

**SECRETARY OF DEFENSE LEON E. PANETTA  
DEFENSE BUDGET REQUEST – SUBMITTED STATEMENT  
SENATE BUDGET COMMITTEE  
TUESDAY, FEBRUARY 28, 2012**

Chairman Conrad, Senator Sessions, members of the committee. Thank you for the opportunity to appear before you to discuss the President's budget request for Fiscal Year 2013 (FY13) for the Department of Defense.

As a former Chairman of the House Budget Committee and Director of the Office of Management and Budget, I have a deep appreciation for the important role played by this committee in helping set the federal government's overall spending priorities. It is a tough job, but it is a critical responsibility, particularly given the significant challenges we are facing as a country. Our economy is still recovering from an historic recession. We are grappling with very large debt and deficits that over the long-term threaten our nation's fiscal solvency. Meanwhile, we remain a nation at war, and we are confronting a complex range of security challenges that threaten global stability and our homeland.

I recognize that there are vigorous debates in Washington about the proper role of government in confronting these challenges. But if there is consensus on one thing, it is that one of the fundamental duties of the federal government is to protect our national security. This is a responsibility for both political parties, and all branches of government. And I know that as members of Congress you take this duty as seriously as I do as Secretary of Defense.

In order to protect our national security, I believe that we must maintain the strongest military in the world, and I am committed to sustaining our military strength as Secretary of Defense. But that is not enough. Our national security also depends on strong diplomacy, it also requires strong intelligence efforts. Above all, protecting the nation requires a strong economy, fiscal discipline and effective government.

As someone with a lifetime of experience developing and implementing budgets, I do not believe that we must choose between fiscal discipline and national security. I believe we can maintain the strongest military in the world, and be part of a comprehensive solution to deficit reduction.

**Defense Strategy Review**

We were able to achieve that balance because the FY13 budget request for the Department of Defense was the product of an intensive strategy review conducted by the senior military and civilian leaders of the Department under the advice and guidance of President Obama. The reasons for this review are clear: first, the United States is at a strategic turning point after a decade of war and substantial growth in defense budgets. Second, given the size of our debt and deficits, Congress passed the Budget Control Act of 2011, imposing limits that led to a reduction in the defense base budget of \$487 billion over the next decade.

We at the Department decided that the fiscal situation presented us with the opportunity to establish a new strategy for the force of the future, and that strategy has guided us in making the decisions contained in the President's budget. These decisions reflect the fact that we are at an important turning point that would have required us to make a strategic shift under any circumstances. The U.S. military's mission in Iraq has ended. We still have a tough fight on our hands in Afghanistan, but 2011 marked significant progress in reducing violence and

transitioning to Afghan-led responsibility for security – and we are on track to complete that transition by the end of 2014, in accordance with our Lisbon commitments. Last year, the NATO effort in Libya also concluded with the fall of Qadhafi. And successful counterterrorism efforts have significantly weakened al-Qaeda and decimated its leadership.

But despite what we have been able to achieve, unlike past drawdowns when threats have receded, the United States still faces a complex array of security challenges across the globe: We are still a nation at war in Afghanistan; we still face threats from terrorism; there is dangerous proliferation of lethal weapons and materials; the behavior of Iran and North Korea threaten global stability; there is continuing turmoil and unrest in the Middle East; rising powers in Asia are testing international relationships; and there are growing concerns about cyber intrusions and attacks. Our job is to meet these challenges and at the same time, meet our responsibility to fiscal discipline. This is not an easy task, but is one that I believe is within our grasp if we all do our part for the American people.

To build the force we need for the future, we developed new strategic guidance that consists of five key elements:

- First, the military will be smaller and leaner, but it will be agile, flexible, ready and technologically advanced.
- Second, we will rebalance our global posture and presence to emphasize Asia-Pacific and the Middle East.
- Third, we will build innovative partnerships and strengthen key alliances and partnerships elsewhere in the world.
- Fourth, we will ensure that we can quickly confront and defeat aggression from any adversary – anytime, anywhere.
- Fifth, we will protect and prioritize key investments in technology and new capabilities, as well as our capacity to grow, adapt and mobilize as needed.

### **Strategy to FY13 Budget**

We developed this new strategic guidance before any final budget decisions were made to ensure that the budget choices reflected the new defense strategy.

While shaping this strategy, we did not want to repeat the mistakes of the past. Our goals were: to maintain the strongest military in the world, to not “hollow out” the force, to take a balanced approach to budget cuts, to put everything on the table, and to not break faith with troops and their families. Throughout the review we also made sure this was an inclusive process. General Dempsey and I worked closely with the leadership of the Services and Combatant Commanders, and consulted regularly with members of Congress.

As a result of these efforts, the Department is strongly united behind the President’s budget request for fiscal 2013, and the Future Years Defense Plan.

### **Defense Topline**

The President’s budget requests \$525.4 billion in FY13 for the base budget of the Department of Defense and \$88.5 billion to support the war efforts. In order to be consistent with Title I of the Budget Control Act, our FY13 base budget request had to be roughly \$45 billion less than we had anticipated it would be under last year’s budget plan. Over the next five years, defense spending under the FY13 budget will be \$259 billion less than we had planned for

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in the FY12 budget – a difference of nearly nine percent. Over the ten years starting in FY12, it will be reduced by \$487 billion. This represents a significant change to our defense spending plans, and in order to meet these new budget targets and our national security responsibilities, we had to fundamentally reshape our defense spending priorities, based on our new defense strategy.

Whereas under last year's budget we had planned for several years of modest real growth in the defense base budget, the \$525.4 billion base budget request for FY13 represents a decline of more than two percent over last year's enacted level in real dollar terms.

At the same time, we expect total defense spending, which includes war-related costs, to be reduced significantly over the next five years. Given the drawdown in Iraq and the ongoing transition in Afghanistan, funding requests for overseas contingency operations have already begun to decrease sharply. After adjustment for inflation, we expect total defense spending to be down by more than 20 percent, mostly because of the drop in war costs. This decline is roughly consistent with the size of the drawdowns after Vietnam and the Cold War – although we are determined to implement these reductions in a manner that avoids a hollow force and other mistakes of the past.

While the defense base budget will not be significantly reduced over the next five years – in fact, it will remain above 2008 levels after adjusting for inflation – the Department has historically required modest real growth in force structure and modernization accounts in order to maintain our force structure without hollowing out the force. That means that even with a defense base budget that is roughly flat in real dollar terms, we will have to get smaller in order to maintain a ready, agile, and deployable force.

I believe that this pattern of defense investment is both appropriate and sustainable within the overall federal budget. Spending on the defense base budget has increased by about 30 percent in real terms since 2001, and by fiscal 2013, it will make up 45 percent of all Federal discretionary budget authority. That said, the defense base budget will represent only 3.2 percent of GDP in 2013 – and as our economy continues to grow, we project that percentage will fall to 2.8 percent by 2017.

Ultimately, we need to base our investment in national defense not on numbers but on strategy, and a clear-eyed assessment of the risks and threats that exist to our national security. Given the complex and dangerous world we continue to inhabit, the President's proposal for spending on the defense base budget represents the investment we need to provide an adequate defense for the nation.

There is no doubt that our budget deficits are too high and that, as the economy recovers, we need to reduce deficits in order to strengthen our long-term economic outlook and protect our national security. The Department of Defense has stepped up to the plate with its share of the cuts needed to meet the original caps enacted under the Budget Control Act. But with these record deficits, no budget can be balanced on the back of discretionary spending alone.

Based on my own budget experience, I strongly believe that Congress and the Administration need to put all areas of the federal budget on the table and work together to achieve sufficient deficit reduction, in a balanced way, to avoid the sequester provisions contained in Title III of the Budget Control Act. Sequester would subject the Department to another roughly \$500 billion in additional cuts over the next nine years, and in FY13, these cuts would have to be implemented with limited flexibility. These changes could hollow out the force and inflict severe damage to our national defense and programs that are vital to our quality of life.

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I understand that sequester is designed to force the Congress to confront the hard choices that must be made in any serious effort to deal with the deficit. We all recognize what those hard choices are. They involve dealing with mandatory spending, which represent almost two-thirds of the federal budget, and additional revenues. It's a matter of simple arithmetic that discretionary spending, which accounts for only one-third of the federal budget, cannot be expected to contribute 100 percent to our deficit reduction efforts.

History has made clear that real deficit reduction only happens when everything is on the table – discretionary, mandatory spending, and revenues. That has been true for every major deficit reduction plan enacted by the Congress in recent history.

We still have time to avert sequestration, and the President's FY13 budget represents a path to doing so. The President's FY13 budget proposes a balanced plan to produce about \$4 trillion in savings, including the \$1.0 trillion in deficit reduction already generated by the Budget Control Act's discretionary caps. The President's plan would add mandatory savings and revenue increases to the already enacted discretionary cuts. If enacted, this proposal would provide a basis for halting sequestration, while ensuring the maintenance of a strong national defense.

### **Accommodating Defense Budget Cuts**

Let me turn now to the changes we made to accommodate the reductions required to be consistent with the Budget Control Act. I believe that these changes offer convincing evidence that we have made tough choices in the Department of Defense, and that we are doing our part to help achieve the national security imperative of deficit reduction while making decisions that fit within our overall defense strategy.

The \$259 billion in five year savings from defense that are part of this plan come from three broad areas:

- First, efficiencies – we redoubled efforts to make more disciplined use of taxpayer dollars, yielding about one quarter of the target savings;
- Second, force structure and procurement adjustments – we made strategy-driven changes in force structure and procurement programs, achieving roughly half of the savings;
- Finally, compensation – we made modest but important adjustments in personnel costs to achieve some necessary cost savings in this area, which represents one third of the budget but accounted for a little more than 10 percent of the total reduction.

The remaining reductions reflect economic changes and other shifts. Let me walk through these three areas, beginning with our efforts to discipline our use of defense dollars.

### **More Disciplined Use of Defense Dollars**

If we are to tighten up the force, I felt we have to begin by tightening up the operations of the Department. This budget continues efforts to reduce excess overhead, eliminate waste, and improve business practices across the department. The more savings realized in this area, the less spending reductions required for modernization programs, force structure, and military compensation.

As you know, the FY12 budget proposed more than \$150 billion in efficiencies between FY 2012 and FY 2016, and we continue to implement those changes. This budget identifies

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about \$60 billion in additional savings over five years. Across the military services, new efficiency efforts over the next five years include:

- The Army proposes to save \$18.6 billion through measures such as streamlining support functions, consolidating IT enterprise services, and rephasing military construction projects;
- The Navy proposes to save \$5.7 billion by implementing strategic sourcing of commodities and services, consolidating inventory, and other measures;
- The Air Force proposes to save \$6.6 billion by reducing service support contractors and rephasing military construction projects;

Other proposed DoD-wide efficiency savings over the next five years total \$30.1 billion, including reductions in expenses in the Office of the Secretary of Defense and the Defense Agencies.

As part of these initiatives, we are continuing the initiative to improve the Department's buying power by seeking greater efficiency and productivity in the acquisition of goods and services. We are strengthening acquisition support to the warfighter, executing acquisitions more efficiently, preserving the industrial base, and strengthening the acquisition workforce. This budget assumes that these policies produce savings of \$5.3 billion over the next five years.

In terms of military infrastructure, we will need to ensure that our current basing and infrastructure requirements do not divert resources from badly needed capabilities.

As we reduce force structure, we have a responsibility to provide the most cost efficient support for the force. For that reason, the President will request that Congress authorize the Base Realignment and Closure process for 2013 and 2015. As someone who went through BRAC, I realize how controversial this process can be for members and constituencies. And yet, it is the only effective way to achieve infrastructure savings.

Achieving audit readiness is another key initiative that will help the Department achieve greater discipline in its use of defense dollars. The Department needs auditable financial statements to comply with the law, to strengthen its own internal processes, and to reassure the public that it continues to be a good steward of federal funds. In October 2011, I directed the Department to emphasize this initiative and accelerate efforts to achieve fully auditable financial statements. Among other specific goals, I directed the Department achieve audit readiness of the Statement of Budgetary Resources for general funds by the end of calendar year 2014, and to meet the legal requirements to achieve full audit readiness for all Defense Department financial statements by 2017. We are also implementing a course-based certification program for defense financial managers in order to improve training in audit readiness and other areas, with pilot programs beginning this year. We now have a plan in place to meet these deadlines, including specific goals, financial resources, and a governance structure.

These are all critically important efforts to ensure the Department operates in the most efficient manner possible. Together, these initiatives will help ensure the Department can preserve funding for the force structure and modernization needed to support the missions of our force.

### **Strategy-driven Changes in Force Structure and Programs**

But it is obvious that efficiencies are not enough to achieve the required savings. Budget reductions of this magnitude require significant adjustments to force structure and procurement

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investments. The choices we made reflected five key elements of the defense strategic guidance and vision for the military.

### *1. Build a force that is smaller and leaner, but agile, flexible, ready and technologically advanced*

We knew that coming out of the wars, the military would be smaller. But to ensure an agile force, we made a conscious choice not to maintain more force structure than we could afford to properly train and equip. We are implementing force structure reductions consistent with the new strategic guidance for a total savings of about \$50 billion over the next five years.

These adjustments include:

- Gradually resizing the active Army to 490,000 soldiers;
- Gradually resizing the active Marine Corps to 182,100 Marines;
- Reducing and streamlining the Air Force's airlift fleet. The Air Force will maintain a fleet of 275 strategic airlifters and 318 C-130s – a fleet more than capable of meeting the airlift requirements of the new strategy. In addition, the Air Force will eliminate seven Tactical Air squadrons but retain a robust force of 54 combat-coded fighter squadrons, maintaining the capabilities and capacity needed to meet the new strategic guidance;
- The Navy will retire seven lower priority Navy cruisers that have not been upgraded with ballistic missile defense capability or that would require significant repairs, as well as two dock landing ships.

### *2. Rebalance global posture and presence to emphasize Asia-Pacific and the Middle East*

The strategic guidance made clear that we must protect capabilities needed to project power in Asia-Pacific and the Middle East. To this end, this budget:

- Maintains the current bomber fleet;
- Maintains the aircraft carrier fleet at a long-term level of 11 ships and 10 air wings;
- Maintains the big-deck amphibious fleet;
- Restores Army and Marine Corps force structure in the Pacific after the drawdown from Iraq and as we drawdown in Afghanistan, while maintaining a strong presence in the Middle East.

The budget also makes selected new investments to ensure we develop new capabilities needed to maintain our military's continued freedom of action in face of new challenges that could restrict our ability to project power in key territories and domains.

Other key power projection investments in FY13 include:

- \$300 million to fund the next generation Air Force bomber (and a total of \$6.3 billion over the next five years);
- \$1.8 billion to develop the new Air Force tanker;
- \$18.2 billion for the procurement of 10 new warships, including two Virginia-class submarines, two Aegis-class destroyers, four Littoral Combat Ships, one Joint High Speed Vessel, and one CVN-21-class aircraft carrier. We are also investing \$100 million to increase cruise missile capacity of future Virginia-class submarines;

*3. Build innovative partnerships and strengthen key alliances and partnerships*

The strategy makes clear that even though Asia-Pacific and the Middle East represent the areas of growing strategic priority, the United States will work to strengthen its key alliances, to build partnerships and to develop innovative ways such as rotational deployments to sustain U.S. presence elsewhere in the world.

To that end, this budget makes key investments in NATO and other partnership programs, including \$200 million in FY13 and nearly \$900 million over the next five years in the NATO Alliance Ground Surveillance system.

The new strategy also envisions a series of organizational changes that will boost efforts to partner with other militaries. These include allocating a U.S.-based brigade to the NATO Response Force and rotating U.S.-based units to Europe for training and exercises; and increasing opportunities for Special Operations Forces to advise and assist partners in other regions.

*4. Ensure that we can confront and defeat aggression from any adversary – anytime, anywhere*

This budget invests in space, cyberspace, long range precision-strike and the continued growth of special operations forces to ensure that we can still confront and defeat multiple adversaries even with the force structure reductions outlined earlier. It also sustains the nuclear triad of bombers, missiles and submarines to ensure we continue to have a safe, reliable and effective nuclear deterrent.

Even with some adjustments to force structure, this budget sustains a military that is the strongest in the world, capable of quickly and decisively confronting aggression wherever and whenever necessary. After planned reductions, the FY17 joint force will consist of:

- An Army of more than one million active and reserve soldiers with 18 Divisions, approximately 65 Brigade Combat Teams, 21 Combat Aviation Brigades and associated enablers.
- A Naval battle force of 285 ships – the same size force that we have today – that will remain the most powerful and flexible naval force on earth, able to prevail in any combat situation, including the most stressing anti-access environments. Our maritime forces will include 11 carriers, 9 large deck amphibious ships, 82 guided missile cruisers and destroyers, and 50 nuclear powered attack submarines.
- A Marine Corps with 31 infantry battalions, 10 artillery battalions and 20 tactical air squadrons.
- An Air Force that will continue to ensure air dominance with 54 combat coded fighter squadrons and the current bomber fleet. Our Air Force will also maintain a fleet of 275 strategic airlifters, 318 C-130s and a new aerial refueling tanker.

*5. Protect and prioritize key investments, and the capacity to grow, adapt and mobilize*

The force we are building will retain a decisive technological edge, leverage the lessons of recent conflicts and stay ahead of the most lethal and disruptive threats of the future.

To that end, the FY13 budget:

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- Provides \$11.9 billion for science and technology to preserve our ability to leap ahead, including \$2.1 billion for basic research.
- Provides \$10.4 billion (base and OCO) to sustain the continued growth in Special Operations Forces;
- Provides \$3.8 billion for Unmanned Air Systems. We slowed the buy of the Reaper aircraft to allow us time to develop the personnel and training infrastructure necessary to make full use of these important aircraft.
- Provides \$3.4 billion in cyber activities. We are investing in full spectrum cyber operations capabilities to address the threats we see today and in the future;

At the same time, the strategic guidance recognizes the need to prioritize and distinguish urgent modernization needs from those that can be delayed – particularly in light of schedule and cost problems. Therefore this budget identifies about \$75 billion in savings over five years resulting from canceled or restructured programs. Key modifications and associated savings over the next five years include:

- \$15.1 billion in savings from restructuring the Joint Strike Fighter by delaying aircraft purchases to allow more time for development and testing;
- \$13.1 billion by reducing investment in procurement of ships, while continuing to focus on the higher-capability vessels most needed to carry out our defense strategy;
- \$1.3 billion in savings from delaying development of the Army's Ground Combat Vehicle due to contracting difficulties;
- \$4.3 billion in savings from delaying the next generation of ballistic missile submarines by two years for affordability and management reasons;

We will also terminate selected programs, including:

- The Block 30 version of Global Hawk, which has grown in cost to the point where it is no longer cost effective, resulting in savings of \$2.5 billion; and
- The weather satellite program, because we can depend on existing satellites, resulting in savings of \$2.3 billion;

We have also invested in a balanced portfolio of capabilities that will enable our force to remain agile, flexible and technologically advanced enough to meet any threat. To that end, ground forces will retain the key enablers and know-how to conduct long-term stability operations, and the Army will retain more mid-grade officers and NCOs. These steps will ensure we have the structure and experienced leaders necessary should we need to re-grow the force quickly.

Another element is to maintain a capable and ready National Guard and Reserve. The Reserve Component has demonstrated its readiness and importance over the past ten years of war, and we must ensure that it remains available, trained, and equipped to serve in an operational capacity when necessary.

Another key part of preserving our ability to quickly adapt and mobilize is a strong and flexible industrial base. This budget recognizes that industry is our partner in the defense acquisition enterprise.

### **Ensuring Quality of the All-Volunteer Force**

Now to the most fundamental element of our strategy and our decision-making process: our people. This budget recognizes that they, far more than any weapons system or technology, are the great strength of our United States military. All told, the FY13 budget requests \$135.1

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billion for the pay and allowances of military personnel and \$8.5 billion for family support programs vital to the well-being of service members and their families.

One of the guiding principles in our decision making process was that we must keep faith with our troops and their families. For that reason, we were determined to protect family assistance programs, and we were able to sustain these important investments in this budget and continue efforts to make programs more responsive to the needs of troops and their families. Yet in order to build the force needed to defend the country under existing budget constraints, the growth in costs of military pay and benefits must be put on a sustainable course. This is an area of the budget that has grown by nearly 90 percent since 2001, or about 30 percent above inflation – while end strength has only grown by three percent.

This budget contains a roadmap to address the costs of military pay, health care, and retirement in ways that are fair, transparent, and consistent with our fundamental commitments to our people.

On military pay, there are no pay cuts. We have created sufficient room to allow for full pay raises in 2013 and 2014 that keep pace with increases in the private sector. However we will provide more limited pay raises beginning in 2015 – giving troops and their families fair notice and lead time before changes take effect. Let me be clear: nobody's pay is cut in this budget nor will anyone's pay be cut in the future years of this proposal.

This budget devotes \$48.7 billion to health care costs – an amount that has more than doubled over the last decade. In order to continue to control the growth of these costs, we are recommending increases in health care fees, co-pays and deductibles to be phased in over four to five years. None of the fee proposals in the budget would apply to active duty service members, and there will be no increases in health care fees or deductibles for families of active duty service members under this proposal. Those most affected will be retirees – with the greatest impact on working-age retirees under the age of 65 still likely to be employed in the civilian sector. Even with these changes, the costs borne by military retirees will remain below levels in most comparable private sector plans – as they should be.

Proposed changes include:

- Further increasing enrollment fees for retirees under age 65 in the TRICARE Prime program, using a tiered approach based on retired pay that requires senior-grade retirees with higher retired pay to pay more and junior-grade retirees less;
- Establishing a new enrollment fee for the TRICARE-for-Life program for retirees 65 and older, using a tiered approach;
- Implementing additional increases in pharmacy co-pays in a manner that increases incentives for use of mail order and generic medicine; and
- Indexing fees, deductibles, pharmacy co-pays, and catastrophic caps to reflect the growth in national health care costs.

We also feel that the fair way to address military retirement costs is to ask Congress to establish a commission with authority to conduct a comprehensive review of military retirement. But the President and the Department have made clear that the retirement benefits of those who currently serve must be protected by grandfathering their benefits. For those who serve today I will request there be no changes in retirement benefits.

## **A Balanced Package**

Members of the committee: putting together this balanced package has been a difficult undertaking and, at the same time, an important opportunity to shape the force we need for the future. I believe we have developed a complete package, aligned to achieve our strategic aims.

As a result, the FY13 request is a carefully balanced package that keeps America safe and sustains U.S. leadership abroad. As you take a look at the individual parts of this plan, I encourage you to do what the Department has done: to bear in mind the strategic trade-offs inherent in any particular budget decision, and the need to balance competing strategic objectives in a resource-constrained environment. The best example of this balancing act is the size of the budget itself, which in my view strikes the right balance between both the fiscal and security responsibilities of the Department to the nation.

But we will need your support and partnership to implement this vision of the future military. I understand how tough these issues can be, and that this is the beginning and not the end of this process. Make no mistake: the savings we are proposing will impact all 50 states. But it was this Congress that mandated, on a bi-partisan basis, that we significantly reduce discretionary funding, which realistically leads to substantial cuts in the defense budget. We need your partnership to do this in a manner that preserves the strongest military in the world. This will be a test of whether reducing the deficit is about talk or action.

My hope is that now that we see the sacrifice involved in reducing the defense budget by almost half a trillion dollars, Congress – and this Committee in particular – will be convinced of its important responsibility to make sure that we avoid sequestration.

The leadership of this department, both military and civilian, is united behind the strategy that we have presented, and this budget. Like all strategies and all defense budgets, there are risks associated with this spending plan. I cannot reduce the defense budget by almost half a trillion dollars and not incur additional risks. In our judgment these risks are acceptable, but nevertheless these additional risks do exist. Those risks primarily stem from the fact that we will be a smaller military. Will our forces be able to mobilize quickly enough to respond to crises? Will we be able to compensate with more advanced technology? Can we ensure the continued health of the all-volunteer force and meet our obligations to transitioning service members so they don't become part of the unemployment rolls?

We believe we can deal with these risks, and that the budget plan we have presented has an acceptable level of risk because it was developed base on our defense strategy. But there will be little room for error. If this Congress imposes more cuts in the defense budget, that will increase the risk and could make it impossible for us to execute the strategy we have developed. And if sequester is triggered, this strategy will certainly have to be thrown out the window and the result will be risks that are unacceptably high. So I really urge you to try to confront this issue and try to do everything you can to avoid that outcome, and to give us the opportunity to implement the strategy we have developed with the necessary and appropriate level of spending.

I look forward to working closely with you in the months ahead to do what the American people expect of their leaders: be fiscally responsible in developing the force for the future – a force that can defend the country, a force that supports our men and women in uniform, and a force that is, and always will be, the strongest military in the world.

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