2020)*
>
> **3.3.5** Reduce excess payments to hospitals for medical education. *(Saves $6 billion in 2015, $60 billion through 2020)*

3.3.6 Cut Medicare payments for bad debts. *(Saves $3 billion in 2015, $23 billion through 2020)*

3.3.7 Accelerate home health savings in ACA. *(Saves $2 billion in 2015, $9 billion through 2020)*

3.3.8 Eliminate state gaming of Medicaid tax gimmick. *(Saves $5 billion in 2015, $44 billion through 2020)*

3.3.9 Place dual eligibles in Medicaid managed care. *(Saves $1 billion in 2015, $12 billion through 2020)*

3.3.10 Reduce funding for Medicaid administrative costs. *(Saves less than $260 million in 2015, $2 billion through 2020)*

3.3.11 Medical malpractice reform. *(Saves $2 billion in 2015, $17 billion through 2020)*

3.3.12 Pilot premium support through FEHB. *(Saves $2 billion in 2015, $18 billion through 2020)*

3.4: AGGRESSIVELY IMPLEMENT AND EXPAND PAYMENT REFORM PILOTS. Direct CMS to design and begin implementation of Medicare payment reform pilots, demonstrations and programs as rapidly as possible and allow successful programs to be expanded without further Congressional action.

3.5: ELIMINATE PROVIDER CARVE OUTS IN IPAB. Give the Independent Payment Advisory Board (IPAB) authority to make recommendations regarding hospitals and other exempted providers.

3.5: ESTABLISH LONG-TERM GLOBAL BUDGET FOR TOTAL HEALTH CARE COSTS. Establish a global budget for total federal health care costs and limit the growth to GDP plus 1 percent.

Other Mandatory Savings

4.1: REVIEW AND REFORM FEDERAL WORKFORCE RETIREMENT PROGRAMS. Create a federal workforce entitlement task force to re-evaluate civil service and military health and retirement programs and recommend savings of $70 billion over ten years.

Use the highest five years of earnings to calculate civil service pension benefits for new retirees (CSRS and FERS) rather than highest three years prescribed under current law, to bring the benefit calculation in line with the private sector standard.
Savings in 2015: $500 million. Savings through 2020: $5 billion.

Defer COLA for retirees in the current system until age 62, including for civilian and military retirees who retire well before a conventional retirement age. In place of annual increases, provide a one-time catch-up adjustment at age 62 to increase the benefit to the amount that would have been payable had full COLAs been in effect.
Savings in 2015: $5 billion. Savings through 2020: $17 billion.

Adjust the ratio of employer/employee contributions to federal employee pension plans to equalize contributions.
Savings in 2015: $4 billion. Savings through 2020: $51 billion.

4.2: REDUCE AGRICULTURE PROGRAM SPENDING THROUGH 2020. Reduce net spending on mandatory agriculture programs by $10 billion from 2012 through 2020 with additional savings to fund an extension of the agriculture disaster fund and allow the Agriculture Committees to reallocate funds as necessary according to their priorities in the upcoming Farm Bill. *Savings in 2015: $1 billion. Savings through 2020: $10 billion.*

4.3: ELIMINATE IN-SCHOOL SUBSIDIES IN FEDERAL STUDENT LOAN PROGRAMS. Eliminate income-based subsidies for federal student loan borrowers in favor of better targeted hardship relief for loan repayment. *Savings in 2015: $5 billion. Savings through 2020: $43 billion.*

4.5: GIVE PENSION BENEFIT GUARANTEE BOARD AUTHORITY TO INCREASE PREMIUMS. *Savings in 2015: $2 billion. Savings through 2020: $16 billion.*

4.6: ELIMINATE PAYMENTS TO STATES FOR ABANDONED MINES.

4.7: EXTEND FCC SPECTRUM AUCTION AUTHORITY.

4.8: INDEX MANDATORY USER FEES TO INFLATION.

4.9: RESTRUCTURE THE POWER MARKETING ADMINISTRATIONS TO CHARGE MARKET RATES.

4.10: REQUIRE TENNESSEE VALLEY AUTHORITY TO IMPOSE TRANSMISSION SURCHARGE.

4.11: GIVE POST OFFICE GREATER MANAGEMENT AUTONOMY.

4.6-4.11 *Savings in 2015: $1 billion. Savings through 2020: $8 billion.*

Social Security Reform

5.1: MAKE RETIREMENT BENEFIT FORMULA MORE PROGRESSIVE. Modify the current three-bracket formula to a more progressive four-bracket formula, with changes phased in slowly. Change the current bend point factors of 90%|32%|15% to 90%|30%|10%|5% by 2050, with the new bend point added at median lifetime income.

5.2: REDUCE POVERTY BY PROVIDING AN ENHANCED MINIMUM BENEFIT FOR LOW-WAGE WORKERS. Create a new special minimum benefit that provides full career workers with a benefit no less than 125 percent of the poverty line in 2017 and indexed to wages thereafter.

5.3: ENHANCE BENEFITS FOR THE VERY OLD AND THE LONG-TIME DISABLED. Add a new "20-year benefit bump up" to protect those Social Security recipients who have potentially outlived their personal retirement resources.

5.4: GRADUALLY INCREASE EARLY AND FULL RETIREMENT AGES, BASED ON INCREASES IN LIFE EXPENCTANCY. After the Normal Retirement Age (NRA) reaches 67 in 2027 under current law, index both the NRA and Early Eligibility Age (EEA) to increases in life expectancy, effectively increasing the NRA to 68 by about 2050 and 69 by about 2075, and the EEA to 63 and 64 in lock step.

5.5: GIVE RETIREES MORE FLEXIBILITY IN CLAIMING BENEFITS AND CREATE A HARDSHIP EXEMPTION FOR THOSE WHO CANNOT WORK BEYOND 62. Allow Social Security beneficiaries to collect half of their benefits as early as age 62, and the other half at a later age. Also, direct the Social Security Administration to design a hardship exemption for those who cannot work past 62 but who do not qualify for disability benefits.

5.6: GRADUALLY INCREASE THE TAXABLE MAXIMUM TO COVER 90 PERCENT OF WAGES BY 2050.

5.7: ADOPT IMPROVED MEASURE OF CPI. Use the chained CPI, a more accurate measure of inflation, to calculate the Cost of Living Adjustment for Social Security beneficiaries.

5.8: COVER NEWLY HIRED STATE AND LOCAL WORKERS AFTER 2020. After 2020, mandate that all newly hired state and local workers be covered under Social Security, and require state and local pension plans to share data with Social Security.

5.9: DIRECT SSA TO BETTER INFORM FUTURE BENEFICIARIES ON RETIREMENT OPTIONS. Direct the Social Security Administration to improve information on retirement choices, better inform future beneficiaries on the financial implications of early retirement, and promote greater retirement savings.

Budget Process Reforms

6.1: SWITCH TO A MORE ACCURATE MEASURE OF INFLATION FOR INDEXED PROVISIONS. Rely on chained CPI to index all CPI-linked provisions across government.

6.2: ESTABLISH A DEBT STABILIZATION PROCESS TO ENFORCE DEFICIT REDUCTION TARGETS. Establish a debt stabilization process to provide a backstop to enforce savings and keep the federal budget on path to achieve long term targets.

6.3: GIVE THE PRESIDENT THE POWER OF EXPEDITED RESCISSION.

6.4: ALLOW CAP ADJUSTMENTS FOR PROGRAM INTEGRITY EFFORTS.

6.5: CONDUCT REVIEW OF BUDGET CONCEPTS TO MORE ACCURATELY REFLECT GOVERNMENT LIABILITIES.