NATIONAL PRESS CLUB

TAKING BACK OUR FISCAL FUTURE

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ISABEL SAWHILL: Good morning. I'm Belle (sp) Sawhill from Brookings and we – I want to welcome you on behalf not only of myself, but of the terrific team of people who put together the paper that we're releasing today. We're here to talk to you about our fiscal future and what we think needs to be done to get it under better control. And although the nominal sponsors of this event are Brookings and Heritage, I want to emphasize that a much broader group of institutions and people have been involved in this effort. And it may be that one of the more significant things about this paper is not just what it says, but who is saying it and what a diversity of people is saying it.

This paper, believe it or not, has 16 authors. You may ask, how in the world could 16 people co-author a paper? And let me tell you, it is difficult. But, of course, the true answer is that several people took the lead, particularly Alice Rivlin. Nevertheless, this was very much a group effort. These are not nominal co-signers to this document; this is a group of people that has been meeting for more than two years, every month, and talking about these issues and wondering what we might be able to do as a group to address the fiscal challenges facing the country.

I think at this point we probably shared at least 600 cups of coffee and an equal number of unhealthy muffins. And, of course, we have more of those this morning and hope you've had a chance to enjoy them. We found it very useful to listen to each other's views and to try to find common ground. We have our differences, of course, but we have found enough common ground to produce the set of ideas that we'll be talking about shortly.

But before we get to that, let me introduce this team. They're all up here in the front and I'm going to ask them to please stand up so you'll know who they are. I'm not going to try to introduce them individually. Their names are on the front page of the paper. So, please, I don't know what to call you all, maybe the sons and daughters of the fiscal revolution. (Laughter, applause.) A subset of us has also been going around the country as part of what we call the fiscal wakeup tour and we've discovered that the public is very undereducated on these issues, but that when they learn about them, they are eager to see their elected representatives take some action. And, as we all know, we haven't seen any action either from those who are already in elected office or from those who aspire to be.

So our purpose today, if I had to summarize it; is first to raise awareness of the issues, probably not necessary in this room; second, to debunk some common myths; third, to call on elected officials and the press to do more than they are currently doing; and, finally, to suggest some concrete steps that we all agree would help to move the country in the right direction. So, with that, let me turn this over to the co-organizer of this affair, Stuart Butler.

(Applause.)

STUART BUTLER: Thank you, Belle. As Belle said, I'm Stuart Butler from the Heritage Foundation and I want to say just a little bit more in terms of the introduction to our event here about how and why we came together on this. Certainly those of us from various organizations around Washington all looked at the same numbers and were very concerned about what we saw. We also were – are very concerned about the gridlock in Washington, the failure to deal with a problem which is gradually getting worse, as you can see actually on the charts that we have here.

But also a number of us – again, as Belle mentioned – have taken part in events outside of Washington, have gone outside the Beltway and actually talked to the American people. The fiscal wakeup tour that Belle referred to is jointly organized by the Concord Coalition, Heritage, the Brookings Institution, and the General Accountability Office, and Dave Walker, the now-former comptroller general of GAO took part in that. And we've been to over 30 cities.

We've talked intimately, really, to over 10,000 Americans right across the country and we learned a lot in that activity that has very much shaped the reason we came together and why we think these kinds of proposals really can take root in the political process and among the American people. I think we learned particularly four things: first, that Americans are indeed under-informed about the situation. And when they become informed, they're shocked and they want something done. They react fiercely to the notion that everybody in America, every man, woman, and child, has essentially $150,000 mortgage around their necks due to the unfunded obligations of the federal government. They want some action on that. So we feel that Americans need to be informed more. And you'll hear from Alice as she talks about the proposal, that a key part of this is to put front and center the actual situation so Americans can see it. And we think that will force action and demands for action by Congress.

Secondly, people make clear that they want bipartisanship. They want a bipartisan approach to dealing with this. And we, indeed, as a group represent people right across the spectrum. I'm sure we've probably in combination voted for every single possible candidate for president imaginable during the primary periods. And so, as a group, we do represent that cross-section. I think it also – we also show that people can come together across the spectrum and actually have a civilized discussion, come to some agreed conclusions about the situation, and actually explore some important ideas to move it forward. So I think we do that.

Thirdly, we found, like Ross Perot found, that, actually, if you go and talk to people and show them the situation, they are actually open to far more radical ideas than it customarily assumed to be possible here in Washington. And I think that those who might look at what we've proposed and say, this isn't feasible; Americans won't go along with it. I think that's wrong. I think we've shown that and I think that very much undergirds our approach. And then, finally, Americans here in Washington – Americans have shown us here in Washington that they see this as not primarily an economic issue. They see it as primarily a moral question, that it is wrong for Washington to continuously make promises that they're not making proper allocation to deal with or they're over-promising. And Americans feel that way very strongly and so we feel as a group we're not here just as policy wonks. We're not just here as Washington insiders and/or economists, but we are here because this is a moral question that American must face and that the Congress must face.

You'll now hear in a bit more detail the proposal itself from Alice Rivlin. She will summarize the main points of our document. Alice, as you may know and hopefully do know, was the first director of the Congressional Budget Office. And also we have three former Congressional Budget Office directors here on the panel to actually talk about this. She was also director of the Office of Management and Budget and was vice chairman of the Federal Reserve Board. So I'll ask Alice to come up and just outline the proposal.

(Applause.)

ALICE RIVLIN: Thank you, Stuart. Anyone might wonder what brought this disparate group of people together. And my answer is: sheer panic. (Laughter.) When the ship is headed straight for an iceberg, the crew just forgets their ideological differences and works together to avert the oncoming collision. You can choose your favorite metaphor – train wreck, whatever – but this group of budget folks sees a collision coming that the politicians are not focusing on or debating either in the election campaign or in the halls of Congress.

As a nation, for worthy and understandable reasons, we have made more promises under three major entitlement programs than we can afford to keep: Social Security, Medicare, and Medicaid. If current policies are not changed, we simply can't afford to keep these promises. Moreover, the Congress doesn't even have a decision process that will force them to consider this problem and what to do about it.

The entitlement programs, almost by definition, are on auto-pilot. These programs grow every year because of the increase in the number of people that are eligible for them and the rising cost of benefits, especially medical benefits. Now, this growth is not new, but we are entering a period in which demographic change will drive spending under these programs up especially fast. And far more important, there's this compounding factor, the rising cost of medical care, which shows no sign of abating.

We worry that this projected rapid growth in spending, if left on auto-pilot, will squeeze out other spending that we need to keep the economy growing, especially investment in the skills of young people, infrastructure, research and development, that it will lead to tax levels that will eventually undercut economic growth or that it will lead to deficits that will precipitate an economic crisis. Now, that's a passel of worries to choose from, but you could get all three.

Some other parts of the federal budget are also on auto-pilot, for example, big tax deductions and special tax benefits that narrow the tax base and often reward people who need them least; these aren't subject to regular review either. Neither are benefits like civilian and military retirement. But we focused on Social Security, Medicare, and Medicaid because they dominate the spending side of the budget looking forward. So we decided to focus on them first.

Now, I've spent a professional lifetime worrying about the federal budget and fiscal responsibility. And I've never been more worried than now. Like my colleagues, I believe the budget should be in balance most of the time, that we should be paying for the government services that we are using and not recklessly and selfishly passing the bill onto future taxpayers, our own children and grandchildren.

Back in the 1980s, we were struggling with big deficits in the budget in the range of 4 percent of GDP. It took a major change in the budget process in 1990, a bipartisan agreement between President Bush senior and the Democratic Congress and a strong bipartisan effort to close the gap and move the budget into surplus by the late '90s.

Now, I'm very proud of the part I played in that effort, but even as we struggled with those large current deficits, we knew that worse was yet to come. We knew that the combination of the baby-boom bulge, increasing longevity, and rising healthcare costs would put enormous upward pressure on federal spending in this century. But way back in the '90s, it was easy to think that this century was a long way off.

But it isn't a long way off now. Here we are. And these forces are already impacting the federal budget and will gather momentum rapidly over the next couple of decades. The first boomers are drawing Social Security this year and the avalanche is yet to come. But that's just part of the problem and, actually, it's a rather small part of the problem. These seniors are now eligible for Medicare and Medicaid and spending on those programs will rise much faster than Social Security and than other spending.

Medical spending for everyone in the country has been going up 2.5 percent faster than the GDP for 40 years. The federal programs tend to rise at the same rate as other medical spending for the obvious reason that people who are sick get roughly the same treatment for the same diagnosis no matter what kind of insurance they have. If one projects past trends forward, it is clear that the federal budget is on an unsustainable track. The cost of the promises, mostly made to older people under these three programs, will rise much faster than other spending, faster than federal revenues at any feasible set of tax rates. The deficits that would result cannot be financed even if patient oil minions and Asian banks keep on lending us money for a while.

What to do? Well, we can raise tax rates to unprecedented levels and keep raising them? Well, not likely. We can cut other programs, but we'd have to cut them to zero. We can keep borrowing until our creditors won't lend us anymore and then face the music. None of those options are attractive.

Now, clearly, some compromise plan is in order. Members of our group would give different weights to different parts of the solution, different mixes of spending cuts, revenue increases, and borrowing. But the thing that struck us hardest as we talked about alternatives – and we did talk about substantive alternatives a lot – was that the Congress really has no way of engaging this question head-on. The annual budget and appropriations process, for all its faults, does force decisions on the level of spending for discretionary programs. If Congress and the administration can't reach agreement, the government shuts down. We tried that a few times and we know the public hates it and for good reasons.

But there's nothing in the normal process that forces Congress to focus on the future of the big entitlement programs and put them on a sustainable track and nothing that forces consideration of tradeoffs with other parts of the budget. So it seemed to us that the first order of business, even before we talk about the substantive changes, was to get these programs off auto-pilot and onto a regular decision process that forces Congress to look seriously at projections of spending and resources and make tradeoffs.

How to do that? Well, we agreed that it didn't make sense to throw the entitlements into the annual budget process. Beneficiaries need more certainty than that and Congress couldn't handle the workload of reconsidering entitlements every year. So we propose the following rules:

First, Congress should enact – Congress and the president – should enact explicit long-term budgets – at least 30 years – for Medicare, Medicaid, and Social Security and be required to review them every five years. The three major entitlement programs could be budgeted for a longer period, but they would have to be subjected to review every five years. These five-year reviews would allow reconsideration of the tradeoffs between entitlement spending and other purposes and might cause adjustments in the benefits or the taxes or both.

Now, what's to make that really happen? The rules for the five-year review must include a trigger or an action-forcing device that requires explicit decisions when projected spending exceeds the budgeted amounts. The trigger might involve automatic benefit cuts or revenue increases including premium increases that could only be overridden by an explicit vote or enactment of alternative policies that would achieve budget outcomes similar to the automatic adjustment.

Alternatively, the trigger process could include requiring that a commission make recommendations for closing the gap, make recommendations to the president and to the Congress on which an up or down vote must be held. The trigger process would force an explicit vote when long-run budgets for any of these programs is exceeded and it will dramatize the importance of modernizing these entitlement programs to reflect longevity, higher incomes, and the rising cost of medical care.

If the public wants the increasingly expensive health benefits provided by Medicare and Medicaid because they judge them to be well worth the cost, the taxes will have to be raised commensurately. And, third, the long-run costs of these three programs should be visible in the budget at all times, which they are not now, and considered when decisions are made. Benefits should not be adjusted either at the five-year review period or in between without ensuring that any increase in benefit cost could be fully financed. In other words, we wouldn't have the Medicare prescription drug benefit if we had that process now or then.

This is a process idea. Getting the decision process right is just the beginning, but it can be very important. We believe that the process rules adopted in 1990, the discretionary caps and pay-go, played a crucial role in returning the budget to surplus in the late 1990s. We have plenty of substantive ideas about how to restructure these programs and the revenues to pay for them, but we think the first thing to do is for the Congress to adopt a budget process that forces them to make choices about the major entitlement programs on a periodic basis.

We haven't got the answer to all of the details like which committees would do what and how the triggers would actually be structured, but we think that the basic point is so important and the fact that a group of budget-worriers with such a broad spectrum of viewpoints could agree on it is so striking that we should bring it forward for discussion before we had all of the detailed answers. We're hoping to start a conversation. If you don't like our proposal, tell us what you think should be done because continuing the status quo is simply not an option. Thank you.

(Applause.)

MS. SAWHILL: Thank you, Alice. We are next going to hear from Bob Reischauer and then from Rudy Penner, both of whom are members of the group and also former directors of CBO. So I do want to fill in a gap that I left earlier when Stuart and I were talking about the fiscal wakeup tour because, as part of this public education campaign that Stuart talked about, one of our other partners' public agenda is viewpoint learning and I see one of our colleagues from that group, Andy Arrow (ph), back there. So I just wanted to acknowledge that they have been a big help and an important partner in this public education effort. Bob –

ROBERT REISCHAUER: Thank you, Belle. This might answer the question of what do former CBO directors who are not advising presidential candidates do with their time – (laughter) – and drink stale coffee and eat bad buns and come up with ideas like this. (Laughter.)

My assignment here is to elaborate a bit on why reforms like this are needed and, in fact, should be welcomed by policymakers in both parties. After all, this is not an issue that just the budget wonks are concerned about. And overwhelming majority of elected policymakers, policymakers in both parties, are well aware that the nation is on an unsustainable fiscal path that without fundamental changes in our tax policy and our spending policy, deficits are going to grow from the rather benign levels that we've experienced in the last couple of years to levels that this nation has not experienced in peacetime.

Policymakers also understand the consequences of inaction. They know that if we allow the deficits to mount to these unprecedented levels, they will threaten both the standard of living that we've enjoyed and our standing in the world. At a minimum, we will risk economic stagnation. More likely, we will risk ceding our economic sovereignty to creditor nations and exposing ourselves to serious economic instability.

There's also widespread agreement among elected officials that the longer we delay addressing this challenge, the more wrenching and politically difficult the unavoidable adjustments will have to be and the more constrained will be the set of options that we have available to deal with the problem. If we act soon, the timing and the nature of the adjustments will be in our hands. If we wait until events force change, our flexibility will be greatly reduced.

Notwithstanding the general understanding of the problem among policymakers, the consequences of it, and the range of solutions that we have available, the fact of the matter is that our elected officials have been unable or unwilling to step up to the plate. Why is this the case? Some argue that the necessary presidential leadership is lacking; what we need is the president to, you know, gird his loins and get in there. Others believe that the major impediment is the political polarization of the Congress, that bipartisan cooperation of the sort that is essential for grappling with difficult issues that involve fiscal restraint and redistribution has gone the way of the black and white television or smoking on airplanes.

Still others argue that what is needed is a public that fully appreciate the seriousness of the problem and the nature of the solutions. After all, what the public sees and feels doesn't look like an immediate crisis. Recent deficits have not been huge by the standards of recent years. In fact, the deficit last year was a mere shadow of what it was in the mid-'80s or the early '90s. Moreover, until the last nine months, the economy has been relatively healthy: relatively low unemployment, acceptable levels of inflation, modest growth, and a healthy increase in home prices. Why worry?

While it may be necessary to have stronger presidential leadership and a spirit of bipartisan cooperation in Congress and more education among the public, in my opinion, these ingredients would not be sufficient to assure that the Congress and the president would deal with the issue that faces this country. The basic reason for my pessimism lies in the fact that there's no real incentive for elected officials to act to improve the long-run fiscal situation and, in fact, there exist strong disincentives to acting.

The problem, after all, is distance and the consequences of inaction are both uncertain and diffuse. On the other hand, the solutions, unavoidably, are painful, they're more immediate, and they're more specific. Moreover, there appears to be no reason to act now as opposed to next year or the year after or the year after. As I said before, deficits are likely to stay well within the range of those experienced during the last four decades. And the real manifestations of our fiscal irresponsibility will not be apparent for a number of years, the distant future, which of course in Washington means two or four or six years from now. And today's decision makers are unlikely to be held accountable for whatever consequences there might be.

It's not surprising that many feel that without clear and convincing evidence that growing deficits will do irreparable harm to the economy and undermine our living standards that it would be political suicide to advocate significant spending restraint or tax increases, even if that restraint were enacted now but implemented many years later as occurred with some of the reforms that were adopted in 1983 with the Social Security reforms.

If you remember that period, we called for an increase in the normal age of retirement, but it didn't go into effect until 17 years later. Republicans look back at 1990 when George Herbert Walker Bush agreed to a multi-year deficit reduction package and was not reelected. Democrats remember 1993 when Clinton's multi-year deficit reduction package, they believe, contributed to their loss of control of the Congress.

Fearing opponents who will argue that sacrifice isn't necessary, that faster economic growth would reduce government fraud and abuse, and elimination of unspecified low-priority programs or earmarks is enough to do the job, few sitting officials are willing to step up to the plate. Moreover, when the circumstances require specific proposals, both the president and congressional leaders feel perfectly comfortable putting forward policies that on paper solve the problem but they know are unacceptable to the other party. And no effort is made to seek compromise because there is no need to.

What we have proposed represents an effort to change this situation. It attempts to change the incentives in a way that would increase the chances the Congress and the president would take steps not just to reduce the dangerous imbalance that is likely to develop between revenues and spending, but also to provide some fiscal flexibility that we need if we're going to address the emerging priorities that face this nation. The proposal we've put together represents a modest change in the budget process that would ensure that elected officials would periodically have to consider the issue, periodically have to take some actions, or allow predetermined adjustments to go into effect, or – and we should make this clear – go on record saying that the road to fiscal insolvency is the desirable path for this nation to follow.

This proposal in some ways is a kissing cousin of the discretionary spending caps and the PAYGO procedures that were first enacted in the 1990 Budget Enforcement Act. They were modestly successful because they were designed, as this one is, to enforce deficit reduction policies that are already been agreed to. No one in this group is naïve. We all have a healthy dose of cynicism coursing through our veins. We all recognize that one can't force the Congress or the president to do that which they don't want to do or that which they consider to be an act of political suicide.

What this proposal does do is encourage the Congress and the president to consider the long term in a more realistic way, make the political costs of inaction higher, and provide a degree of political cover for difficult decisions. It's not so radical that it represents an unfamiliar change because, as I said, it has roots in the Budget Enforcement Act; nor is it unworkable as the Gramm-Rudman-Hollings procedures were. It is a mechanism that we think represents a realistic first step towards putting our fiscal house in order. Thank you.

(Applause.)

RUDOLPH PENNER: Thank you. Well, an important component of our proposal is the notion of an automatic trigger mechanism that it bring some discipline to the process. And I get the wonkish task of trying to explain how that might work. Gene Steuerle and I have written at length about this; and you can find more details than you'd ever want to know probably in the bibliography.

But the basic idea is pretty simple. You select some variable that's an indicator of the financial health of a program or a set of programs. And if that indicator suggests financial weakness, some action is taken automatically. We budgeters differentiate soft triggers where the action sets in motion a process – for example, may force the president to make some proposals and the Congress to act on them expeditiously. We differentiate that from hard triggers where some change in policy happens automatically.

While this group has no detailed design for the trigger, just as an example, you might think of triggering an increase in the full retirement age in Social Security or an automatic increase in the payroll-wage base, or a dozen other things that would restrain the program. This group, I think, leans toward a hard trigger, but also contemplates the possibility of softer triggers.

Now, this isn't a new idea. This group isn't real original, after all. Triggers can be found in the budget processes of a lot of democracies. Most notably, hard triggers have been adopted as an integral part of fundamental social security reform in Sweden, Italy, Canada, Germany, and Japan. And you can find modest triggers scattered throughout our own budget process.

The most important point to make about triggers is that it's very difficult, indeed perhaps impossible, to design one that would lead to a completely rational policy outcome if the trigger was pulled year after year after year. And we wouldn't expect a trigger to keep altering policy for a very long period. But in the short run, the existence of the trigger changes the default from a path where policy is unsustainable to one where policy is more constrained. Perhaps not made totally sustainable – that depends on the design of the trigger – but certainly one that would be superior to current law.

Second, if the Congress does not like the policy path resulting from the trigger, they can change it by passing a new law. And we would expect this to be the usual outcome after a number of years. And we have no illusions about this. They may totally waive the trigger and go back to the original unsustainable path. But if they do that, they'll be doing it explicitly. And that is a really important point here. We don't want to stay with this automatic pilot. If we're going to do bad things, let's vote to do them.

But one hopes to avoid that kind of outcome and one can reduce the probability of it happening by carefully designing the trigger. There are two crucial related design issues. First, what variable should be used as the trigger? What pulls it? And then, what action should result once the trigger is pulled?

On the first, you don't want to use a variable that is erratic and hard to predict so that the trigger goes on and off surprisingly. The budget deficit is a bad trigger because it jumps all over the place; it's hard to predict; and economic conditions and other factors push it around violently. It was the trigger in what might be called the mother of all trigger laws; that is to say, Gramm-Rudman-Hollings, passed in 1985. That law specified targets for the budget deficit. And if the target was not achieved, spending was to be cut sufficiently using an automatic formula to bring the deficit in line with the target.

Unfortunately, deficits turned out to be considerably higher for economic reasons than envisioned when the law was passed. And the required spending cuts were too large to be thinkable politically. The deficit targets were first raised and then abandoned altogether.

So one might say that trigger failed miserably. But in a sense, it led to just the kind of outcome desired by this committee. The president and Congress didn't feel that they could totally abandon the law. Alice talked about the fact that this in turn led to the negotiation of the 1990 budget agreement, a huge bipartisan deficit reduction package consisting of both tax increases and spending restraints. And Bob noted that that agreement was protected by the Budget Enforcement Act that contained the pay-as-you-go rules and the discretionary spending caps that were partially – and I emphasize the word partially – responsible for moving to surpluses in the late '90s.

Nevertheless, it would certainly be preferable to choose a target that is more stable than the annual deficit. Again, this group has not designed that in detail, but just as an example, Gene and I suggested in Social Security looking at the declaration of an actuarial deficit by the trustees. Or you could base triggers in Medicare on the rate of growth of spending.

The more difficult design question involves the type of action that is triggered. Ideally, it would be significant enough to make a difference to the financial health of a program and painful enough to induce the Congress to choose some more rational alternative. But it can't be so painful that it makes it look as though the Congress is doing the public a big favor if it is waived entirely. And the latter problem afflicts one of the triggers we have in our budget process, the so-called sustainability factor that would automatically cut physician fees to improve the financial health of Medicare. It is too harsh. There wouldn't be any physicians around to serve Medicare if it were to go into effect. So Congress routinely waives it.

Well, the $64-trillion-dollar question is why on earth would Congress adopt such a trigger mechanism? Well, first it has been adopted in other democracies. Second, they have adopted it in the past: a very severe one with Gramm-Rudman-Hollings. And there really are a lot of triggers that I can't describe in detail scattered through our budget process.

The basic point of a trigger is that it provides one layer of political insulation. If the trigger is pulled and spending is restrained or taxes raised, it happens by immaculate conception. It doesn't require an explicit vote. If the Congress chooses to substitute a more rational action in place of the trigger, they appear to be dong the public a favor rather than hurting them by just cutting programs or raising taxes. So all we can hope for is that the Congress sees the great wisdom of our proposal. Thank you very much.

(Applause.)

MR. BUTLER: We'd like to take your questions now. If you could direct them to one of the speakers or to us, then we might invite some of the others of our group also to answer them. Yeah, I see one over there.

Q: This question is for Stuart Butler. So do I understand from this presentation that the Heritage Foundation is endorsing a proposal here that would include, among other things, triggers for an automatic tax increase?

MR. BUTLER: No, you don't understand it. (Laughter.) First of all, we're here as individuals. And secondly, what we're actually proposing is a process to require decisions to be made. And those decisions would include a trigger and the notion of what should be in that trigger should be open to debate. I would certainly oppose one that would involve a tax increase. On the other hand, I think ones that involve premium changes, for example, so that people pay the full amount, the full freight of things like the Medicare drug benefit, would be an example of something that I personally would support and have done in the past.

So I think it's very important to recognize what we're talking about here is a proposal designed to force decision making, to force a debate that is not taking place. And as you well know, with that debate not being forced right now, what we are seeing is both steady increases in taxes – as we'll see over there – and steady increases in spending and steady increases in deficits. And all of us are committed to getting off that track, which leads us to disaster in the future.

MS. SAWHILL: Is there anybody amongst the front row here who participated in the creation of this proposal that would like to add anything to what's been said so far? I just want to give them a chance to come in if they'd like to. Maybe they want to wait. Okay, they want to wait.

MR. BUTLER: There's a question over here. There's a microphone too.

Q: Thank you. Hi, my name is Liz Chimienti. I'm with the Center for Economic and Policy Research. I think this may be on your chart but my vision isn't that good. Dr. Reischauer mentioned that we've never seen deficits of this proportion in peacetime. We aren't in peacetime right now. I was wondering what percentage of the coming deficits are related to the wars in Iraq and Afghanistan? Thank you.

MS. RIVLIN: Not much is the answer. The defense budget is now about 4 percent of GDP. And in the normal projections, people assume the Iraq war is eventually over and the defense budget goes forward at something like 4 percent of GDP. It might go back to the pre-war level, which was 3-point-something. But the defense budget is not a big part of the problem. And I think that's one of the myths that people think of.

We're spending a lot of money on defense; 4 percent of GDP is a lot; it's as much as Social Security. But nobody expects the defense budget to grow in the future. The things that grow are especially Medicare and Medicaid, but also Social Security.

ME. BUTLER: Yes?

Q: Wasn't the 1983 Social Security reform supposed to protect Social Security for longer than this? It's especially important since the three-legged stool of retirement includes pensions, which are far less secure than they used to be, and savings, which is difficult when you have very low rates of return – 2 percent, 4 percent. I mean, that's what CDs are getting now and the market may not be as reliable – I mean, there may be a bubble in the market too.

MR. BUTLER: Alice, do you want to respond to that too?

MR. PENNER: I can discuss that. The 1983 reforms tried to make the process secure for 75 years. So very obviously, we're 24 years beyond that again. And it didn't quite work out as expected. But even if it had, we would be seeing Social Security deficits. Indeed, every time the trustees do their 75-year projections, you add one year of very big deficits and subtract now a year of surpluses, so that tends to make the situation worse and worse.

In terms of the detailed role that Social Security should play in our society, one could talk about not a very long time. But one of the crucial questions, I think, is detailed role for who. Should affluent people like me and my wife be getting over 30,000 (dollars) a year from Social Security benefits? We're not giving it back; we love it; and we thank you taxpayers for it. But it is a very strange kind of program, I think you have to admit. So I don't want to get into a whole long discussion of reforms, but clearly reforms are warranted. And the degree to which they occur on the tax or the benefit side, this group has not taken a definite position on that.

MR. BUTLER: The gentleman here?

Q: I think the trigger is a great idea. I remember when we passed an automatic means-tested component of Medicare, and people pounded on Rostenkowski's car, and everybody fled the exit to – (inaudible) – got to be something of the kind – (inaudible). My question is this. This has been a bit antiseptic and the panel has been very moderate about the out-year. But I'd like someone to sketch, if they would, the scenario that could occur if the foreign borrowing gets to a point where people are not willing to hold dollar-denominated debt anymore. What are some of the feedback, kickback scenarios that could start unfolding in terms of impact on our economy and this multiple reverberations?

MR. BUTLER: Maybe I should ask Alice to respond to that. But before you do, I just would mention - you mentioned Rostenkowski as a good example, I think, of when a new entitlement was proposed with an actual price tag to it, where people were required, expected to pay the full. And there was reaction against that. And I think that's one of the things we really want to focus on here, making clear what the long-term budget is and what the long-term expectations are for people to force changes. But anyway, let's – were you going to respond to that?

MS. RIVLIN: I think we should also say that the questioner didn't identify himself. This is Jim Moody, former member of Congress. I think we're getting a flavor of the disaster now as the dollar falls because that's partly because capital isn't flowing into the U.S. as much as it was. But we're still able to sell our bonds. And we sell them – at least half of them – to other countries. And if those other countries lose faith in the U.S. dollar, they're going to stop buying bonds. They don't even have to dump them. If they dump them, it would be worse. But if they stop buying them at the rates that they have, we can see the dollar plummeting, a big spike in interest rates, and a serious recession in the United States.

Now, nobody really wants that to happen, not our foreign creditor or us. So with any good luck, we can work through this without that happening. But the disaster scenarios are certainly there.

Some of us have worried that without a disaster, we won't have the political will to do anything about this. It will have the situation of what we sometimes call termites in the woodwork, slowly eroding our strength as a nation as opposed to the house being blown down. I'm an advocate of a mini-crisis.

(Laughter.)

MR. BUTLER: There was a question over here.

Q: Thank you for taking my question. I am – (inaudible) – from the federal government. Could you please elaborate more on the impact on current and future economic and national security of having as creditors countries that are not traditionally our allies and what we can do about it now? Thank you.

MR. BUTLER: Do one of you want to take that? Bob, do you want it?

MR. REISCHAUER: I think that really goes well beyond the purview of this commission. But just to follow onto the previous answers to Jim's question, we're right now dependent of inflows of resources from countries that do not have longstanding relationships with the United States. It used to be a time when Europeans, British in particular, were our major creditors. Now, it's China, Japan, maybe some countries in the Middle East. And they dynamic there is a business dynamic. And when it no longer serves their national interest to buy dollar-denominated assets, we're going to have to go through a serious and painful adjustment.

And what it means is that as Alice said, interest rates will rise. We will have to as a nation save more than we have been saving so that our savers can purchase our government-issued securities. And if that adjustment takes place too rapidly, obviously, as we save more, we consume less. And there then is a downturn in the economy. And there's not much we can do in that kind of circumstance. Tax cuts? Fine, but when you've got taxes you have to borrow more money and therefore save more as a nation.

MS. RIVLIN: It just makes us more vulnerable.

MR. BUTLER: The gentleman back here.

Q: My name is David Auckster (ph) of the Research Institute for Independent Living. And in the conclusions of the paper, you indicated there is going to be pain. And my question is, who is going to suffer this pain and what's the magnitude of the pain?

MR. BUTLER: I might just respond first by saying that is something that very much comes up in our events outside of Washington when you have people in the audience who are young and people in the audience who are older. And these very issues come up. And what we're doing in showing this in the proposals we have is to make explicit what the scope of the problem is and the burden is, and to then provoke a real discussion about where that should lie.

I think a lot of people, including elderly people, feel very strongly that this is not something – this pain is not something that should be simply put off to our children and particularly our grandchildren, that it should be discussed honestly and openly, and that is exactly what this proposal is intended to force: both give the information to the public and force the Congress, members of Congress to make actual decisions and say what they're going to do. So in terms of just the process itself, it's a very important process to trigger the kind of honest discussion that you just sort of alluded to in terms of who is going to deal with this?

I don't know if any of the others want to respond to that?

MS. RIVLIN: Yes, let me on a happier note say clearly there is going to be pain. But one thing that the projections dramatize is how important it is to use our health resources more efficiently. If we could get the healthcare programs rising less rapidly – they're not going to come down and they're not going to even rise at the same rate as GDP – we're going to use more health care over the years than we spend on other things. But if we could reduce the rate of growth of healthcare spending by making our healthcare system more efficient, and there is lots of scope for that, we could reduce it from 2.5 percent faster than GDP to say 1.5 or even 1 percent. That is a lot. And it's not that there wouldn't be some pain there. Some doctors in the hospitals wouldn't like it, but that's part of the win-win situation.

MR. BUTLER (?): Rudy?

MR. PENNER: I think, too, it is important to ask pain compared to what. What we're talking about is pain relative to the promises that we've made. And the way Social Security, for example, is structured, it implies a continually increasing real benefit, as our wages go up. So maybe it's a little painful to have it shrink relative to the wage earners in our society, but it's no shrinking compared to where it is right now. Comparably in Medicare, one of the major things driving the costs are all of these wonderful technological changes that come along and keep improving the system, but a great expense. I find it hard to envision that we would start throwing out the technologies we have today. So we're talking about looking at the costs as they expand faster than the GDP in the future.

MS. SAWHILL: If I could –

MR. REISCHAUER: Also, if we look out into the future, let's say just simply for Social Security under the current law, what happens is benefits continue as they called for in the law until through 2041, and then in 2042, they are ratably reduced by 22 percent. That is a significant amount of pain for everybody receiving benefits then. So something would have to be done even if we did nothing.

Just to add on to Alice's response about health care, I think we all also recognize that the growing burden of health care is not one that is solely within the federal government; it applies to society at large, and we're going to have to deal with this on a societal basis, the private health insurance, as well as the government health insurance. This proposal that we have might prod Medicare, CMS, to play more of a leadership role in encouraging changes in delivery systems and payment policies that can lead to a more efficient national healthcare system.

MS. SAWHILL: I wanted to just add a comment about another kind of pain that tends to get forgotten. And that is the fact that if we stay on our current course, what's going to happen is that most of the other things that the federal government does are going to get crowded out by increased spending on these programs that primarily serve the elderly. And those programs that are going to get crowded out disproportionately serve younger families and lower-income families. So we are imposing costs on those families now. We also imposing costs or pain on the taxpayers of the future who are likely to be the same people who will have to pay higher taxes if nothing has done. And the cummulation of interest on the debt will make their taxes even higher than they otherwise would have been.

Gene Steuerle, who is a member of our group, has not only written the paper that Rudy referred to earlier, which I highly commend to all of you on the trigger process, but he has also done some work with some other colleagues on how long it will be before everything else that the government does other than defense interest on the debt and spending on these large entitlement programs will crowd out everything else. And it's only about 10 years from now that that occurs. Now, that isn't going to happen, but it probably is, as Alice said, is going to happen if in some measure if nothing else is done.

Q: My name is Richard Owens. I'm retired. I don't represent anybody. But I am a member of the under-informed general public. (Laughter.) It seems to me that that is the primary concern that changing any policy requires, and that is the involvement of the under-informed public. It further seems to me that this topic is not very sexy. It may be drastic or dramatic but it's not very sexy; it's not pedophilia in the House of Representatives – (laughter) – it's not, what civil union versus marriage; it's nothing that grabs the public's attention.

And my question is would it make any sense to treat the federal individual tax rates like one does of variable interest mortgage based upon the national debt and the projections to reduce the national debt over a number of years so that every taxpaying individual would immediately feel some pain because on a yearly basis, those rates would go up or down depending on how long it was going to take to reduce the national debt.

MR. BUTLER: Well, I think that is a good analogy. I would of course be in favor of refinancing to lower your rates as you would probably imagine. (Laughter.) But certainly one of the things that you do in that situation, and anybody with too much debt starts to look at whether the house is bigger than they need, whether they should be moving into something smaller, and so on, I think that is partly what we are talking about here.

But in terms of getting – we are all under-informed to some extent of course, but I think that is why it is very important we are counting an urging depress to talk a lot more about this issue and to do so in ways that really do relate to ordinary people. And certainly there are many journalists who do that, and we would certainly encourage other journalists here to do the same thing and certainly translating these big issues into individual situations. I mentioned the $175,000, the equivalent to that is a mortgage without a house that everybody in America has is due to the unfunded obligation to the federal government. And I think those are examples. But the fact is that it's very important for media to take a very prominent role in looking at ways of explaining this more clearly to people.

Anybody? Yeah, Alice.

MS. RIVLIN: The gentleman poses a very interesting trigger, actually – (laughter) – the ultimate trigger, perhaps, and maybe we should have considered it.

Q: We still can.

MS. RIVLIN: Still can. But I just wanted to say we have been out on the hustings, all of us, on this fiscal wakeup tour. And we do find people aren't very well informed, but they do listen. And the things that public agenda has been doing, if you gather a group of ordinary folks in different parts of the country and give them this problem, they will sit down and work on it and actually find it kind of fun. And they come up with solutions that are perfectly plausible, and why isn't the Congress doing this?

MR. REISCHAUER: Can I just prove that this group is not unanimous on every issue here. I think the point that was raised with the question is a very interesting one, but two things should be kept in mind. One is the vast majority of professional economists would say that there is no particular reasons to, quote, "pay off the national debt." What you worry about is the size of the national debt relative to the economy.

MR. : (Off mike.)

MR. REISCHAUER: I am now going to get more wonky (?). And the debt-to-GDP ratio that we have right now is considerably lower than the one we experienced during the first half of the 1990s. What we're worried about is that over the next 30-or-so years, it's going to get a lot worse, and it's going to go up to levels that we think are unsustainable given our dependence on borrowing from abroad to finance our debt.

MS. RIVLIN: The picture is right over your head.

MR. REISCHAUER: But I did it without even referring to a picture. (Laughter.)

MR. BUTLER: Yes, in the back.

Q: Good morning. I'm Dane Von Breichenruchardt with the Bill of Rights Foundation, but that is neither here nor there. I'm here on my own to try to understand this. My question is, if there is anything worse than being under-informed or un-informed is to be misinformed. And I always that when I come to something like this is that I come uninformed and leave improperly informed.

I cannot figure – tell me where I'm wrong – I cannot understand. It seems like that what we are doing is like rearranging the chairs on the Titanic, that we are facing – and they tell us that, you know, in the hall of Congress they have got these charts at certain places showing the debt being somewhere around about $9 trillion, where in reality, if you really looked – I mean, that is if we paid it right now today, if we all reached in our pockets and paid it today.

And so they are telling us that we are in the 50 trillions in debt if we pay it off over a period of time, and that we're talking about 40-some thousand dollars for household. So with all of this that you have put on here today, I mean, who is going to win the footrace on this thing? I mean, it would seem to me at some point the bottom has got to drop out, and that we have David Walker, who is the former controller of the currency, who says that our economy, our dollar, our monetary system is literally in the toilette.

So I'm wondering why isn't what we're doing here today rearranging chairs on the Titanic when we are facing a much worse situation in the national debt?

MR. BUTLER: I think we're saying that rather than rearranging the chairs, we should go into the bridge and start altering course. And I think that is what we're arguing for here, and to look ahead in terms of what is likely to happen.

I think one of the powerful things that's certainly on the fiscal wakeup tour that we've mentioned in here with this group, is that we're not arguing about the numbers. We can give – we are not shouting heads when it comes to telling you what the numbers are. What we are doing is saying that we need to have a process to reveal those numbers, to do so in a bipartisan way and in an official way, and then there ought to be some steps to require specific action behalf of the Congress to confront those numbers with the American people, to talk to the American people, and to make some decisions about which way forward.

So I think it's very different from the sort of the panic-attack view of this situation, which I think does grip a lot of lawmakers today. They see the problem as so large that, A, they don't want to talk about it, and, B, they just are in sort of like a deer in the headlights when it comes to trying to take some step forward. And we're trying to offer a modest step forward in the sense of changing the rules, changing the process, so we can face up to the situation and start having an orderly debate about which way forward to go.

And I don't know if, Belle, you want to elaborate on that.

MS. SAWHILL: No, I think that is a very correct, and I would particularly emphasize that David Walker does put out the kinds of number you mentioned. They are consistent with the numbers that we are using today. And we all work with Dave Walker very closely as part of this fiscal wakeup tour. So there is no disagreement about the problem. There is still some differences of course even within our group about the appropriate solutions. But we have found it very useful to sit down, as I said at the beginning, and hear each other's views and see if we can find some way to help the Congress and the country move forward.

Now, we're just a group of private citizens; we're here representing ourselves only, not even the institutions that we work for. So we are going to need help from all of you and from – especially from the media to get this message out, whether you like our particular proposals or not is not as important as that you recognize that something needs to be done. And as Alice says, if you don't like our particular proposal, that's fine. We're not particularly wedded to the details of it. We're just really interested in starting a conversation, and we didn't want to come up here and do one more event around, oh, my gosh, the sky is falling and we don't have any ideas about what to do about it. We wanted to put forward some concrete ideas, but we welcome others.

MR. BUTLER: The gentleman here and then we'll go over there.

Q: Thank you. My name is Tim Mcnamara. Two points. One, where do we get the charts and the speeches to go with the report on the website? Will they be one package?

MS. SAWHILL: The report itself, the paper, will be on the Brookings website, the Heritage website, and I think several other websites. I'm not sure. Is it on the – some of the other –

Q: Yeah, I just wanted to make sure I can get the charts and the –

MS. SAWHILL: On the talks, I think you'll have to get those from the people who spoke today, although I'm happy, if it would be helpful to do some coordinating on that.

MR. BUTLER: And I would mention, these charts are all taken from the Congressional Budget Office's long-term projections. Those are available on the CBO cite, cbo.gov.

MS. SAWHILL: We all have a lot of material on our various websites. Bob Bixby, who is the executive director of the Concord Coalition is a member of this group. Their website has a great deal of this sort of material on it.

Q: Excuse me. Second point – I just wanted to say because I'm not of the town, I want to thank you for your efforts in addressing the problem that we should be addressing. And you're absolutely correct; none of the presidential candidates are touching it so thank you.

MR. BUTLER: This gentleman here has been waiting.

Q: In your paper you suggested starting off with a long-term budget for Social Security, Medicare, and Medicaid, and then perhaps later moving into a unified budget perspective officially. And I was wondering if you could talk about the tradeoffs because it seems like given the amount of funding that comes from the general fund from Medicare and Medicaid, it seems like you're sort of missing half of that issue. And I know that in theory you could have any sort of funding. If people want to increase funding for those programs, they could do it anyway, including increasing individual income taxes and then allocating that, that in practice it seems like if you're starting with those three programs in isolations, that you're more likely to ignore the rest of the budget and have less opportunity for reducing other spending and transferring some of that money to these programs or increasing the other types of taxes that are not currently dedicated to those programs.

MS. SAWHILL: We struggled with that question within the group. And as Alice I think emphasized, we decided tha the first step needed to be to address these programs that are growing most rapidly and therefore are threatening fiscal sustainability the most. But that doesn't mean that we don't agree with some of your concerns. Anybody else want to say anything about that?

MS. RIVLIN: No, I think it is a very good question and we didn't entirely solve it. We think that the periodic reconsideration of these three programs would force conversations across the wider budget as well.

MR. BUTLER: And we would just emphasize that what our proposal does is put those programs on the same playing field, if you like, as other programs. And that means there should be an orderly discussion about the commitment we make and how money is allocated and so on. And you're right. There could be a decision to increase those programs and to reduce other programs somewhere else. That is the kind of debate that should take place rather than today where no decision is made. Those three programs and other entitlements expand, crowd out other programs, and that at no point is the Congress forced to actually disclose what its long-term plan is and have a conversation with Americans about it. And that is what we want to bring about.

There was a lady over here I think. Oh, she disappeared. Oh, I'm sorry right here, right here.

Q: Thanks. I just wanted to hear from the panel on how this type of proposal would then interface with the trustees' report because we do have a mechanism to review the situation and to do some forecasting, and there are systems in place. What would be the interface between this proposal and those trustees' reports?

MR. BUTLER: Well, today of course, that report doesn't force action. That is the key difference. We have a very weak action-forcing trigger right now which Rudy may want to comment on in a Medicare program. And there is no requirement. Nothing is going to happen if Congress doesn't do that. You know, Congress is suppose to receive and has received a proposal from the president. Is suppose to expedite, on an expedited basis deal with that because the unfunded – the general revenue financing of Medicare has gone beyond the point that the Medicare legislation in 2003 required action. But there is no default; nothing happens.

And the key thing about our proposal is that first of all, that would be made clear, and then, secondly, if Congress didn't act, some automatic trigger would occur to reign in that – that is the big difference between today and what we're proposing. Rudy, do you want to elaborate on that?

MR. PENNER: One of the questions here would have to be whose numbers are going to be used to ascertain whether we are on the budget path that was specified by the Congress or not. And, you know, conceivably it would be the numbers from the trustees' report, so they would play a very critical role in this whole process.

MR. PENNER: And in fact those numbers could be used as the trigger, which is really exactly what Jane (?) and I suggest.

MS. RIVLIN: We actually weaseled in the report. We said that Congress would have to decide whether to use the trustees' numbers or the CBO numbers.

MR. BUTLER: We have time for one more question to the gentleman there in white, but we will be here for a few minutes afterwards if any of you want to –

Q: I'm Dennis Gilbert from Hamilton College. Political question: It seems to me one of the more bizarre developments of recent years is that the Democrats have emerged as the party of fiscal responsibility and the Republicans seem determined to run the deficit through the ceiling. One suspicion on the left is that there is a current among conservatives. It's perfectly happy to see this happen because they think it will bring the ultimate crash that will result in a radical reduction the size of the federal government.

I wonder if – direct this to you, Mr. Butler, do you think there is any truth to this notion – (laughter) – and second – that is, that some conservatives believe this. And what has been conservative reaction to your initiative? Supportive, suspicious? How is it playing out?

MR. BUTLER: I must say, first of all, I'm not somebody who is in favor of the entire American economy crashing. I want that to be made official on behalf of myself and everybody else. Secondly, I think that for those who want to see big crashes precipitating action I have this horrible fear that if a crash were to come, there is no guarantee that the right action should be taken – would be taken and certainly not the action that maybe I would approve of.

So I don't subscribe to this view that we should somehow be looking forward with excitement about the next crash. I share the view, as others on this group, that it is important to be realistic and to look ahead, and to look at the options, and to debate those options. I think that if – and I say this now as a conservative, but I think that if we debate the options about whether we should see spending continue to increase and taxes keeping up, well, we know from the Congressional Budget Office that it should require very high rates of tax. Americans would not accept that option. Others may disagree with me.

In terms of I think how conservatives look at this, and others can say how they think liberals look at this, I think that a concern of course is whether debating these issues will in fact lead to a surge of support for tax increases. My opinion is it won't, that if it is debated, there will be an honest discussion and appropriate steps. And so I think that

that's how I would respond to the question. Others can respond from their particular perspectives, left, right, and center. You don't even have to disclose them.

Rudy.

MR. PENNER: (Chuckles.) Well, as Alice said, I think really the ideal solution here would be to think of some kind of artificial crisis that provoked action but didn't harm the economy that much. And that was sort of what Gramm-Rudman did. It's also in Europe some of the Social Security reforms have been provoked by the Maastricht Treaty, which set deficit targets like Gramm-Rudman, and that's a very artificial kind of discipline, but nevertheless, I think that that did play some role in the German social security reforms, for example, certainly in the Italian reforms. So it would be nice if we could think up something like that for the United States.

MR. BUTLER: I just wanted to see if any of our colleagues, Gene or any of the others want to make a comment. Gene.

GENE STEUERLE: A quick reaction to your question, Stewart. I think a number of us believe that the real tax rate in the economy is equal to the spending rate. And what you see is the collection rate, that when added to the – (inaudible) – the taxes will be pushing off onto the future generations of the – (inaudible) – so it's not clear if you get any part of the – (inaudible) – you're not reducing long-term taxes. And it's just another very – (inaudible) – comment on why you think that you might get action in he ear term, is I think when then next president steps into office, it's very likely that he or she will face the budget office – (inaudible) – and say that in three or four years, you've got less flexibility than any president in modern history, unless you get this budget – (inaudible).

MR. BUTLER: Anybody else. Do you want to say some –

MS. SAWHILL: I think that we're going to call this to a close. And we all want to thank you for coming. We appreciate it very much, and we will hope that Congress and others who are in position to act will do something as a result of all of us caring about the future of the country. Thank you.

(Applause.)

(END)