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# CONCURRENT RESOLUTION ON THE BUDGET FISCAL YEAR 2016

## HEARINGS

BEFORE THE

## COMMITTEE ON THE BUDGET UNITED STATES SENATE

ONE HUNDRED FOURTEENTH CONGRESS

FIRST SESSION

**January 28, 2015-CBO'S BUDGET AND ECONOMIC OUTLOOK: FISCAL YEARS 2015-2025**

**February 3, 2015-THE PRESIDENT'S FISCAL YEAR 2016 BUDGET PROPOSAL**

**February 11, 2015-THE COMING CRISIS: SOCIAL SECURITY DISABILITY TRUST FUND INSOLVENCY**

**February 25, 2015-THE COMING CRISIS: AMERICA'S DANGEROUS DEBT**

**March 4, 2015-WASTEFUL DUPLICATION IN THE FEDERAL GOVERNMENT**

**March 11, 2015-BENEFITS OF A BALANCED BUDGET**

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# CBO'S BUDGET AND ECONOMIC OUTLOOK: FISCAL YEARS 2015–2025

**WEDNESDAY, JANUARY 28, 2015**

UNITED STATES SENATE,
COMMITTEE ON THE BUDGET,
*Washington, D.C.*

The committee met, pursuant to notice, at 10:00 a.m., in Room SD–608, Dirksen Senate Office Building, Hon. Mike Enzi, chairman of the committee, presiding.

Present: Senators Enzi, Crapo, Portman, Toomey, Johnson, Ayotte, Wicker, Corker, Perdue, Sanders, Murray, Stabenow, Whitehouse, Merkley, Baldwin, King, and Kaine.

Staff Present: Eric M. Ueland, Republican Staff Director; and Warren Gunnels, Minority Staff Director.

## OPENING STATEMENT OF CHAIRMAN ENZI

Chairman ENZI. Good morning. I will call to order the first Senate Budget Committee hearing of the 114th Congress.

This morning, we will hear testimony from the Congressional Budget Office Director, Doug Elmendorf, as he explains CBO's outlook on critical fiscal issues confronting our country.

Congress is under new management, and so is this committee. I am Mike Enzi. I am a Senator from Wyoming. I was first elected in 1996. Budgets matter to me. I am an accountant. I ran a small business in Wyoming for many years and kept my books balanced. I ran for mayor when I was 29 on a balanced budget platform and got elected, and then later got elected as a State legislator on the same platform. In both roles, one of my key jobs was making sure that the city budget, and then the State budget, balanced every year. I did not forget that when I came to the Senate. My first floor speech was to support a Constitutional amendment to balance the budget. After several years in the Senate, I finally had a chance to join this committee and got to be Chairman earlier this month.

There is some activity across the nation that we should be interested in. There are 24 States that have already passed a Balanced Budget Constitutional Convention amendment, and there are ten more that are working on it. If 34 states pass it, that makes it happen.

What could that mean? Currently, we spend 3.9 trillion dollars—that does not sound like nearly as much as 3,900 billion dollars, which is what we spend. I think that is easier to understand. Twenty-eight-hundred billion of those are checks that are automatically written. We do not make any special decisions on them. So, that leaves us with 1,100 billion to make the decision. Last

year, we spent one-and-one-tenths trillion, 1,100 billion. The deficit last year was 468 billion. So, we spent almost 50 percent more than we took in.

So, to balance the budget, we would have to make some really detrimental decisions. Just trying to balance the budget over ten years, which is what we are trying to do in this budget, will be a difficult task. Of course, that is all related to the debt and interest. It would help if we could stay at a mere one-and-seven-tenths percent interest rate.

This year, I intend to run a Budget Committee dedicated to the proposition that we have to confront spending, bringing the deficit to an end and ultimately balancing the budget. We are currently receiving more revenues than we have received in the history of the United States, but we are still spending a lot more than our revenues.

As the first accountant to handle the gavel, the focus for me will always be the numbers. What do we spend? Where does that spending go? Where does the money we spend come from? Can we afford the spending we have? Where can we find the best value for the money that comes to Washington and leaves our Treasury?

One thing I learned at an early age, while you can lie about the numbers, numbers never lie, and so I will always be looking for the numbers—looking at the numbers and, hopefully, understanding the numbers to be able to explain to colleagues and constituents the facts about our budget and our spending.

Let me give you an example. I hear repeatedly that the Federal Government has trust funds to cover a variety of multi-decade commitments our government has. But, these trust funds are like nothing we know of in the private sector. They do not keep resources in trust for beneficiaries to claim in the future. Show me the cash. Instead, money sent to Washington for trust funds are swapped out for Federal bonds, and the cash that you think you can count on is instead spent now on present needs. That is why some of our greatest so-called trust funds are facing serious difficulties, according to the people responsible for them. Without action, we face the prospect of beneficiaries suffering significant harm in just a few years. So, be careful. If it is a Federal trust fund, do not trust it.

Runaway spending habits have bred excessive deficits and incredible debt. As we meet this morning, our Federal debt totals over $18 trillion. That means every man, woman, and child—child, even if they were born today—owes over $56,000 on that debt. Every man, woman, and child owes $56,000 of that debt. I remember about three years ago when I was telling the people in Wyoming what every man, woman, and child owed, and it was over $49,000. It was almost $50,000. Now, we are at $56,000.

Federal spending has hit a record high. Revenues are at an historic height, as well. Yet, every year, we run deficits that are on track to hit one trillion dollars. The more deficits we have, the more debt we owe, the more we add to the tab for future Americans as yet unborn. That just does not seem right to me. Our budget process lacks transparency. It seems designed to confuse. It leaves the general public unsatisfied that their concerns have been heard in Washington.

Over time, I would like this committee to begin work on addressing problems with the budget framework that exists so it becomes more responsive to the people we serve. Working with you and your colleagues, Senator Sanders, I think there are good opportunities for bipartisanship here. After all, no one likes the budget process we currently have.

The committee has a significant responsibility. We are required by law to produce a budget resolution. Congress has not produced a budget resolution since 2009, and it has been ten years since the House and Senate agreed together on a budget. The law says we should get it done by April 15. As of today, there are only 77 days before April 15 for us to get our work done. Together with my House counterpart, I am dedicated to doing all I can to meet that deadline.

The committee will act on a budget resolution. We will report it out. The Senate will consider it. We will negotiate with the House. We will pass a common budget resolution. We will write a plan to restore common sense and good budgeting to Washington. We will act to control the spending, reduce the deficits, and end the debt.

We will act to restore balance to our budget, certainty to the economy, and confidence to our constituents, and in doing so, we will take the first necessary step to standing up for Americans so that, over time, their share of what we all owe can stop growing and start shrinking and people can see more of the American dream. They can keep more of what they earn. They can save for what they need. They can expect the government to help them when it must, while they can accomplish all they dream. Our country needs to act. It is time for us to come off the sidelines and get the job done to balance the budget.

Senator SANDERS.

**OPENING STATEMENT OF SENATOR SANDERS**

Senator SANDERS. Well, thank you very much, Chairman Enzi. Congratulations on your assuming the Chairmanship of this important committee, and we are delighted that Director Elmendorf is here with us today. We look forward to his testimony.

Mr. Chairman, the good news is that our economy has come a very long way since President Bush left office in January 2009. At that time, we were hemorrhaging some 800,000 jobs a month, our financial system was on the verge of collapse, and the deficit was $1.4 trillion. Over the last six years, the economy has made substantial progress. During the last reported quarter, we saw very strong economic growth of five percent, and last month, the economy created another 252,000 jobs. This is the 58th straight month of private sector job growth.

Further, the Federal deficit has been reduced by more than two-thirds since 2008 and Federal deficits over the next decade are estimated to be about $5.5 trillion lower compared to what the CBO projected in 2010. That is more than what the Simpson-Bowles Fiscal Commission called for just four years ago.

All of that good news, however, does not tell the full story of what is happening in our economy and what is happening to the lives of tens of millions of working families in all of our States. While we must continue to focus on the Federal deficit, we must

also be aware that there are other deficits in our society that are causing horrendous pain for the vast majority of the American people. There are deficits in decent paying jobs. There are deficits in infrastructure, deficits in income, deficits in equality, deficits in retirement security, deficits in education, and deficits in trade.

Let me briefly make six points. One, the United States today is experiencing more income and wealth inequality than any major country on earth and more than any time in our country since 1929. Today, if you can believe it, the top one-tenth of one percent own almost as much wealth as the bottom 90 percent, and one family—the Walton family of Walmart—owns more wealth than the bottom 40 percent of Americans. Since 1999, the typical middle class family has seen its real income go down by nearly $5,000. Meanwhile, since the Wall Street crash of 2008 were then, 95 percent of all new income has gone to the top one percent. In 2013, 25 hedge fund managers made more income than 425,000 public school teachers. The simple truth is that the rich are becoming much richer while the middle class continues a 40-year decline. This committee, Mr. Chairman, in my view, must address that issue.

Two, while unemployment has fallen significantly over the last six years, we must be mindful of the fact that real unemployment, which includes those people working part-time when they want to work full-time and those people who have given up looking for work, is not the official 5.6 percent, but over 11 percent. Further—and we do not talk about this—youth unemployment is close to 17 percent, and African American youth unemployment is close to 30 percent. In other words, while we have made some progress in reducing unemployment, we still have to create millions of decent paying jobs. And, in my view, the fastest way to do that is to rebuild our crumbling infrastructure—roads, bridges, water systems, wastewater plants, rail, et cetera—and we can create millions of jobs doing that, and that is an issue that this committee must address.

Three, in a time when millions of Americans are working longer hours for low wages, we need to substantially increase wages for low- and middle-income workers. Today, the minimum wage after adjusting for inflation is about one-third lower today than it was in 1968. To equal the purchasing power of what the minimum wage was back then, we would have to raise it to $10.88 an hour. Furthermore, we have got to reform our antiquated overtime regulations. There are supervisors at McDonald's who work 60 hours a week and make $27,000 a year and they do not get paid time-and-a-half for any overtime. So, I think this is an issue that this committee should address.

And, four, if we are going to lower our deficit, invest in our economy to create the jobs that we need and bring about more income and wealth equality [sic] in our country, we need real tax reform. It is unacceptable that each and every year, millionaires, billionaires, and profitable corporations avoid $100 billion in taxes by stashing their cash in the Cayman Islands and other offshore tax havens. It is unacceptable to me that huge profitable corporations, like General Electric, Verizon, Bank of America, and Citigroup, have in recent years paid nothing in Federal income taxes, and in

some cases have even gotten huge rebates from the IRS. That is an issue that this committee should be addressing.

Five, at a time when the United States is engaged in an extremely competitive global economy, it is unacceptable to people throughout this country that millions of our young people cannot afford to go to college and are leaving school deeply in debt. We have got to address the issue of college affordability and make sure that in a competitive global economy our kids get the education they need.

And, last but not least, in the midst of the obscene level of wealth and income equality that we are experiencing, the United States has by far the highest rate of childhood poverty of any major country on earth, and I would trust that there is no person on this committee who is happy that 20 percent of our kids are living in poverty. Further, millions of seniors and disabled people are struggling to put food on the table, and over the last six years, as this committee knows, the cost-of-living adjustments for Social Security have been incredibly paltry—zero percent, zero percent, 3.6, 1.7, 1.5, 1.7—not keeping up with inflation that our seniors need. According to some of the most recent statistics, 20 percent of seniors live on an average of just $7,600 a year. In 2013, half of all older adults lived on less than $21,000 a year. Bottom line: We have got to move aggressively to expand benefits for our Social Security beneficiaries.

The bottom line to me, Mr. Chairman, is when we put people to work, when we have the best educated workforce in the world, people will be paying more taxes. Our deficit will go down. That is, in my view, the way we deal with deficits, and thank you very much.

Chairman ENZI. Thank you, Senator Sanders. I look forward to working with you and having some very spirited debates in the years to come.

Our witness this morning is Dr. Doug Elmendorf, the eighth Director of the Congressional Budget Office. The CBO serves an instrumental role for the Budget Committees. The agency provides necessary information important to assessing the budget impact of proposals from both the administration and Congress. As well, CBO continually examines the state of the economy and the budget to keep us apprised of the fiscal context in which we operate.

Dr. Elmendorf has served as Director of the CBO since 2009, coming to this Congressional support organization from previous stints at CBO, at the Federal Reserve Board, at the Council of Economic Advisors, at the Treasury Department, and at the Brookings Institution.

This morning, Director Elmendorf will be talking to us about CBO's latest baseline, which is their outlook on the economy and the Federal budget over the next ten years. As he revealed on Monday, our annual deficit, already too high at nearly $500 billion, is expected to grow to a trillion in just ten short years. The debt is expected to grow by nine trillion over the next decade, and that is without any new programs and realizing we are already receiving more revenues than at any time in our history. The interest costs, which we must pay but which provide no services to Americans, are expected to cost five-and-six-tenths trillion dollars. It is clear

that our $18 trillion debt is the anchor which will sink us if we do not change course.

For your information, colleagues, Dr. Elmendorf has let us know that he will take about eight minutes with his opening statement this morning. Following that, we will turn to questions.

Welcome, Dr. Elmendorf. Please begin.

**STATEMENT OF DOUGLAS W. ELMENDORF, DIRECTOR, CONGRESSIONAL BUDGET OFFICE**

Mr. ELMENDORF. Thank you very much, Chairman Enzi, Senator Sanders. My colleagues and I look forward to working with both of you and with all the members of the committee in this Congress.

The Federal budget deficit, which has fallen sharply during the past few years, is projected to hold steady relative to the size of the economy through 2018. Beyond that point, however, the gap between spending and revenues is projected to grow, further increasing Federal debt relative to the size of the economy, which is already historically high.

Those projections are based on the assumption that current laws governing taxes and spending will generally remain unchanged, and they are built upon our economic forecast. According to that forecast, the economy will expand at a solid pace in 2015 and for the next few years, to the point that the gap between the nation's output and its potential, or maximum sustainable output, will be essentially eliminated by the end of 2017.

Let me address the budget outlook first and then turn to the economic outlook.

We estimate that the deficit for this fiscal year, 2015, will amount to $468 billion, slightly less than the deficit for 2014. At 2.6 percent of GDP, this year's deficit is projected to be the smallest relative to the nation's output since 2007, but close to the average 2.7 percent of GDP the deficits have averaged over the past 50 years.

Although the deficits in our baseline projections remain roughly stable as a percentage of GDP through 2018, they rise after that. The deficit in 2025 is projected to be $1.1 trillion, or 4.0 percent of GDP. And, cumulative deficits over the 2016 to 2025 period are projected to total $7.6 trillion.

We expect that Federal debt held by the public will amount to 74 percent of GDP at the end of this fiscal year, more than twice what it was at the end of 2007 and higher than in any year since 1950. By 2025, in our baseline projections, Federal debt rises to nearly 79 percent of GDP.

When we last issued long-term projections last summer, we projected that under current law, debt would exceed 100 percent of GDP 25 years from now and would continue on an upward trajectory thereafter. That trend could not be sustained. Such large and growing Federal debt would have serious negative consequences, including increasing Federal spending for interest payments, restraining economic growth in the long term, giving policy makers less flexibility to respond to unexpected challenges, and eventually heightening the risk of a fiscal crisis.

Why will deficits and debt increase relative to the GDP under current law? In our projections, outlays rise from a little more than

20 percent this year, which is about what Federal spending has averaged over the past 50 years, to a little more than 22 percent in 2025. Four key factors underlie that increase: The retirement of the Baby Boom generation, the expansion of Federal subsidies for health insurance, increasing health care costs per beneficiary, and rising interest rates on Federal debt. Consequently, under current law, spending would grow faster than the economy for Social Security, for the major health care programs, including Medicare, Medicaid, and subsidies offered through insurance exchanges, and for net interest costs.

In stark contrast, mandatory spending other than that for Social Security and health care, as well as both defense and non-defense discretionary spending, would shrink markedly relative to the size of the economy. By 2019, outlays in those three categories taken together would fall below the percentage of GDP they were between 1998 and 2001, when such spending was the lowest since at least 1940, the earliest year for which comparable data have been reported.

Revenues are projected to rise significantly by 2016, buoyed by the expiration of several provisions that reduced tax liabilities and by the ongoing economic expansion. In our projections, based on current law, revenues equal about 18.5 percent of GDP in 2016 and remain between 18 and 18.5 percent throughout the coming decade. Revenues at that level would represent a greater share of the economy than their 50-year average of about 17.5 percent of GDP, but would still be less than outlays by growing amounts over the course of the decade.

Turning from the budget to the economy, we anticipate that increases in consumer spending, business investment, and residential investment will drive the economic expansion this year and over the next few years. As measured by the change from the fourth quarter of the previous year, we expect that real GDP will grow by about three percent in 2015 and 2016, and by 2.5 percent in 2017. We construct our forecast to be in the middle of the distribution of possible outcomes at the time the forecast is made, but significant uncertainty surrounds it and all economic forecasts.

The difference between actual GDP and our estimate of potential GDP, which is the measure of slack for the whole economy, was about two percent of potential GDP at the end of 2014. During the next few years, we expect actual GDP will rise more rapidly than its potential, gradually eliminating that slack. By our projections, increased hiring will reduce the unemployment rate from 5.7 percent in the fourth quarter of last year to 5.3 percent in the fourth quarter of 2017, which is close to the natural rate of unemployment, that is, the rate arising from all sources except for fluctuations in the overall demand for goods and services. That increased hiring will also encourage more people to enter or stay in the labor force, boosting the labor force participation rate.

Our projections beyond the next few years are not based on estimates of cyclical developments in the economy because we do not attempt to predict economic fluctuations that far into the future. Instead, those projections are based on estimates of underlying factors that affect the economy's productive capacity.

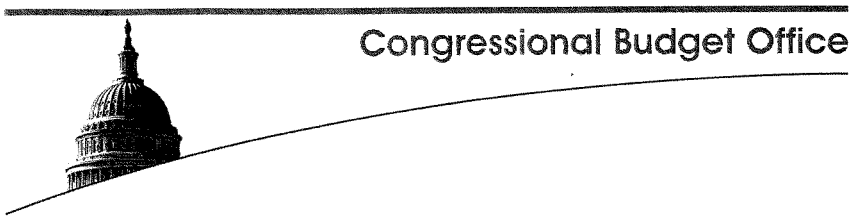
For 2020 through 2025, we project that real GDP will grow by an average of 2.2 percent per year, a rate that matches our estimate of the potential growth of the economy in those years. Potential output is expected to grow much more slowly than it did during the 1980s and 1990s, primarily because the labor force is anticipated to expand more slowly than it did then. Growth in the labor force will be held down by the ongoing retirement of the Baby Boom generation, by a relatively stable labor force participation rate among working age women after sharp increases from the 1960s to the mid-1990s, and by Federal tax and spending policies in current law.

The elimination of slack in the economy will eventually remove the downward pressure on the rate of inflation and on interest rates that has existed in the past several years. By our estimates, the rate of inflation, as measured by the price index for personal consumption expenditures, will move up gradually to the Federal Reserve's goal of two percent, hitting that mark in 2017 and beyond.

Interest rates on Treasury securities, which had been exceptionally low since the recession, will rise considerably in the next few years, we expect, but remain lower than they were, on average, in previous decades. Between 2020 and 2025, the projected interest rates on three-month Treasury bills and ten-year Treasury notes are 3.4 percent and 4.6 percent, respectively. Interest rates, of course, are volatile, and those figures represent CBO's projections of the average rates over that period.

Thank you. I am happy to take your questions.

[The prepared statement of Mr. Elmendorf follows:]




# Testimony

# The Budget and Economic Outlook: 2015 to 2025

**Douglas W. Elmendorf**
**Director**

**Before the**
**Committee on the Budget**
**United States Senate**

**January 28, 2015**

*This document is embargoed until it is delivered at 10:00 a.m. (EST) on Wednesday, January 28, 2015. The contents may not be published, transmitted, or otherwise communicated by any print, broadcast, or electronic media before that time.*

Chairman Enzi, Senator Sanders, and Members of the Committee, thank you for inviting me to testify on the Congressional Budget Office's most recent analysis of the outlook for the budget and the economy. My statement summarizes CBO's new baseline budget projections and economic forecast, which cover the period from 2015 to 2025. Those estimates were released this week in the report titled *The Budget and Economic Outlook: 2015 to 2025*.

The federal budget deficit, which has fallen sharply during the past few years, is projected to hold steady relative to the size of the economy through 2018. Beyond that point, however, the gap between spending and revenues is projected to grow, further increasing federal debt relative to the size of the economy—which is already historically high.

Those projections by the CBO, based on the assumption that current laws governing taxes and spending will generally remain unchanged, are built upon the agency's economic forecast. According to that forecast, the economy will expand at a solid pace in 2015 and for the next few years—to the point that the gap between the nation's output and its potential (that is, maximum sustainable) output will be essentially eliminated by the end of 2017. As a result, the unemployment rate will fall a little further, and more people will be encouraged to enter or stay in the labor force. Beyond 2017, CBO projects, real (inflation-adjusted) gross domestic product (GDP) will grow at a rate that is notably less than the average growth during the 1980s and 1990s.

## Rising Deficits After 2018 Are Projected to Gradually Boost Debt Relative to GDP

CBO estimates that the deficit for this fiscal year will amount to $468 billion, slightly less than the deficit in 2014 (see Table 1). At 2.6 percent of GDP, this year's deficit is projected to be the smallest relative to the nation's output since 2007 but close to the 2.7 percent that deficits have averaged over the past 50 years.

Although the deficits in CBO's baseline projections remain roughly stable as a percentage of GDP through 2018, they rise after that. The deficit in 2025 is projected to be $1.1 trillion, or 4.0 percent of GDP, and cumulative deficits over the 2016–2025 period are projected to total $7.6 trillion. CBO expects that federal debt held by the public will amount to 74 percent of GDP at the end of this fiscal year—more than twice what it was at the end of 2007 and higher than in any year since 1950 (see Figure 1). By 2025, in CBO's baseline projections, federal debt rises to nearly 79 percent of GDP.

### Outlays

In CBO's projections, outlays rise from a little more than 20 percent of GDP this year (which is about what federal spending has averaged over the past 50 years) to a little more than 22 percent in 2025 (see Figure 2 on page 4). Four key factors underlie that increase:

- The retirement of the baby-boom generation,
- The expansion of federal subsidies for health insurance,
- Increasing health care costs per beneficiary, and
- Rising interest rates on federal debt.

Consequently, under current law, spending will grow faster than the economy for Social Security; the major health care programs, including Medicare, Medicaid, and subsidies offered through insurance exchanges; and net interest costs. In contrast, mandatory spending other than that for Social Security and health care, as well as both defense and nondefense discretionary spending, will shrink relative to the size of the economy. By 2019, outlays in those three categories taken together will fall below the percentage of GDP they were from 1998 through 2001, when such spending was the lowest since at least 1940 (the earliest year for which comparable data have been reported).

### Revenues

Revenues are projected to rise significantly by 2016, buoyed by the expiration of several provisions of law that reduced tax liabilities and by the ongoing economic expansion. In CBO's projections, based on current law, revenues equal about 18½ percent of GDP in 2016 and remain between 18 percent and 18½ percent through 2025. Revenues at that level would represent a greater share of the economy than their 50-year average of about 17½ percent of GDP but would still be less than outlays by growing amounts over the course of the decade. Revenues from the individual income tax are expected to rise relative to GDP—mostly because people's income will move into higher tax brackets as income gains outpace inflation, to which those brackets are indexed. But those increases are expected to be offset by reductions relative to GDP in revenues from the corporate income tax and other sources.

**Table 1.**

**CBO's Baseline Budget Projections**

| | Actual, 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | Total 2016-2020 | Total 2016-2025 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | | | In Billions of Dollars | | | | | | | |
| Revenues | 3,021 | 3,189 | 3,460 | 3,588 | 3,715 | 3,865 | 4,025 | 4,204 | 4,389 | 4,591 | 4,804 | 5,029 | 18,652 | 41,670 |
| Outlays | 3,504 | 3,656 | 3,926 | 4,076 | 4,255 | 4,517 | 4,765 | 5,018 | 5,337 | 5,544 | 5,754 | 6,117 | 21,540 | 49,310 |
| **Deficit** | **-483** | **-468** | **-467** | **-489** | **-540** | **-652** | **-739** | **-814** | **-948** | **-953** | **-951** | **-1,088** | **-2,887** | **-7,641** |
| Debt Held by the Public at the End of the Year | 12,779 | 13,359 | 13,905 | 14,466 | 15,068 | 15,782 | 16,580 | 17,451 | 18,453 | 19,458 | 20,463 | 21,605 | n.a. | n.a. |
| | | | | | | | As a Percentage of Gross Domestic Product | | | | | | | |
| Revenues | 17.5 | 17.7 | 18.4 | 18.2 | 18.1 | 18.1 | 18.0 | 18.1 | 18.1 | 18.2 | 18.2 | 18.3 | 18.1 | 18.2 |
| Outlays | 20.3 | 20.3 | 20.8 | 20.7 | 20.7 | 21.1 | 21.4 | 21.6 | 22.0 | 21.9 | 21.8 | 22.3 | 21.0 | 21.5 |
| **Deficit** | **-2.8** | **-2.6** | **-2.5** | **-2.5** | **-2.6** | **-3.0** | **-3.3** | **-3.5** | **-3.9** | **-3.8** | **-3.6** | **-4.0** | **-2.8** | **-3.3** |
| Debt Held by the Public at the End of the Year | 74.1 | 74.2 | 73.8 | 73.4 | 73.3 | 73.7 | 74.3 | 75.0 | 76.1 | 76.9 | 77.7 | 78.7 | n.a. | n.a. |

Source: Congressional Budget Office.

Note: GDP = gross domestic product; n.a. = not applicable.

### Changes From CBO's Previous Budget Projections

The deficit that CBO now estimates for 2015 is essentially the same as what the agency projected in August.[1] CBO's estimate of outlays this year has declined by $94 billion, or about 3 percent, from the August projection because of a number of developments, including higher-than-expected receipts from auctions of licenses to use the electromagnetic spectrum for commercial purposes. But CBO's estimate of revenues has dropped almost as much—by $93 billion, also about 3 percent—mostly because of the enactment of legislation that retroactively extended a host of expired tax provisions through December 2014.

Over the 2015–2024 period, deficits are now projected to total about $175 billion less than CBO's August estimate for that period. The current projections of revenues and outlays for those years are both lower than previously estimated, outlays a little more so.

1. See Congressional Budget Office, *An Update to the Budget and Economic Outlook: 2014 to 2024* (August 2014), www.cbo.gov/publication/45653.

### The Longer-Term Outlook

When CBO last issued long-term budget projections (in July 2014), it projected that, under current law, debt would exceed 100 percent of GDP 25 years from now and would continue on an upward trajectory thereafter—a trend that could not be sustained.[2] (The 10-year projections presented here do not materially change that outlook.)[3] Such large and growing federal debt would have serious negative consequences, including increasing federal spending for interest payments; restraining economic growth in the long term; giving policymakers less flexibility to respond to unexpected challenges; and eventually heightening the risk of a fiscal crisis.

## The Economy Will Grow at a Solid Pace Over the Next Few Years

CBO anticipates that, under current law, economic activity will expand at a solid pace in 2015 and over the next

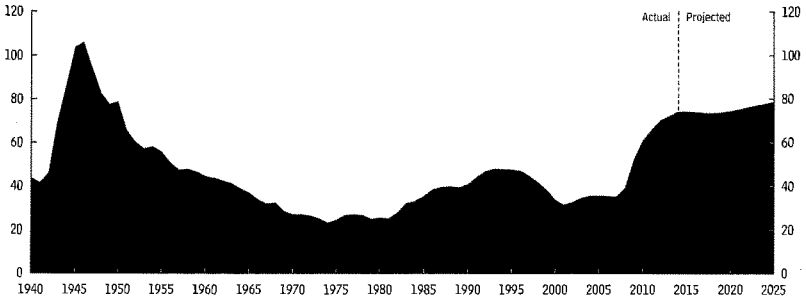
2. See Congressional Budget Office, *The 2014 Long-Term Budget Outlook* (July 2014), www.cbo.gov/publication/45471.

3. CBO's current projection of debt as a percentage of GDP in 2024 is quite close to that used as the starting point for the projections in *The 2014 Long-Term Budget Outlook*.

**Figure 1.**

**Federal Debt Held by the Public**

Percentage of Gross Domestic Product




Source: Congressional Budget Office.

few years—reducing the amount of underused resources, or "slack," in the economy.

### Economic Growth Over the Next Few Years

In CBO's estimation, increases in consumer spending, business investment, and residential investment will drive the economic expansion this year and over the next few years. The growth in those categories of spending will derive mainly from increases in hourly compensation, rising wealth, the recent decline in crude oil prices, and a step-up in the rate of household formation (as people are more willing and able to set up new homes). As measured by the change from the fourth quarter of the previous year, real GDP will grow by about 3 percent in 2015 and 2016 and by 2½ percent in 2017, CBO expects (see Figure 3).

### The Degree of Slack in the Economy Over the Next Few Years

The difference between actual GDP and CBO's estimate of potential GDP—which is a measure of slack for the whole economy—was about 2 percent of potential GDP at the end of 2014. During the next few years, CBO expects, actual GDP will rise more rapidly than its potential, gradually eliminating that slack. For the labor market in particular, CBO anticipates that slack will dissipate by the end of 2017. By CBO's projections, increased hiring will reduce the unemployment rate from 5.7 percent in the fourth quarter of 2014 to 5.3 percent in the fourth quarter of 2017, which is close to the expected natural rate of unemployment (that is, the rate arising from all sources except fluctuations in the overall demand for goods and services). That increased hiring will also encourage more people to enter or stay in the labor force, boosting the labor force participation rate (which is the percentage of people who are working or actively looking for work).

### Economic Growth in Later Years

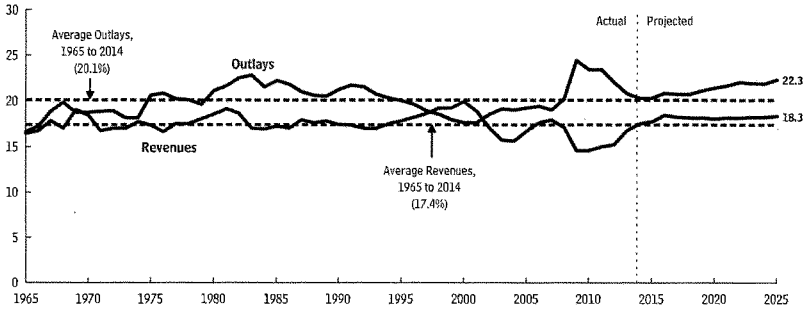
The agency's projections beyond the next few years are not based on estimates of cyclical developments in the economy, because the agency does not attempt to predict economic fluctuations that far into the future; instead, those projections are based on estimates of underlying factors that affect the economy's productive capacity.

For 2020 through 2025, CBO projects that real GDP will grow by an average of 2.2 percent per year—a rate that matches the agency's estimate of the potential growth of the economy in those years. Potential output is expected to grow much more slowly than it did during the 1980s and 1990s primarily because the labor force is anticipated to expand more slowly than it did then. Growth in the potential labor force will be held down by the ongoing retirement of the baby boomers; by a relatively stable labor force participation rate among working-age women, after sharp increases from the 1960s

**Figure 2.**

**Total Revenues and Outlays**

Percentage of Gross Domestic Product




Source: Congressional Budget Office.

to the mid-1990s; and by federal tax and spending policies set in current law.

### Inflation and Interest Rates

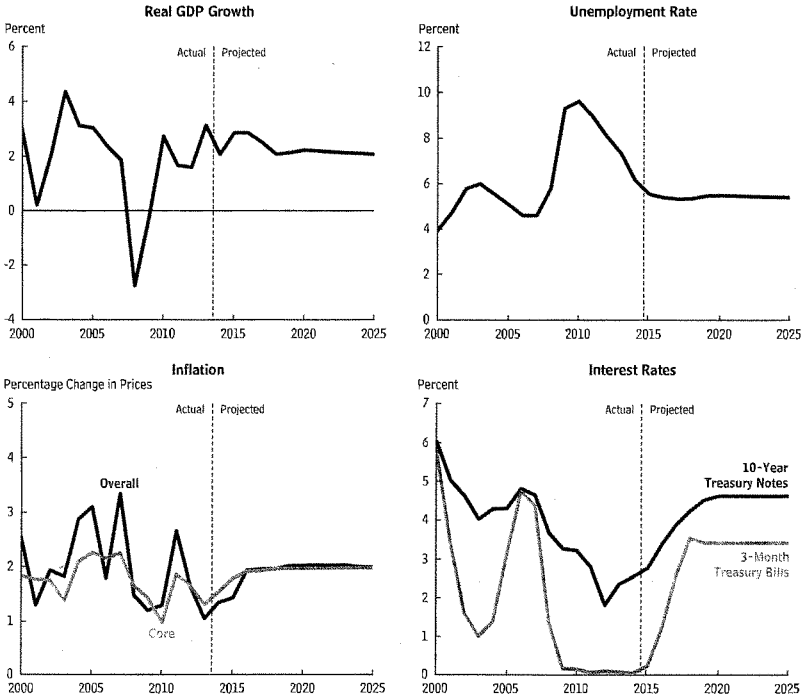
The elimination of slack in the economy will eventually remove the downward pressure on the rate of inflation and on interest rates that has existed for the past several years. By CBO's estimates, the rate of inflation as measured by the price index for personal consumption expenditures will move up gradually to the Federal Reserve's goal of 2 percent, hitting that mark in 2017 and beyond. Interest rates on Treasury securities, which have been exceptionally low since the recession, will rise considerably in the next few years, CBO expects, but remain lower than they were, on average, in previous decades. Between 2020 and 2025, the projected interest rates on 3-month Treasury bills and 10-year Treasury notes are 3.4 percent and 4.6 percent, respectively.

### Changes From CBO's Previous Economic Projections

Last August, CBO projected real GDP growth averaging 2.7 percent per year for 2014 through 2018; CBO now anticipates that real GDP growth will average 2.5 percent annually over that period. The revision mainly reflects a reduction in CBO's estimate of potential output and therefore of the current amount of slack in the economy. On the basis of the current projection of potential output, CBO now forecasts that real GDP in 2024 will be roughly 1 percent lower than the level estimated in August. In addition, the sharper-than-anticipated drop in the unemployment rate in the second half of last year caused CBO to lower its projection of that rate for the next few years.

**Figure 3.**

**Actual Values and CBO's Projections of Key Economic Indicators**




Sources: Congressional Budget Office; Bureau of Economic Analysis; Bureau of Labor Statistics; Federal Reserve.

Notes: Real gross domestic product is the output of the economy adjusted to remove the effects of inflation. The unemployment rate is a measure of the number of jobless people who are available for work and are actively seeking jobs, expressed as a percentage of the labor force. The overall inflation rate is based on the price index for personal consumption expenditures; the core rate excludes prices for food and energy.

Data are annual. For real GDP growth and inflation, actual data are plotted through 2013; the values for 2014 reflect CBO's estimates for the third and fourth quarters and do not incorporate data released by the Bureau of Economic Analysis since early December 2014. For the unemployment and interest rates, actual data are plotted through 2014.

For real GDP growth and inflation, percentage changes in GDP and prices are measured from the fourth quarter of one calendar year to the fourth quarter of the next.

GDP = gross domestic product.

Chairman ENZI. Thank you, Dr. Elmendorf. You know, predictions really are tough, particularly when they are about the future.

Mr. ELMENDORF. Yes, Mr. Chairman.

[Laughter.]

Chairman ENZI. We appreciate all your effort on that. So, we will turn to questions, but let me take a minute to explain the process for the committee members before we start.

Each member will have five minutes to question. I will begin with myself and then Senator Sanders. And then following the two of us, I will alternate questions between the majority and the minority. All members who are in attendance when the hearing began will be recognized in the order of seniority. For those who arrived after the hearing began, you are on the list in the order of arrival. If it comes to your turn on the list to be recognized but you are not here, then you will move to the bottom of the list and we will turn to the next Senator on that side of the aisle to ask questions. When everyone is done—when everyone else is done, then I will recognize that person for questions.

With that, Dr. Elmendorf, thank you for your testimony and I have a few questions. I am very concerned about the national debt. I wake up in the middle of the night concerned about its effects. Am I right to believe that a failure to confront our debt challenge with a serious plan to reduce deficits could only worsen our economic and fiscal health? Congress needs to act on deficits sooner, rather than later, is that correct?

Mr. ELMENDORF. I think it is certainly right, Mr. Chairman, that the sooner Congress sets a course, decides what sorts of policy changes would be appropriate to address the fiscal imbalance, then the more gradually those changes can be implemented while still achieving whatever particular target for deficits and debt you would consider. I think the pace at which particular changes are set in motion would depend on your and your colleagues' judgments about how quickly benefit programs or tax policies could be changed without being too disruptive to individuals or firms or State and local governments. It would also depend on your assessment of economic conditions.

Chairman ENZI. Thank you. Your analysis finds that the interest costs on the national debt will rise dramatically in the next decade, from $227 billion this year to $827 billion in 2025. To me, every dollar spent on interest is another dollar we will not be able to use for government services on an individual in need or another dollar that will not be available to a taxpayer for their own needs. Are the large and growing interest costs a problem for us? How conservative were you?

Mr. ELMENDORF. So, Mr. Chairman, the growing interest costs are a problem, because, as you say, for any given level of spending, they require higher taxes, or for any given level of taxes, they require less of some of the sort of spending.

We were not conservative in our projection of interest rates, though. As I say, we make an effort to have all the elements of our projection be roughly in the middle of the distribution of possible outcomes at the time we set the forecast. In fact, market readings of interest rates have declined since we set this forecast in place

in early December, but we think there are both upside and downside risks to the interest rates that we project, and we provide in an appendix in the report our rules of thumb for you and your colleagues to see how much different outcomes for GDP growth or inflation or interest rates would affect budget outcomes. And, naturally, with a debt as large as our debt is, changes in the interest rate that the Treasury pays on that debt can have very large effects on the deficit.

Chairman ENZI. Thank you. One of my concerns with all of this is that when I first came to the Senate, I went on a trip to Korea with Senator Lieberman, and it was at a time that Korea was having some tremendous financial difficulties and the International Monetary Fund stepped in to help them and they outlined a plan. And, it happened to be election time, too, so Senator Lieberman and I got to meet with both of the potential leaders for them, and our job was to explain to them the need for them to follow the IMF plan exactly to get their debt reduced and to stay in line. And, we were so persuasive, they immediately went on television and said, "If I get elected, I am going to change every one of those articles." Their money plunged 18 percent per day for three days and they came back on television and said, "We are going to follow it precisely."

So, that is some of my background, and you noted my concern about the debt and we have discussed the problem of the large and growing interest costs. But, what about the debt itself? Is debt at the levels projected in the report a danger to the country and my grandkids' future, and could you explain that.

Mr. ELMENDORF. Yes, Mr. Chairman. Under normal economic conditions, when the Federal Government borrows more money, it is making it more difficult for other people to borrow money and, thus, tends to crowd out some capital investment. And, it is capital investment that helps over time to boost GDP and to boost wages and incomes.

So, on an ongoing basis—again, under normal economic circumstances—the high level of debt that we have is reducing wages and incomes relative to what they would otherwise be. We are still on an upward path of wages and income, but we would—with less debt, we would be on a stronger upward path.

Also, as we have said a number of times, there are risks associated with high levels of debt. You cannot tell just when that risk might hit. But, for example, if there were another financial crisis or severe recession or international events to which you and your colleagues wanted to respond with government resources, the more debt you have going into that kind of situation, the harder it is for you to respond. Additionally, there is a risk of a fiscal crisis in which investors would become unwilling to hold Treasury debt, except at extraordinarily high interest rates.

There is no way for our economists to predict what level of debt might cause such a crisis to occur, and other countries that have gotten into that sort of situation have gotten there through a variety of circumstances. So, we do not know of any particular tipping point, but we think the risk is higher, the higher the level of debt is relative to the size of the economy.

Chairman ENZI. Thank you, and my time has expired.

Senator SANDERS.

Senator SANDERS. Thank you very much, Mr. Chairman.

I think, before we go forward and talk about where we want to go, it is important to know how we got to where we are today, because I hear a lot of my Republican friends saying, well, you know, we have got this deficit. We are going to have to cut Social Security, Medicare, Medicaid, education, nutrition, infrastructure, whatever. But, I think it is important to know how we got to where we are.

Dr. Elmendorf, am I correct in remembering that in January of 2009 [sic], when President Clinton left office, we had a $236 billion surplus?

Mr. ELMENDORF. That sounds right, Senator.

Senator SANDERS. Okay, and that the CBO projected a ten-year budget surplus of $5.6 trillion?

Mr. ELMENDORF. Yes, Senator.

Senator SANDERS. Well, I think, Mr. Chairman, we might want to figure out how we went from projections of a huge surplus into significant deficits.

Dr. Elmendorf, is it fair to say that one of the reasons we saw that transition is that under President Bush, we went to war in Iraq and Afghanistan, but we forgot to pay for those wars, that important part?

Mr. ELMENDORF. Well, the forgetting, I cannot speak to, Senator—

Senator SANDERS. Well—

Mr. ELMENDORF. —but relative to CBO's projections in early 2001, the high levels of defense spending was a significant factor in why the deficit was much—

Senator SANDERS. Well, I asked that question as maybe the major deficit hawk on this committee. See, I did not vote to go to that war in Iraq. I did not go to war in Iraq.

Now, what about the tax cuts that were initiated by President Bush? Did they have any impact on the deficit?

Mr. ELMENDORF. Yes, a very large effect, Senator.

Senator SANDERS. Oh, they did have to cut education, when families cannot afford to send their kids to college. I think that, frankly, that set of priorities does not make sense to me.

Dr. Elmendorf, given the fact, as I think we all know, that the wealthiest people in this country have become much wealthier in recent years and their tax rates have gone down, is it not correct that if we did nothing more than restore the income and capital gains tax rates to where they were in 2000 for the wealthiest two percent of Americans earning $250,000 a year or more, that we could raise more than $200 billion over the next decade?

Mr. ELMENDORF. Senator, we have not done an estimate of that that I know offhand. I certainly agree that the changes you describe, a significant amount of additional revenue would be collected. But, I think to actually get a specific number, you would have to ask for an estimate from the Joint Tax Committee—

Senator SANDERS. Okay. Let me ask you this. According to a November 2014 CBO report, the income of the wealthiest one percent of Americans has risen 200 percent since 1979 at the same time that their income tax rates have fallen. Is that a fair statement?

Mr. ELMENDORF. Yes, Senator.

Senator SANDERS. Okay. So, I think what the debate that we are going to have in this committee, and I think it is going to be a very interesting debate, as the Chairman indicates, is one of national priorities, and that is that at a time when the wealthiest people are doing phenomenally well, when corporate profits are at an all-time high, do we ask those people who are doing extremely well to start paying their fair share of taxes so that we can invest in our economy and reduce the deficit, or, in fact, do we continue the war against the working families of this country and low-income people by cutting the programs that they desperately need, and that is a strong philosophical division and I look forward to some very interesting debates on that issue.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Next will be Senator Crapo, and then Senator Stabenow.

Senator CRAPO. Thank you, Mr. Chairman.

And, just briefly, in response to some of the comments of Senator Sanders, back in the time frame he was talking about, did we not also have a terrorist attack around 9/11?

Mr. ELMENDORF. Yes, Senator.

Senator CRAPO. And, did we not have a stock market crash right in that time frame, as well?

Mr. ELMENDORF. We did, Senator.

Senator CRAPO. And, were not both of those events, both on the spending and the revenue side, pretty significant to our budget circumstances?

Mr. ELMENDORF. Yes, Senator. As I said, the military response in the 2000s was a costly one. We are not in a place to judge the strategic effect, but certainly it was costly, as we describe in our report.

Senator CRAPO. I understand. I just wanted to be sure that a little bit more of that picture was painted.

Let me talk for a minute about the interest issue, which Senator Enzi brought up with you. As I understand your report, essentially, over the budget window that you are reporting on, the interest costs will go from about 6.5 percent today to about 13.5 percent at the end of the budget window, is that correct?

Mr. ELMENDORF. That is—I guess as a share of total spending, Senator—

Senator CRAPO. Yes.

Mr. ELMENDORF. —that sounds right to me.

Senator CRAPO. Yes. I think that would be as a share of total spending.

Mr. ELMENDORF. Yes.

Senator CRAPO. And, just to give that number a little bit of perspective, that means that in about four or five years, the share of total spending that interest represents will exceed the share of total spending that our defense spending represents, is that correct?

Mr. ELMENDORF. Yes, Senator.

Senator CRAPO. And, by the end of the budget window, it will exceed that by a significant amount.

Mr. ELMENDORF. Yes, Senator, that is right.

Senator CRAPO. And, as we look at seeing the interest costs alone on our debt rising to such an increasing level of our overall spending capacity, does that not crowd out all other, not just defense, but all other kinds of spending options that the Congress has?

Mr. ELMENDORF. Well, it can either reduce other spending or lead to higher tax revenue or lead to a larger deficit for some period of time. But, you are right, Senator, that it makes those other choices more difficult, so larger—

Senator CRAPO. So, we either have to raise taxes or cut spending elsewhere.

Mr. ELMENDORF. Yes.

Senator CRAPO. Or, figure out a way to reduce interest costs, which would be where I want to go next. It seems to me that we should talk for a minute about the impact of the debt on our GDP. Your report indicates that the potential output and GDP growth after 2017 will be noticeably less than the average growth of the 1980s and 1990s, and also that the debt increasing as a percentage of GDP in the latter half of the decade to levels—it will increase to levels that are higher than they have been since 1950, is that correct?

Mr. ELMENDORF. That is right.

Senator CRAPO. My question is, what effect does that increasing debt have on our economy and our potential output and GDP?

Mr. ELMENDORF. So, as the economy continues to improve and moves along in the second half of the coming decade, that higher—that level of debt will lead to lower capital investment and lower incomes than would be the case if debt were lower, all else equal.

Senator CRAPO. The fact is, the debt is a drag on the economy.

Mr. ELMENDORF. When the economy is functioning normally, Senator. As I suggested in my earlier answer, in periods when the economy is constrained by shortfall of demand for goods and services like we have had the last several years, then government borrowing is a stimulus to the economy. But, over longer periods of time, when the economy tends to be closer to full employment, then large debt is a drag on the economy.

Senator CRAPO. If I am understanding what you are saying, you are saying that stimulus spending in the short term can boost economic strength, but in the long term, because it is added to the debt, it is not taxed and paid for, then it becomes a drag, is that correct?

Mr. ELMENDORF. Yes. That is right, Senator.

Senator CRAPO. I guess my question basically is, can we simply spend ourselves into prosperity on a continuous basis with borrowed money?

Mr. ELMENDORF. Umm—

Senator CRAPO. Can we just continue to drive the debt up and use that short-term stimulative impact of borrowed money to keep ourselves always in a positive economic posture?

Mr. ELMENDORF. No, Senator. It is not feasible to continually have debt rising relative to the size of the economy, because eventually, people will become more skeptical about the government's ability and willingness to pay that.

Senator CRAPO. And then we face the question as to whether they are willing to buy our debt.

Mr. ELMENDORF. Yes. That is right, Senator, at some point.

Senator CRAPO. And there, I know, have been a number of economists who have tried to find that tipping point. You indicated that we really do not know when it is. But, can we have any kind of general ideas?

Mr. ELMENDORF. Senator, we really do not know. I think the best thing we can say is that the United States has rarely had Federal debt as large relative to the economy as it is now and as we project it to be over the coming decades under current law, and, thus, we are in mostly uncharted territory, and that is part of why there is a risk. But, because it is uncharted territory for us, economists just do not have much to offer about what might happen when.

Senator CRAPO. Well, I would just say—I know my time is running out—I am one of those who thinks that the risk is very high and that we are in very dangerous uncharted territory. And, we continue to get the answer that we cannot take the fiscally responsible steps that we need to take on both the tax and the spending side of the budget because we need to continue to stimulate this difficult economy with stimulative spending on borrowed money in order to make it strong. My point in my questions to you was just that there comes a time, and I think the time is here, when we have got to recognize that we cannot just continue the stimulative spending theory at the cost of continuing to drive up this massive debt. Thank you.

Chairman ENZI. Senator Stabenow.

Senator STABENOW. Thank you very much, Mr. Chairman, and congratulations. I am looking forward to working with you.

Lots to talk about, and it really does come down to a difference in approach about how you grow the economy. I would just say to my good friend who just spoke that we really have not been using a stimulative approach now for a few years. We have been doing sequestration and cutting and not funding infrastructure and watching student loan debt go up and not investing in things. So, it is an interesting debate.

I guess what I would say is that we, in real simple terms, we should do what works and we should look at the past to know what works. I was around in the House of Representatives in the 1990s under the Clinton administration when we balanced the budget for the first time in 30 years. I had only been there six months, and so I thought it was pretty good, after six months, I had balanced the budget. But, it was because of an arrangement that asked those at the top to pay a little more and also to invest in education and innovation and, basically, a middle class economy.

Then we went to a different approach under the Bush administration, saying, let us give it all to those at the top, two different large trickle-down tax cuts to the wealthiest Americans hoping it would trickle down to everybody else. In the meantime, we all know about the wars that were not paid for. Go to war, do not pay for it. The President says, go shopping, because consumer spending is obviously very important—if you have a job and money in your pocket. A whole range of things happened, including not watching Wall Street, the biggest collapse since the Great Depression, and we saw what happened.

So, President Obama comes in and, again, turns around and says, we are going to protect American jobs in the auto industry and manufacturing and we are going to make sure we do not lose making those things in America. We have asked the top to pay a little bit more. There was an outcry the world would end. Instead, we have brought down the yearly deficit more than two-thirds. The economy is growing again.

And, now, the question is, is everybody going to benefit from that or just those at the top, and that goes to the question, I believe, of investing in education and innovation and creating a way to stop the deficits that, frankly, Senator Sanders talked about, which focus on blocking opportunities for people who work hard to get into the middle class.

And, in your report, Director Elmendorf, you talked about, of course, consumer spending, and people cannot spend if they do not have money in their pocket, and if they do not have a job that pays well, they are not going to have money in their pocket. So, my question to you goes to a different way of looking at this in terms of how do we have resources? How do we make sure we are responsible, we are paying for the things that we are doing as a country, but do it in a way that does not hurt folks that are trying very hard to get into that middle class.

One way is to ask those who are abusing the system through tax loopholes to pay their fair share for public services, individuals or businesses. On the business side, I have a bill called the Bring Jobs Home Act that just addresses one small policy, that basically says if you pick up and move the factory, the taxpayers are not going to pay for the move. It ought to be simple to pose that. We know about inversions. We know about other techniques, as well as individuals.

So, my question to you, Director Elmendorf, is if we actually closed those loopholes, both on the individual and the business side, so that everyone was contributing to the public services they benefit from, like breathing the air and drinking the water and driving on the roads and all of the other things that we, as Americans, benefit from, what impact would that have on tax receipts?

Mr. ELMENDORF. Well, Senator, if you reduced or eliminated certain deductions or exclusions from income or tax credits or other tax expenditures, as many of them are known, then that would raise revenue, all else equal. How much effect it would have on revenue, of course, would depend on the specifics of the provisions that you changed and on whether there were changes in tax rates or other elements of tax provisions that were altered. So, the specific outcomes would depend on the specific policy choices.

Senator STABENOW. Taking inversions as an example, or the fact that we have seen over the years—when Senator Conrad was here, he always showed us the picture in the Cayman Islands, I think, it was up to 18,000 businesses that had the same address, in the same building. Making sure that they at least had to pick different buildings in the United States, what are we talking about in terms of savings that we could put into rebuilding our roads and infrastructure and investing in our children's schools?

Mr. ELMENDORF. Yes. So, Senator, we highlight the role of tax expenditures in the revenue chapter of the outlook, because, as you

know, they are very large in magnitude but do not necessarily get the scrutiny in the budget process that spending programs of comparable magnitude receive. By our estimates, the total tax expenditures for the individual income tax, the payroll tax, and corporate income taxes is about $1.5 trillion in 2015 alone. That is almost as much money as is collected by the individual income tax. It is a lot more than is spent on any of the largest government programs.

So, there is a tremendous amount of money which is being used by the Federal Government to support particular individuals or particular activities, and that is up to you and your colleagues to decide whether you think all those things are appropriate, just as that is the case for other tax provisions and for spending programs and so on. But, we did try to bring—make sure that—

Senator STABENOW. Thank you.

Mr. ELMENDORF. —people are aware of the magnitude.

Senator STABENOW. And, Mr. Chairman, I hope we will have that—

Chairman ENZI. Your time—

Senator STABENOW. Yes. I hope we will have that discussion. I am not advocating we close every one of the—change that tax policy, but $1.5 trillion in spending through the tax code seems to me a worthy place for us to scrutinize, as well. Thank you.

Chairman ENZI. Senator Ayotte.

Senator AYOTTE. Thank you very much.

I would like to understand the effects of a higher average interest rate on the fiscal state of the country. Including if interest rates were one percent higher than in your baseline, what would that do to the baseline projected deficit over the period of 2016 to 2025. And can you tell us how you estimated the rise in interest rates here and whether that was a conservative estimate or not, because I think it is important for the American people to understand that as interest rates go up, even by one percentage point, the amount of money we owe goes up very dramatically. Could you help us with that, Dr. Elmendorf?

Mr. ELMENDORF. Yes, Senator. So, we provide in our report rules of thumb to help you and your colleagues understand the effects of different economic outcomes, and we estimate that if interest rates were one percentage point higher each year throughout the coming decade, the deficit would be $1.7 trillion larger. And, conversely, if interest rates were one percentage point lower per year, the deficit would be $1.7 trillion smaller.

Our projection of interest rates is not conservative in the sense in which I think you mean it. We try to have our projections be in the middle of the distribution of possible outcomes, recognizing a great deal of uncertainty. But, we try to end up with projections for which the upside risks and the downside risks are roughly balanced in all of our projection, on both the economy and the budget.

So, we think there is a chance interest rates will be higher than we project, but also a chance they will be lower, and, in fact, market interest rates in the six weeks since we closed this forecast have moved down notably. So, our forecast right now, actually, is a little above what the latest reading on market interest rates would suggest, although we do not put too much weight in any particular reading because interest rates are so volatile.

Senator AYOTTE. Obviously, if the interest rates go up one percentage, we owe over a trillion dollars more in terms of the debt. In terms of looking at the projected outlook, if you combine spending for Social Security, major health care programs, which would include Medicare, Medicaid, the Children's Health Insurance Program, and subsidies for health insurance purchased through the exchanges created by the Affordable Care Act, and net interest on our national debt, it accounts for nearly 85 percent of the total increase in outlays over the next decade. Would you agree with that?

Mr. ELMENDORF. That sounds roughly right to me, Senator. I do not have that precise calculation. But, we do show in our report that the overwhelming share of the rise in outlays is concentrated in just this handful of programs.

Senator AYOTTE. As we look at putting our country on a fiscally sustainable path, I look at your projected outlook where deficits go down, but then they go back up to over trillion-dollar deficits in 2025. And so looking at the fiscal state of the country in the long term, is there any way we can put ourselves on a fiscally sustainable path without considering at how we preserve those programs? As you know, the Trustees have said, especially for Medicare and Social Security, that they will become insolvent. The Disability Fund is looking us right in the eye in terms of insolvency. Without making some bipartisan reforms to these programs, can we do it without looking at those issues?

Mr. ELMENDORF. I think—I think you and your colleagues will need to either make significant changes in those large programs or significant changes in our tax code—or both. It is very hard not to tackle at least one of those, because, as you know, under current law, spending on the other government programs is shrinking relative to the size of the economy to levels that we have not seen in our lifetimes. But, whether you would choose to make changes by focusing on these large spending programs or by focusing on tax revenues—

Senator AYOTTE. Could you do it—

Mr. ELMENDORF. —that is really up to you, Senator.

Senator AYOTTE. If you did it with tax revenues alone, how big is the tax increase?

Mr. ELMENDORF. You would have to do—well, to balance the budget, say, in 2025, which the Chairman expressed as his goal, we think in 2025 that tax revenues will be about 20 percent smaller than spending. You would have to raise—

Mr. ELMENDORF. You would have to cut spending by 20 percent or raise revenues by 20 or 25 percent or some combination—

Senator AYOTTE. But, my point is, even as we look at balancing over the decade, that still does not address the long-term fiscal health, issues of Social Security, Medicare, the Disability Fund, really, the long-term viability for people who rely on the programs, and also the fiscal sustainability for the country. Would you agree with that?

Mr. ELMENDORF. Yes. I think it makes good sense for you to be looking further ahead. And, as you know, we provide a long-term budget outlook once a year that looks beyond the ten-year window, because, as you say, some of the significant—the pressures that are happening over the coming decade do not end in the 11th year or

the 12th year. They intensify over time, because the Baby Boomers will continue to retire and health care spending will continue to grow. So, the problems are long term in nature, I think that is absolutely right. And, when we look to alternative paths for the budget in our long-term budget outlook, we look not just at changes in the first ten years. We extrapolate those over longer periods of time.

Senator AYOTTE. Thank you.

Chairman ENZI. The Senator—yes. Senator Whitehouse.

Senator WHITEHOUSE. Thank you very much, Chairman, and welcome to your Chairmanship. I appreciate working with you.

Mr. Elmendorf, I think it is important, and I agree with my colleagues that we need to address the long-term debt that we carry right now. My belief is that solving that problem with cuts while in a recession has been proven by experience to be a failed strategy. The President has said it is time to turn the page, and so maybe it is time to start to look at not just supporting the economy immediately, but also beginning to look at the long-term debt and deficit issues.

But, I would urge my colleagues, if they wish to be taken seriously on the debt and deficit warnings that they make—that this is a high-risk proposition, that this is dangerous to the country, that this is unsustainable—then their priorities should match the warnings. And, when it is a greater priority to protect the folks who make millions of dollars a year and who in recent years have paid lower tax rates than truck drivers and hospital orderlies and brick masons, it is hard to take seriously the warning or the sincerity of the warning. When they are asked whether the—when they take the side of the big oil companies to protect their subsidies instead of taking serious action against the debt, again, it is a matter of priorities and it makes it hard to take it seriously.

We have tried to address the problem of the big multinational corporations who get tax advantages from offshoring American jobs or from offshoring American intellectual property, and we are always stymied and blocked in trying to do that. Again, that would help the debt and it would help the deficit. And, the relentless opposition we get, again, is a signal of priorities.

And, finally, protecting corporations who pay zero or single-digit taxes—zero or single-digit tax rates—many of whom are declaring enormous revenues—again, if protecting that is a priority above addressing the debt and deficit, it makes it hard to take seriously those warnings.

If discussion of the debt and deficit is nothing more than a leverage point, a fulcrum to attack spending programs that the Republican Party has long opposed, like Social Security and Medicare, we are going to have a problem. But, if we are serious about it—and we should be, because we have just heard from Director Elmendorf that there is $1.5 trillion that we spend through the tax code through all these deals, and we have heard from our new Chairman that the actual appropriated spending is only $1.1 trillion, we actually spend more out the back door of the tax code than we do through appropriations, so if you want to look at this as a serious debt and deficit problem, to put on your blinders and say, we are only going to look at the appropriated spending side and we are

never, never, never, never, never, never going to look at the revenue side, first of all, it does not make you look serious, and second of all, it drops the major part of the deficit reduction opportunity, the $1.5 trillion part, right out of the toolbox. And, I do not think that is sensible, and I do not think that is what the American people want, and I do not think that is fair.

So, one last thing on this. You have said before, Dr. Elmendorf, that health care is a very big part of our debt and deficit problem going out. Is that still true?

Mr. ELMENDORF. Yes, Senator.

Senator WHITEHOUSE. And, is it not also true that since the passage of the Affordable Care Act, the projections for Medicare, Medicaid, and other mandatory health programs have fallen by $2 trillion for the coming decade—

Mr. ELMENDORF. They have fallen quite a bit, Senator—

Senator WHITEHOUSE. —in your baseline?

Mr. ELMENDORF. They have fallen quite a bit. I do not have those particular numbers—

Senator WHITEHOUSE. But, $2 trillion is pretty close. If I do not have it to the dollar, I am in the right order of magnitude.

Mr. ELMENDORF. I think that is right. We made a substantial downward revision to our projection of Federal health care spending.

Senator WHITEHOUSE. Twenty-twenty alone is $122 billion in reduced anticipated spending.

Mr. ELMENDORF. That sounds right, Senator.

Senator WHITEHOUSE. Now, does any of that have anything to do with any of the programs that were launched by the Affordable Care Act?

Mr. ELMENDORF. Well, perhaps, Senator. It is hard for us to know, right now. So, when the Affordable Care Act was enacted, we built into our baseline projections our best estimate of the—at that time of the effects of the Affordable Care Act. So, since then, various things have happened—

Senator WHITEHOUSE. Since my time has run out, let me jump to the next question. Secretary Burwell has just announced new programs to change the way payments are made. Do you expect that that will have a good effect?

Mr. ELMENDORF. I have seen the announcement, Senator. We have not had time to study it yet. I am sorry.

Senator WHITEHOUSE. When you have, would you let us know? Thank you, Chairman.

Chairman ENZI. Senator Corker.

Senator CORKER. Well, thank you, Mr. Chairman. I will say, I have never attended a Budget meeting before, and I assume it is only on the first day that people make partisan comments, and then after that, we move towards trying to solve the problem. So, I am looking forward to that.

Mr. Elmendorf, in your assumptions, you assume that the extenders, the tax extenders that we keep extending, will not be extended, is that correct?

Mr. ELMENDORF. That is right. We follow current law, Senator. Of course, it is not an assessment by us of the probabilities of things happening. We follow current law.

Senator CORKER. And you also assume that we are actually going to enact SGR as it is written?

Mr. ELMENDORF. Again, we follow current law, in which—

Senator CORKER. No, I understand. I mean, that is what you are supposed to do.

Mr. ELMENDORF. Yes.

Senator CORKER. So, in essence, we are probably a trillion dollars, at least, on those two topics, worse off than your projections say, is that correct?

Mr. ELMENDORF. If Congress were to freeze Medicare's payments to doctors, that would raise the deficit by about $130 billion over the coming decade. And, if you were to extend all the expiring tax provisions, that would add about $900 billion to the deficit directly, both of them, and then there will be interest costs alongside of that, as well.

Senator CORKER. So, as a famous Republican politician once said, "Deficits do not matter," but they do matter, do they not?

Mr. ELMENDORF. Yes, Senator, they do.

Senator CORKER. And, the reason they matter is they, as you have mentioned, once you get to a full recovery, they affect economic growth, is that correct?

Mr. ELMENDORF. Yes. They also affect it in weak conditions, but in a rather different way.

Senator CORKER. And, so, deficits and debt, over time, actually directly affect the standard of living of the American people, is that correct?

Mr. ELMENDORF. Yes, Senator.

Senator CORKER. Very directly.

Mr. ELMENDORF. I mean, economists, I think, have a very strong view about that. Whether people see that, I think, is less clear. But, I think, the effect seems to us to be quite strong.

Senator CORKER. So, our inability to somehow figure out a way collectively to solve this problem, and being unwilling, if you will, to take the steps that most of us know we have to take, really is hurting the standard of living of Americans.

Mr. ELMENDORF. I think, over time, the standard of living would be higher than otherwise if deficits were small—

Senator CORKER. Thank you. Deficits affect the standard of living of Americans. Debt affects the standard of living of Americans. Tell me the impact, from your standpoint, of increased taxes on the economy and on the standard of living of Americans.

Mr. ELMENDORF. Well, so the direct effect, of course, if people pay higher taxes, they have less after-tax income. And, as you know, Senator, if the government cuts benefits to people, then they have less income for that reason, as well. That is why this deficit problem is a hard one to confront, because people pay taxes and they also receive the benefits, and as Senator Ayotte noted, the vast majority of the growth in spending on Federal outlays is in benefit programs. And, so, you and your colleagues face a difficult set of choices, I think.

Senator CORKER. But, the actual, just the net effect of taxes themselves, tell me the effect that it has on economic growth, increased taxes.

Mr. ELMENDORF. Oh, so higher tax rates on work or on saving will tend to discourage work and saving, and that would tend to reduce economic growth. And, in our modeling of the effects of changes in fiscal policy on the economy, we try to capture the effects of changes in deficits, but also the effects of changes in incentives through the tax code as it affects work and saving, and, in fact, transfer programs can have effects on incentives, as well, and we try to capture those in our modeling, also.

Senator CORKER. So, debt and deficits hurt the standard of living of Americans by slowing economic growth, and increased taxes on work—and I think you are very specific there, on work—affect the standard of living of Americans because they also slow economic growth. So, we have quite a challenge, do we not?

Mr. ELMENDORF. Yes, Senator.

Senator CORKER. I hope we will come together and figure out a way of solving that.

Have we had a situation, and you project in this budget window that net interest spending—and someone has already alluded to this—will be more than defense spending—have we ever had a situation like that in the history of our country?

Mr. ELMENDORF. I do not think so, Senator, but I can r budget window and you look at the mandatory spending component which has been put in place by both sides of the aisle, the issues relative to debt and deficits—have we ever faced a situation like this that you can remember with more difficult choices?

Mr. ELMENDORF. No, Senator. I think what is strikingly different now from the past discussions of this topic ten, 20 years ago—at which point the demographic changes, of course, were foreseen—what is different now is that our debt is already more than—equal to more than 70 percent of GDP, and that is a level of debt that we have only seen in this country for a few years around the end of the Second World War, and that makes the situation quite different from other times at which this question has arisen.

Senator CORKER. So, Mr. Chairman, I know everybody is sort of staking out their territory today and sort of taking potshots. I do look at this Budget Committee as being a serious committee and I hope that over the course of the next two months, we will figure out a way to come together and actually deal with these issues in a way that is meaningful so that our lack of action does not continue to hurt the American people. Thank you.

Chairman ENZI. Thank you.

Next will be Senator King, then Senator Johnson.

Senator KING. Thank you, Mr. Chairman. Welcome to the Chairmanship. I look forward to working with you.

And, Dr. Elmendorf, I just want to thank you for your extraordinary service. I have served on this committee now for going on three years and you have done such a great job of giving us unbiased and very thoughtful and thorough advice. I want to thank you for that.

I think we have got universal agreement around this table on one thing, and that is the debt is a problem and the interest rate is a looming serious problem. We have all made statements about how interest rates, if it goes up one—a one percent increase in interest rates costs $180 billion a year, and that is going to sink us,

and it is money that goes for nothing. It does not buy anything. In fact, what it does is buy airports in China, because that is where the interest, or a significant amount of the interest, is going.

So, the question is not is debt and deficit a problem, the question is how do we deal with it? There are several ways. One is the Budget Control Act and the sequester. My problem with that, and, I think, one of the most important charts in your material is on page 62 that shows the outlays by types of expenditures over history, and what that shows is that discretionary spending, including defense and non-defense, is at virtually an all-time low and headed for certainly an all-time low as a percentage of the economy. And, yet, most of our budget cutting effort around here seems to focus on that relatively small target.

And, the real increases—on page 17 you have a chart of what is driving the increases—the real increases are in health care and in other mandatory programs. When we are cutting Head Start or the defense budget in order to try to solve this debt and deficit problem, it is like attacking Brazil after Pearl Harbor. It is a vigorous reaction, but it is the wrong target. The real growth, if you look at your chart, is in mandatory spending, and then there is a fundamental question about revenues.

You mention that the historic level is 17.5 percent. We are now at about 18.5. The question that we have to grapple with as public officials here is 18.5 percent or 18 percent or 19 percent, what is the right number, given the demographics of America in 2015 through 2030. We cannot keep the commitments we have made to people who are retiring and maintain any level of discretionary spending without some additional revenues. The arithmetic simply does not work.

And, I think an interesting debate here would be what is the right level? Is it 20 percent of GDP? If you add the numbers together on your projections, it is 22.3 percent. That is 14.2 for mandatory, 5.1 for discretionary, and 3.0 for interest. So, anything short of 22.3 percent equals a deficit and the problem continues to get worse.

So, it seems to me we have really got to look at the—and be realistic about what is happening, because if we do not deal with both the growth of mandatory spending, which is mostly in health care, and look at the revenue side, we are on a path that there is really no way out, unless the American people want us to drive discretionary spending, including national security, to zero. That is the direction that we are headed.

So, I would go back to when President Reagan was President. Ten percent of GDP was discretionary spending. We are headed for 5.1, in half of what it was when Reagan was President. The difference, interestingly, in 1990 between discretionary and mandatory was one percent. Nine percent was discretionary, ten percent was mandatory. Those two lines are separating dramatically and that is the problem.

But, to think that we can solve it entirely by revenues, I think, is unrealistic. To think that we can solve it entirely by cutting programs that are benefitting people who we made commitments to is unrealistic. There has got to be—somebody around here has got to

be saying, here is the arithmetic and here is how we have to solve this problem.

If you can find a question in there, Dr. Elmendorf, you are better than I.

[Laughter.]

Senator KING. But, would you agree that the overall analysis is that we have got to look at—you know, it is Willie Sutton. You have got to go where the money is, and the money is in mandatory spending and in revenues based upon the change of demographics.

Mr. ELMENDORF. Yes, Senator, we think—we agree with that, that given how low discretionary spending is already on track to be relative to our historical experience, there seems no way around the country agreeing to either cut some of the large benefit programs relative to the benefits promised under current law, or to increase tax revenues well above the historical share of GDP, or to do some combination of those changes.

Senator KING. But, on the cutting side, I want to emphasize, we do not have to necessarily cut. We have to get control of health care costs, which we spend twice as much per capita than anybody else in the world. And, if we could just control that, it would solve a great deal of this problem. It is not necessarily cutting fees to doctors or cutting—you know, saying we are not going to pay as much, we have got to get at the underlying structural costs that are driving these extraordinarily high health care costs.

Mr. ELMENDORF. So, yes, Senator, if there were ways to—when I refer to cutting benefits in the programs, I mean cutting the spending for those benefits. If there are ways to provide comparable benefit as viewed by a beneficiary at lower cost, then that would help. I think there is widespread agreement among analysts that our health care system should move in the direction of paying for care, not per unit in the way that encourages volume, but by paying for keeping people healthy at the lowest possible cost.

But, once you get beyond that general principle, exactly what changes in Federal laws and Federal policies could achieve those goals is very unclear, and part of what was put in place in the Affordable Care Act is a collection of specific changes and also some mechanisms to experiment with other changes, and those experiments are underway. But, just which ones will pan out and how well is very hard to know at this point.

Senator KING. Thank you, Dr. Elmendorf. I appreciate it.

Thank you, Mr. Chairman.

Chairman ENZI. Senator Johnson.

Senator JOHNSON. Thank you, Mr. Chairman.

Let me provide some of the arithmetic. I have passed out a one-page income statement for the United States, for our Federal Government, over 30 years. I think that is—if you are going to solve a problem, you have to properly define it. When we keep talking about a ten-year budget window problem, I think we dramatically understate the problem. And, so, what I have been doing a lot of work with is your CBO alternate fiscal scenario. Rather than—that is always laid out as a percentage of GDP, so I have turned it into numbers, and then I have taken those numbers and put them onto a one-page income statement to highlight really what the problem

is. So, I think you have got a copy of that income statement there now.

Mr. ELMENDORF. Yes, Senator.

Senator JOHNSON. I have highlighted the areas. It is pretty stark. Over the next 30 years, Social Security will pay out $14.6 trillion more in benefits than it takes in the payroll tax, according to CBO. Medicare will pay out $35 trillion more in benefits than it takes in the payroll tax over the next 30 years. And, then, we will pay out to our creditors $71 trillion. That all totals up to $121 trillion. The entire deficit over the next 30 years is $127 trillion.

Let me just lay out how that occurs by decade. Eight trillion dollars the first decade, $31 trillion the second decade, $88 trillion the third decade. Now, my little baby girl just turned 31, and I can tell you, that went by like that.

And, just in case people think the alternate fiscal scenario is way out there, just way overstates the case, if you compare the percentage of spending to GDP versus our 20-year average for all the entitlements over the last 20 years, it has been about 8.3 percent. Over the next 30 years, according to this scenario, it is about 13.5, and everybody is pretty much in agreement in terms of the entitlements. Defense, we spent $3.9 trillion over the last 20 years. The CBO's alternate fiscal scenario says we will spend 3.5, so it is actually under the 20-year average. All other spending, we spent about 6.7. The alternate fiscal scenario is six percent.

So, if you look at the past and project to the future, even your alternate fiscal scenario shows spending less than we have spent over the last 20 years. So, I just want you to comment on, is that basically your understanding of what the 30-year projection is according to CBO's alternate fiscal scenario?

Mr. ELMENDORF. As you understand, Senator, I cannot actually absorb or check all these numbers sitting here—

Senator JOHNSON. No, I understand, but—

Mr. ELMENDORF. —but the thrust of your remarks, that the big pressure on outlays is coming from Social Security and the health care programs, and then because the deficit is an accumulating debt, interest on the debt, that is right, Senator.

Senator JOHNSON. And, so, again, that is—again, I am not saying these are the numbers, but largely true. Eight trillion dollars the first decade, $31 trillion the second, $88 trillion the third, $127 trillion. Quick, put that in perspective. The entire net private asset base of America today, every asset held by every household, every business large and small, is about $106 trillion. So, there is a problem that is completely unsustainable, but when we are just focusing on a ten-year budget window, somewhere in the $7 to $8 trillion deficit, we are not even beginning to understand the real depth of the problem, are we?

Mr. ELMENDORF. Senator, no. I think that looking over the longer term is very important for you and your colleagues to see the real challenges, as Senator Ayotte and others have commented. I agree.

Senator JOHNSON. So, let me focus in on Social Security, because you might be a little bit more familiar with those. The $15 trillion in Social Security over the next years, that actually breaks down to about $1.5 trillion the first decade, about $4 trillion the second decade, about $8 trillion the third. Now, what happens when the

Social Security Trust Fund runs out of money? By law, what happens?

Mr. ELMENDORF. By law, then the benefits can only be paid up to the amount of money coming into the fund, which would be a good deal less than the benefits that are in current law.

Senator JOHNSON. So, the Disability Trust Fund is going to run out, according to your current paper here, about 2017. So, according to current law, unless we do something, according to current law, how much would those benefits be reduced by, approximately?

Mr. ELMENDORF. I think it is around a 20 percent cut in Disability Insurance benefits in early fiscal year 2017, under current law.

Senator JOHNSON. And, then, when the Trust Funds run out of the retirement benefits, right now, somewhere around 2033, what is the projection in terms of reduction—by law, the reduction in benefits when we run out of that Trust Fund?

Mr. ELMENDORF. Again, Senator, I think the reduction is on the order of about 20 percent relative to current law benefits.

Senator JOHNSON. And, again, I appreciate during the special conferences we had last December—was it last December? I think so. I appreciate the fact that you were very honest in your assessment of the value of that Trust Fund. It is an asset to the—those U.S. Government bonds are assets to the Trust Fund, but they are a liability to the Treasury—

Mr. ELMENDORF. Yes.

Senator JOHNSON. And, to consolidate the Federal books, that nets to zero, right?

Mr. ELMENDORF. Yes.

Senator JOHNSON. So, the Trust Fund has no value to the Federal Government, dollar value, correct?

Mr. ELMENDORF. Yes. As you say, it has legal meaning for the Trust Fund, but it is—on the Federal Government, taken on a consolidated basis, which is the way that we focus on the Federal Government, then it nets out to zero.

Senator JOHNSON. So, of $15 trillion, we really have nothing, really, in the Federal Government to pay those benefits even through 2033 other than that accounting, bookkeeping transfer from the Trust Fund to the Treasury, who then have to go either float more bonds or raise more taxes?

Mr. ELMENDORF. Yes, Senator. What our projection is—you know, what we focus on is the unified Federal budget, and the sources of funds for benefits in a given year is tax receipts in that year or borrowing. And, we show this by focusing not on the Trust Funds, but on the projections of outlays and revenues, including the ones that you used from our alternative scenario.

Senator JOHNSON. Thank you. That helps define the problem. Thank you.

Chairman ENZI. Senator Baldwin is not here. Senator Murray.

Senator MURRAY. Well, thank you so much, Chairman Enzi, Ranking Member Sanders. Chairman Enzi, as the person who held that gavel last year, I wish you luck and I am looking forward to working with you. I also want to acknowledge my friend, Senator Sanders, who I always enjoy working with and who I know will do an excellent job on behalf of working families.

I want to join in thanking our witness today, Dr. Doug Elmendorf, for joining us, and wanted also to take a minute to thank you for your six years of outstanding service to this committee and to Congress and to our country. I am especially grateful for the work you put in last year to help Chairman Ryan and I reach our two-year budget deal. You and all of your hardworking staff, which I really appreciate, have set a standard of professionalism and trust and objectivity, and I cannot tell you how much that meant to all of us, especially, I think, in the recent years when the pressure could not have been higher. Your work to provide us with the best information you could gather, free of politics or partisanship, was absolutely critical.

Mr. ELMENDORF. On their behalf, thank you, Senator.

Senator MURRAY. Of course. And to paraphrase, actually, Senator Moynihan, all of us in Congress are entitled to our own opinions, but you made sure that we were all working off the same set of facts, so I really appreciate the work of you and all your staff.

You know, as this committee meets today, our country is in a far better position than we were two years ago, if all of us will remember. Two years ago, Tea Party Republicans were pushing us from one manufactured crisis to the next and we had debt limit scares that were unraveling our businesses and the markets. We had senseless automatic across-the-board cuts that were set to kick in. We were headed towards a completely absurd and unnecessary government shutdown, and people across this country were really losing faith that their elected officials could not get anything done when it came to our budget and to our economy.

But, when we finally came together at the end of last year, Chairman Ryan and I were finally able to work with many of you on this committee, and I appreciate it, to reach that two-year budget deal that prevented another government shutdown, restored critical investments in education and research and defense and jobs, and reduced the deficit in a balanced and responsible way.

Because of that deal, we were able to pass our bipartisan spending bills for the last two fiscal years and work together on other economic priorities. Senator Isakson and I, for example, passed and got signed into law the bill to expand worker training. And, I think Congress was really able to reach through the gridlock and dysfunction that was so holding us apart and finally move us away from these constant crises that were hurting us and killing jobs and really hurting our economy.

Now, I know we have a lot of work left to do, but I want to remind us that, across the country, businesses have now added 11 million new jobs over 58 straight months of job growth. The unemployment rate is now under six percent and downward trending. The economy grew by over five percent last quarter. Health care costs are growing at their lowest rate in almost 50 years. And, we have reduced the Federal budget deficit by over two-thirds since 2009.

So, I am really hopeful that the new Republican Chairmen in the House and the Senate can now build on that bipartisan foundation that we set in the last two years and not let it all unravel. We all know Republicans control both Chambers of Congress now. I want them to know that Democrats are ready to continue to work across

the aisle on our deficits, fairly and responsibly. And, I know on this side, our highest priority remains job creation and economic growth that will benefit all of our families, not just the wealthiest few, and I am really hopeful that Republicans do invite us to the table to work towards that goal and do not revert back to the crises of the past.

So, Dr. Elmendorf, I just have a minute left, but I did want to ask you, we are heading towards another debt limit deadline. Many of us are going to fight back against any attempts to hold the economy hostage. I am very worried about that. But, I wanted you to talk just a little bit to our committee about the value of us in Congress working together to avoid those kinds of "bad old days," constant manufactured crises. Why is that important for our economy?

Mr. ELMENDORF. Well, Senator, I think it is uncertainty about Federal policies, and particularly uncertainty about whether the Federal debt obligations will be paid in the way that the government has committed to, that kind of uncertainty can really hinder businesses' ability to plan for the future and to make the investments in capital equipment and to make the decisions to hire people that they would otherwise make. So, among the considerations, I think, as you and your colleagues consider policy changes, I think the greater predictability that you can provide to businesses, and also to households and to State and local governments, the better that would be for economic growth. It is very hard for economists to quantify that kind of effect, but we think it is there.

Senator MURRAY. Yes. I think that is a good reminder to all of us as we head into this year and we are facing debt limit deadlines and sequestration that one of the things that we saw happen last time was the economy really halt because of the uncertainty. So, I think it is a cautionary note to all of us to work together and come together and find a path forward and bring that certainty back again and not go to another manufactured crisis.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

In the order that we have established, I want to welcome our newest Senator to the committee and thank him for all the work that he has done in the private sector at balancing budgets, and so you are next, Senator Perdue.

Senator PERDUE. Well, thank you, Mr. Chairman, but I would like to correct you on one thing. If I had ever balanced a budget, I would have been fired every single time. We had to produce a few more dollars on the positive side than the negative side, but thank you. I appreciate the comments so far. I appreciate you being here, Dr. Elmendorf.

I was not prepared for the partisan conversation this morning, but let me give you another take on my perspective. We have got a crisis. This financial crisis, however you look at it, is out of control. Right now, we have the lowest workforce participation we have had since 1978. In the last five years alone, we have allowed four million women to fall into poverty. Two-thirds of small businesses are not hiring or have stopped hiring or pulled back hiring because of the Affordable Care Act. The middle class is worse off today than they were five years ago, by any measure. We have $2 trillion or more stuck in foreign banks because of our archaic tax

system, and we have $2 trillion on the balance sheets of the Russell 1000 that are stuck there because of the uncertainty coming out of this city. We have got a crisis.

I just have a question, two bookkeeping issues. One, what is the total debt today? I understand the net debt is $13 trillion in your numbers. Talk to me a little bit about the Trust Fund debt and why we do not consider that part of our responsibility in terms of talking about total debt that we eventually, over the next 30 or 40 years, have to make right.

Mr. ELMENDORF. So, the measure of debt that we focus on, Senator, is debt held by the public, and we focus on that because we look at the Federal Government on a unified basis. That was a concept of budgeting that began in the late 1960s. It predates CBO.

Senator PERDUE. When we had much lower debt, by the way.

Mr. ELMENDORF. And, by looking at the Federal Government on a unified basis, then financial transactions between pieces of the government or debts owed between pieces of the government, we do not give that priority to. So, in our analysis, we look at the total outlays of the Federal Government, the total revenues of the Federal Government, and the amount the Federal Government has to borrow from the public to fill the gap between outlays and revenues. So, we focus on Federal debt held by the public, but we also do projections of and report to you other concepts of debt, including debt held by the public minus financial assets held by the government and gross debt and debt subject to limit, which is quite close to gross debt.

Senator PERDUE. So, the 229 interest payment we have this year, what would be the total interest if we were paying the Trust Fund?

Mr. ELMENDORF. Well, so, as you know, the Trust Fund is paid interest. I think our report may have that number, but I do not know it offhand. I think about $430 billion.

Senator PERDUE. So, the $18 trillion, which is the current gross debt, grows to about $27 trillion, I think, which is about—

Mr. ELMENDORF. Yes.

Senator PERDUE. —it is growing at about the rate the GDP is growing over the next ten years. I think that is right.

Mr. ELMENDORF. A little faster, I think.

Senator PERDUE. Okay. So, the question then is, if today our interest rates were at a historical average, between five and six percent, today, we would be paying, by my math, over a trillion dollars of interest, and that is just not sustainable. So, I would encourage the committee to look at the total responsibility we have to our taxpayers in terms of the total payment over the next 30 years.

The second one is I want to talk about the baseline just a second. I understand the baseline budgeting process, but that works on the assumption that everything we spent last year is going to get spent unless there is a cut coming that has already been adjudicated, is that correct?

Mr. ELMENDORF. So, our baseline projections mostly follow current law, but there are some specific directions to us that are written into the Budget Act of 1985.

Senator PERDUE. I am sorry. It is law and not policy, right? It is the law that—

Mr. ELMENDORF. It is current law. Again, there are some particular exceptions that are dictated to us by other laws in constructing the baseline projections. But, it is generally current law. So, if a tax provision is scheduled to expire, then our projections, in general, have that expiring.

Senator PERDUE. I get nervous when people with numbers talk about "in general," so we will have a one-on-one—

Mr. ELMENDORF. I am happy to run some of the—

Senator PERDUE. I know you will. We just do not have time now to get into it.

Is there a possibility, eventually, and what would we have to do in this baselining process to actually go in and do a zero-based look at this?

Mr. ELMENDORF. It depends what you mean by that, Senator. So, we build up our projections piece by piece, and you can—we can try to explain to you where those numbers come from, starting from zero. I mean, and if you think about appropriations, for example, current law has no appropriations for fiscal year 2016. That has not happened yet. But, our baseline takes the level of funding under the caps. But, the Congress, when it thinks about appropriations, I think you and your colleagues mostly think about them starting from zero and you decide how much you want to provide to something or something else. And, I know when CBO makes its own budget request to the appropriators, we try to defend the entire $47 million, starting from zero, and the Appropriations Committee can do as it sees fit.

Senator PERDUE. Thank you. I have ten seconds left, so, just, is it possible for us to get what Senator Johnson was talking about, a good look at years 11 through 30 on Social Security, Medicare future liabilities, unfunded liabilities with Social Security, Medicare, and pension benefits for Federal employees? You make a rough estimate, I know, but can we get a good look at that?

Mr. ELMENDORF. Yes, Senator. So, we will send you right away our last long-term budget outlook, and then we are happy to answer questions about it.

Senator PERDUE. Great. Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Senator MERKLEY.

Senator MERKLEY. Thank you, Mr. Chair, and I add my congratulations on your stewardship of this committee. I look forward to working with you and to addressing these big issues.

If we turn to the Appendix and look at the flow of revenues and outlays going back through 1965 up through last year, what we see is a substantial and dramatic change. In the year 2000, we were running a $2.5 billion surplus, or two-and-a-half—yes. And—if I have those numbers right. And, then, we are seeing, basically, a big change throughout the eight years that follow, and it has often been talked about that the impact of the war in Afghanistan and the war in Iraq were big factors, but also the cuts that were made in basic core tax rates, often benefitting those who are above the middle class in a very generous manner. And, now, we are seeing a substantial increase in inequality in this country.

Have you taken and analyzed the impact of the Bush tax cut rates on those earning more than $100,000 and their contribution

to the deficits from year to year and the overall debt, and could you give us a little bit of insight on that?

Mr. ELMENDORF. Yes, Senator. So, we have published—it is available on our website—the changes in CBO's projections of the budget surplus from January 2001 through the current day, so for the ten-year window that we were making projections for in January 2001. We had projected a surplus at that time over the ten years of about $5.5 trillion. The outcomes were a deficit of about $6 trillion, so that is a swing of more than $11 trillion. About $2 trillion of that is attributable to the tax cuts of 2001 and 2003, and then to the extension of those cuts in 2010. There was a very large effect of higher discretionary spending, and Senator Sanders raised the issue earlier about the—and you have—about the spending for the wars, and there are other changes in law, and also, of course, some errors on our part in projecting the economic conditions and technical factors.

Senator MERKLEY. Certainly, and those errors can swing either direction. But, essentially, that $10 trillion swing was the result of key policy decisions, not all of it to the tax rates, but a substantial amount.

If we turn to the issue of health care, and there have been several folks who have noted the challenge of the public costs of health care, there is also a shift from private costs to public costs under the current rules. If we take health care as a whole, what are we seeing in terms of core inflation and how does that compare, say, to five years ago?

Mr. ELMENDORF. So, total national health care spending has been growing much more slowly of late than it had before that, and we can see that in both the private sector and in the Federal programs.

Senator MERKLEY. And, is it accurate to say it is at a lower rate now than it has been over, say, the previous 25 years?

Mr. ELMENDORF. I think that is right, Senator, but I am not completely—

Senator MERKLEY. Let me turn to college loans. Many of us are very concerned about college loans being a source of profit to the government, and in your book here, it is laid out as a current source of positive revenue, but that may not capture the full impact. That may be one year's slice versus an overall picture of a loan portfolio. As you analyze a loan portfolio and the likelihood of defaults and the interest rates, does it come out as a source of profit to the Federal Government?

Mr. ELMENDORF. Well, Senator, under the rules of the Federal Credit Reform Act in 1990, we make projections of the cost of a loan issued in a given year as the present discounted value of all the future flows. And, what we have said, though, and maybe this is what you are alluding to, is that we do not think that that provides a comprehensive measure of cost, not because it does not capture the future effects, but because it does not incorporate a cost of the risk the government has taken on. But, the baseline projections follow, of course, the law established under the Federal Credit Reform Act, and under that law, a number of loan programs.

Chairman ENZI. Senator Portman.

Senator PORTMAN. Thank you, Mr. Chairman, and to Dr. Elmendorf, thank you for being here and for your service. You have got a tough job and I appreciate what you do.

I have been on the Budget Committee in the House and OMB Director, and I do not think I have ever been at a hearing where we have had kind of more misinformation out there. So, I was not going to do this, but I am going to start by asking you whether I am correct in this. I have sat here this morning and heard how we have got this huge problem that you just outlined. By the way, I stayed up and watched you on C–SPAN the night before last. That is how boring my life is.

[Laughter.]

Mr. ELMENDORF. I am sorry, Senator.

[Laughter.]

Senator PORTMAN. Where you presented this, and you might have thought it would have put me to sleep, but, in fact, it kept me up because it was so troubling. We are talking about unprecedented levels of debt and deficits. You know, we are taking our country into a situation where we are going to have a debt as a percent of our economy, as you outlined today and as you reported on this, that is unprecedented. We have never been there before.

And, we are sitting here this morning talking about how we can spend more and how, gosh, we cannot touch anything. If we do not touch anything, we are going to have a devastating impact on the people I represent, those middle class families that everybody says they care so much about. They are going to have about $160,000 a family in debt. That will be the amount of debt attributable to them. That is just wrong.

So, everybody is talking today about, okay, we have got this big problem, now what do we do about it. Let us look back at what happened. How did we get into this problem? And, so, everybody has said, including the most recent speaker, my friend, Mr. Merkley, he said, I would like you—he said he is glad that you affirmed, and I would quote, "that the very significant impact on the deficit was tax cuts for the rich." Okay, let us talk about that.

By the way, these tax cuts were supposed to stimulate economic growth. That was the idea. It increases savings and investment, including capital gains cuts. But, you are on report—I looked at it, I got it out earlier today—when everybody was saying, it is all about tax cuts for the rich, that is how we got into this deficit, this is your June 2012 report, which I assume you still stand by. This is what I get out of that.

The difference between the projection in 2000 as to what the surplus was going to be and where we ended up, you say 27 percent of that difference was because of the economy, basically, the market crash. You say 22 percent was because of other spending increases. Net interest was 12 percent. The stimulus rebates, AMT patch, ten percent.

And then you get down to the wars. People talked about the wars. Well, it is all about the wars. Look, we did spend more on our military and our homeland security after 9/11. That was 11 percent of it. So, that was not the reason. Yes, it was part of the reason, and we can argue that, you know, whether we are spending enough on defense or not. I am one who believes there is a lot of

waste at the Pentagon and there is room to do more there, even. But, the fact is, we made a decision as a country to respond to those horrific events.

People said, well, it is because we did not pay for Part D. That was three percent of it. And, for those who do not want prescription drug coverage for our seniors, that is fine. You can say you do not want Part D. You can say, well, we should have had it, but it should have been paid for. We can have that discussion, but it is three percent.

Tax cuts, all the tax cuts, you say—and, this is your report, okay, this is not me or some partisan potshot—14 percent of the difference. Fourteen percent. And, by the way, tax cuts for the rich—they have been talked about today again and again as the reason—how much was that, Mr. Elmendorf?

Mr. ELMENDORF. I am sorry, the tax—

Senator PORTMAN. Tax cuts for those over 250,000 bucks a year.

Mr. ELMENDORF. Right. So, the table shows—

Senator PORTMAN. It is four percent.

Mr. ELMENDORF. The table shows—

Senator PORTMAN. Four percent.

Mr. ELMENDORF. The point I made—

Senator PORTMAN. Four percent.

Mr. ELMENDORF. —was about the—I referred to the tax cuts of 2001 and 2003 and their extension in 2010. I do not have it in hand and this table does not show the breakdown by income, but I assume you have gone back to an original estimate from the Joint Tax Committee or something. I do not have that—

Senator PORTMAN. It is about four percent. And, so—and we can argue about that. I would guess that of that four percent, there was an economic benefit that exceeded that. That is my sense. And, I do not know if you have done that analysis. I know you have the ability to look at macroeconomic scoring and you do that. Do you have any comment on that?

Mr. ELMENDORF. We have not done that for those tax cuts, to my knowledge, Senator.

Senator PORTMAN. But, if you assume they had any benefit at all to the economy, including savings and investment we talked about and the reasons it was done, I mean, as you know, after all those tax cuts, the percentage that people were paying at the top and the burden of taxation increased, not decreased. We did a lot of things, including taking about five million people off the tax rolls altogether, middle class families and families that, frankly, today, even today, need a break. I totally agree. I mean, this economy has created a situation where wages are not just stagnant, they are going down, and where you have the rich are getting richer. That is not good. But, to blame it on those tax cuts is just not accurate. Do you agree, Dr. Elmendorf?

Mr. ELMENDORF. Well, Senator, as you have explained at greater length than I did, there are a lot of contributing factors, and we provide the information so that you and your colleagues can draw the conclusions you would draw from them. It is up to all of you to decide which of these policies you think were good ones and which ones you would like to do differently in the future. I cannot speak to that.

But, we did provide this decomposition, and as you said, there were a lot of different factors. It was mistakes on our part and the economic and technical aspects of the projections. It was the effect of the tax cuts of 2001 and 2003. It was the effect of higher discretionary spending, partly for defense, but not entirely for defense. It was the effect of a lot of other changes.

Senator PORTMAN. I appreciate you providing us whatever update you have on that, but I appreciate you also affirming the numbers that I gave, because those are consistent with your study of this issue. And, look, I totally agree with what Senator King said earlier, and Senator King talked about what we need to do going forward. Senator Corker, I thought, laid it out really well. You know, we have got to figure out how to work together as Republicans and Democrats to avoid this coming catastrophe.

You know, sitting right where you are, we had Erskine Bowles a couple of years ago at this committee, and he made the statement that is one that I always will remember, which is this is the most predictable economic crisis we have ever faced, if we do not do something about it. You laid that out earlier, that it has an impact on today's economy because it crowds out other investment and savings. That hurts middle class families in America right now, to have this huge and growing debt, and, obviously, the interest payments that everyone has talked about that they want to try to avoid.

You also said that this is an issue that does create a risk for us, and the risk is that we will have another crisis, and that risk is not one that I, personally, think that we ought to put our people that we represent through. Instead, we ought to deal with this issue and do it in a responsible way.

Thank you, Mr. Chairman.

Chairman ENZI. Senator Kaine.

Senator KAINE. Thank you, Mr. Chairman, and to Chairman Enzi and Senator Sanders, I have high hopes for the committee. I look forward to our work together.

And, Dr. Elmendorf, great job. It is good to have you back before us today.

Mr. ELMENDORF. Thank you.

Senator KAINE. So, you gave us a lot of material, and we are all focusing on the things that we are interested in. Budgets say a lot about what our priorities are. Sometimes our—well, always, our budgets speak more loudly than our words in terms of what our priorities are. And, the way I look at our priorities, based on your testimony, is essentially this.

Expenditures as a percentage of GDP, so in 2015, we are spending 1.3 percent of GDP on interest payments. That is going to increase. We are spending 3.2 percent of GDP on defense. That is on a downward path. We are spending 3.3 percent on non-defense discretionary. That is on a steeper downward path. We are spending 4.9 percent of GDP on Social Security. That is on an upward path. We are spending 5.1 percent on other Federal health care kind of combined programs. That is on an upward path. But, the largest expenditure item is tax expenditures, and that is 8.1 percent of GDP, and that is also likely on an upward path.

Now, of course, tax expenditures do some good things, just like Social Security is good, just like Federal health care expenditures are good, or defense or non-defense discretionary. But, it is just my hope as we grapple with this budgetary challenge that we do not grapple with everything except the largest item of expenditures, which is tax expenditures.

Dr. Elmendorf, there are proposals that have been introduced by members of this committee and others to move Federal budgeting to a two-year budgeting cycle. I do not know if this question was asked before I came in, but you spoke briefly about the values of certainty. Would it, in your view, be good for the economy if we budgeted on a two-year cycle?

Mr. ELMENDORF. I am not sure, Senator. That is a fair question. I do not—we have not thought hard about what the answer to that would be. I think it is—as I said, I think predictability is a good thing. Whether the two-year budget cycle would be a lot more predictable than a one-year cycle would depend a bit on how well the Congress actually resolved appropriations by the beginning of each of the fiscal years when it would have to do that.

And, I think, from your point of view, the other side of the predictability is whether you and your colleagues would regret not having an annual opportunity to shift direction of various programs and agencies, and we are not in a position to judge that, either.

Senator KAINE. I think there are bills now that have a two-year budget cycle with one-year appropriations, sort of six of the functional areas of government in one year and six in the next year so there are continuous appropriations and oversight. But, I will take your answer as you have indicated.

What would the impact on GDP be, generally, of immigration reform or trade deals of the kind that are being discussed by the administration now, or a major decision by Congress to do an infrastructure investment bill?

Mr. ELMENDORF. So, on immigration reform, as you know, Senator, we did a careful analysis of the comprehensive immigration bill that the Senate took up in 2013 and we thought that bill would boost the output of the economy, partly by having more people here working, but also over time because those additional people would lead to additional capital investment and somewhat faster—slightly faster productivity growth.

On infrastructure investment, an increase in government investment in physical infrastructure or in human capital or in research and development would, all else equal, lead to a stronger economy over time. The "all else equal" part is important, because if one borrows the money to do that investment, then that borrowing has a cost itself. So, it would depend how that investment was financed.

And, I am sorry, the—

Senator KAINE. And trade.

Mr. ELMENDORF. And trade. So, we have not done an analysis of the specific trade bills that are being discussed today. As a general matter, economists usually conclude that freer international trade is good for the overall U.S. economy, although not necessarily good for every individual in the economy, and even that overall result

could be different for specific bills, and we just have not looked at the ones that are being discussed now.

Senator KAINE. And then a last question, Dr. Elmendorf, my understanding of the CBO's projections is you do not factor into future projections any sort of increased expenditures that might be necessitated by climate change, is that correct?

Mr. ELMENDORF. We do not specifically incorporate them, Senator. We were asked this question—I was asked this question at a hearing last year. In an answer to the question for the record, we talked a bit about what consequences climate change would have. We have done work before on the possible effects on the U.S. economy, and then there could be effects on the budget through that. It is hard to—in most estimates of the effects of climate change on the U.S. economy suggest changes that are fairly small relative to the underlying economic growth and very small relative to the uncertainty about how big the economy will be in ten or 20 or 30 or 40 or 50 years. Obviously, for some other countries that are much more vulnerable, the effects could be proportionately larger for them.

In terms of the effects on the budget, there is also the question about what you and your colleagues might appropriate funds to address, but we do not really take that on board in our projections in any sense. We take a level of funding that you all have agreed to recently and we grow that out according to certain algorithms without trying to identify exactly what you might choose to spend money on or not spend money on in the future.

Senator KAINE. Thank you. Thank you, Mr. Chairman.

Chairman ENZI. Thank you, and I want to thank Senator Corker, as one of the new members, for being here for the entire hearing. I know that he is very busy because he is the Chairman of Foreign Relations, as well, and I appreciate your participation.

I would mention that Senator Grassley and Senator Sessions are not here because they are on the Judiciary Committee and the Judiciary Committee is doing the hearing for the Attorney General. The Finance Committee was also meeting, and that is where Senator Toomey is and where Senator Portman was for part of the discussion.

Dr. Elmendorf, I want to thank you for your testimony today, and for your answers to our questions. They are very concise and give people a lot more opportunity with their time than we are used to. I want to thank you for your professionalism as you served in this job and your economic forecasting and your management of 235 people. It is pretty amazing, with all the reports that we call on for you to do.

As information, all Senators' questions for the record are due by 6:00 p.m. today, with hard copy delivered to the Committee Clerk in Dirksen 624. Under our rules, Dr. Elmendorf will have seven days from receipt of the questions to respond with answers.

If there is no further business, the hearing is adjourned.

Mr. ELMENDORF. Thank you.

[Whereupon, at 11:51 a.m., the committee was adjourned.]

Congressional Budget Office

FEBRUARY 27, 2015;
UPDATED MARCH 4, 2015

# Answers to Questions for the Record Following a Hearing on the Budget and Economic Outlook for 2015 to 2025 Conducted by the Senate Committee on the Budget

*On January 28, 2015, the Senate Committee on the Budget convened a hearing at which Douglas W. Elmendorf, Director of the Congressional Budget Office, testified about CBO's report* The Budget and Economic Outlook: 2015 to 2025 *(January 2015), www.cbo.gov/publication/49892. Following that hearing, Chairman Enzi, Ranking Member Sanders, and other Members of the Committee submitted questions for the record. This document provides CBO's answers.*

## Chairman Enzi

**Question.** The baseline includes drastic increases in the cost of price support programs in the farm bill. The cost projections of the Price Loss Coverage program, for instance, nearly doubled in the ten-year window from last April's baseline. The Agricultural Act of 2014, passed about a year ago, was based on the May 2013 baseline. When it passed, there were complaints that the price support baseline no longer accurately reflected the agricultural market. Can you explain if the savings that CBO attributed to changes in the price support programs included in the Agricultural Act of 2014 will still materialize?

**Answer.** The Agricultural Act of 2014 ended direct payments to agriculture producers, who previously had been paid about $4.5 billion annually regardless of the market prices of the crops they produced. Under that act, direct payments were replaced with two new price and revenue support programs known as price loss coverage and agriculture risk coverage. The size of any federal payments under each of those programs depends on crop prices; if those prices fall below the reference prices in the law, then payments to producers are triggered. Estimates of future costs under those programs are much less certain than estimates of future savings from ending direct payments, which did not depend on crop prices. According to CBO's most recent projections, the replacement of direct payments with the two new programs will probably still yield budgetary savings, but those savings are likely to be smaller than CBO estimated when the legislation was enacted.

CBO's final cost estimate for the Agricultural Act of 2014, which was made in January 2014, indicated that ending direct payments would save $40.8 billion over the 2014–2023 period.[1]

1. Congressional Budget Office, cost estimate for H.R. 2642, the Agricultural Act of 2014 (January 28, 2014), www.cbo.gov/publication/45049. The Agricultural Act of 2014 also eliminated two price and revenue support programs—countercyclical payments and the average crop revenue election program—yielding additional savings, estimated to be $6.2 billion relative to the May 2013 baseline, over the same period. Spending for those programs depended on prices and yields.

Note: Originally transmitted to the Senate Committee on the Budget on February 27, 2015, this document was updated on March 4, 2015, to include answers to questions from Senator Corker, which were inadvertently omitted earlier. Those answers appear at the end of this document.

At that time, CBO estimated that the price loss coverage and the agriculture risk coverage programs would cost $27.2 billion over the 2014–2023 period, or about $13.6 billion less than the cost of continuing direct payments over the same period.[2]

Those estimates were prepared relative to baseline projections that CBO had issued in May 2013 because CBO and the Budget Committees have a long-standing convention of using a consistent baseline to prepare cost estimates for major legislation when its consideration spans the first and second sessions of a Congress. Therefore, the final cost estimate for the Agricultural Act of 2014 reflected crop price forecasts that had been developed early in 2013. However, by the time the Agricultural Act of 2014 became law on February 7, 2014, the historically high crop prices had begun to fall.

CBO now expects that crop prices in general will be significantly lower over the next 10 years than it anticipated in May 2013. For its January 2015 baseline, CBO estimated that the price of corn will average $3.97 per bushel over the 2016–2023 period, 14 percent less than the $4.63 per-bushel average anticipated for the same period in the May 2013 baseline.

On the basis of that January 2015 forecast, the budgetary savings from replacing direct payments with the price loss coverage and agriculture risk coverage programs are now expected to be less than CBO estimated when the Agricultural Act of 2014 was enacted. CBO now projects that the price loss coverage and agriculture risk coverage programs will cost $36.7 billion over the 2014–2023 period, about $9.5 billion more than it estimated when the law was enacted.[3]

Crop prices could turn out to be higher or lower than CBO currently anticipates. Hence, the actual budgetary savings realized or costs incurred from ending direct payments and replacing them with price loss coverage and agriculture risk coverage could be greater or smaller than the amounts CBO estimated when the Agricultural Act of 2014 was enacted. For each annual baseline, CBO develops a consistent set of projections for the supply, use, and prices of major crops over the next 10 years.[4] The agency aims for its forecast of prices to be in the middle of the distribution of potential outcomes; consequently, the current forecast is as likely to be too high as it is to be too low.

Such estimates are very uncertain because crop prices have historically been highly variable, as shown in the figure below. The average year-to-year change in the price of corn, in one direction or the other, was $0.50 per bushel over the 1975–2013 period. The largest annual change during that period was $2.43 per bushel. Those changes represented a significant percentage of the average price of corn during that period, which was $2.82 per bushel.

In the past decade, corn prices rose sharply under tighter market conditions—in important part because of high oil prices and the enactment of renewable fuel standards (and the consequent increased demand for corn-based ethanol). Over the past year, corn prices fell as those market conditions began to reverse. In addition, weather and other influences on commodity markets often lead to significant changes in supply and demand for commodities even within a single year, not just from one year to the next.

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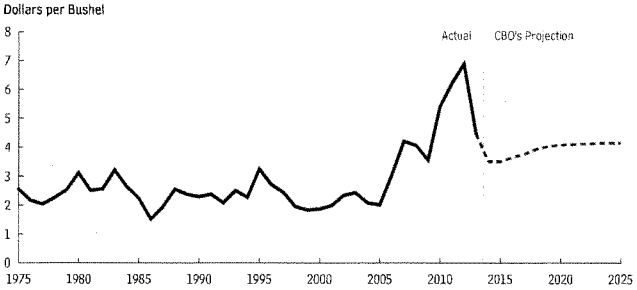
2. CBO's baseline projections incorporated the assumption that direct payments would continue indefinitely, although they were scheduled to expire with the 2013 crop, following the rules for developing baseline projections specified by the Balanced Budget and Emergency Deficit Control Act of 1985.

3. That estimate reflects the assumption that those programs will be in effect throughout that period.

4. For the most recent projections, see Congressional Budget Office, *USDA Mandatory Farm Programs—Baseline Projections* (January 2015), **www.cbo.gov/publication/44202**.

**Price of Corn**




Sources: Congressional Budget Office; Department of Agriculture.

Note: Prices are the average price during a marketing year, which runs from September 1 of the year shown to August 31 of the following year.

**Question.** The Highway Trust Fund is currently insolvent. Since 2005, spending has far exceeded revenues because gas-tax levels plateaued while spending grew. To make up for funding shortfalls, the trust fund has required large general fund contributions totaling more than $50 billion since 2008. Although a bill with questionable offsets extends highway funding until May 2015, there is still no long term solution. CBO projects that the Highway Account of the Highway Trust Fund will have difficulty meeting obligations sometime during the latter half of Fiscal Year 2016. The HTF will still require more than $170 billion in bailouts, with the next installment necessary at some point in FY 2015. Revenues are far less than outlays. Is that correct? Are there any options besides raising the gasoline tax or reducing spending that will provide long-term solvency for the Trust Fund? Would moving Transit spending to the General Fund provide any long-term relief for the HTF? Should we eliminate the Highway Trust Fund altogether and fund all highway improvement programs with discretionary funds? What if we had a separate budgetary cap for Highway Trust Fund spending? Should we increase the gas tax to a level that will ensure the solvency of the Highway Trust Fund indefinitely? What would that option look like?

**Answer.** In the past 10 years, outlays from the Highway Trust Fund have exceeded the fund's income (apart from transfers from other funds) by more than $65 billion. Since 2008, lawmakers have addressed shortfalls by transferring $65 billion, mostly from the general fund of the Treasury, to the Highway Trust Fund. If current policies are maintained, the fund's revenues will continue to fall short of the amounts necessary to cover spending for the programs it finances. Specifically, if obligations from the fund continued at the 2015 rate (with increases to account for future inflation) and the expiring taxes on fuels and heavy vehicles were extended at their current rates, the gap between the projected spending and the projected tax revenues would amount to $164 billion over the 2015–2025 period. Under current law, the trust fund cannot incur negative balances, nor can it borrow to cover unmet obligations.[5]

5. For more information on the Highway Trust Fund, see Congressional Budget Office, *The Highway Trust Fund and the Treatment of Surface Transportation Programs in the Federal Budget* (June 2014), **www.cbo.gov/publication/45416**.

To help balance the trust fund's resources and outlays, lawmakers could choose to reduce spending for surface transportation programs, boost the fund's revenues, authorize additional transfers, or adopt some combination of those approaches:[6]

- If lawmakers chose to address the projected shortfalls solely by cutting spending, over the 2016–2025 period, the highway account would see a decrease of more than 30 percent in the authority to obligate funds, and the mass transit account's authority would decrease by about 60 percent, compared with CBO's baseline projections.

- Revenues credited to the trust fund could be increased by raising existing taxes on motor fuels or other transportation-related products and activities or by imposing new taxes on highway users, such as those based on vehicle-miles traveled. The staff of the Joint Committee on Taxation (JCT) estimates that a 1 cent increase in taxes on motor fuels—primarily gasoline and diesel fuel—would raise about $1.5 billion each year for the trust fund. If lawmakers chose to meet obligations projected for the trust fund solely by raising revenues, they would need to increase motor fuel taxes by between 10 cents and 15 cents per gallon, starting in fiscal year 2016. The trust fund's revenues could also be boosted by raising new revenues from nontransportation sources and allocating them to the fund.

- The trust fund could also continue to receive supplements from the general fund—which could be accomplished either by transferring specific amounts of funds or by designating that funds from a particular source be credited to the Highway Trust Fund. To finance projected spending without increasing taxes or generating new revenues for the trust fund from other sources, lawmakers would need to transfer $5 billion in 2015 and between $12 billion and $18 billion every year thereafter through 2025. Spending resulting from such general fund transfers could be paid for by reducing other spending, by increasing broad-based taxes, or by increasing federal borrowing.

Moving new spending for transit from the Highway Trust Fund to the general fund and transferring revenues currently credited to the transit account to the highway account would leave substantial shortfalls in the Highway Trust Fund in both the short term and the long term. As under current law, such shortfalls would prevent the program from operating normally in any year, starting in 2015. Over the 2015–2025 period, CBO projects that shortfalls in the highway account will amount to $125 billion. CBO further projects that the transit account will be credited with revenues of about $5 billion per year over the 2015–2025 period (totaling about $53 billion), leaving a shortfall of $72 billion in the highway account even if all of the transit account's revenues were credited to the highway account. Moreover, crediting those future deposits to the highway account would prevent the transit account from meeting obligations that have already been made. That is because most obligations from the transit account (and from the highway account as well) involve capital projects that take several years to complete, and most of the transit account's current obligations will therefore be met using tax revenues that have not yet been collected. At the end of 2014, for example, $16 billion in contract authority for transit programs had been obligated but not spent and another $8 billion was available to states but not yet obligated.[7] As a result, even if states were given no further authority to commit

6. For more information about the range of options available to the Congress for deciding how much to spend on highways and other surface transportation programs and for deciding how to finance that spending, see the testimony of Joseph Kile, Assistant Director for Microeconomic Studies, Congressional Budget Office, before the Senate Committee on Finance, *The Status of the Highway Trust Fund and Options for Financing Highway Spending* (May 6, 2014), www.cbo.gov/publication/45315.

7. See Office of Management and Budget, *Budget of the U.S. Government, Fiscal Year 2016: Appendix* (February 2015), p. 981, www.whitehouse.gov/omb/budget/Appendix.

funds from the transit account, another five years' worth of motor fuel taxes would need to be credited to the transit account just to meet the account's obligations at the end of 2014. Thus, taxes on motor fuels now credited to the transit account could not be used by the highway account for the next five years.

One possible change, which you inquired about, is to eliminate the Highway Trust Fund and treat surface transportation programs as entirely discretionary, possibly with a separate budgetary cap. Currently, the programs' budget authority is mandatory, and their annual obligations are controlled by limits set in appropriation acts. As a result, surface transportation programs funded from the Highway Trust Fund are generally not subject to the processes that control spending for most other programs, including sequestration for mandatory programs, statutory pay-as-you-go rules, and caps on discretionary funding. Under the possible change, surface transportation progtams would be subjecr to trade-offs similar to those that affect all other discretionary priorities. If funding was not constrained by trust fund revenues, lawmakers would have more flexibility in setting spending amounts, but because funding would be provided one year at a time, this oprion could reduce the ability of states to plan for future capital expenditures, as they would not have multiyear transportation acts. Such a change would also significantly alter the way the Department of Transportation (DOT) carries out its programs. Under current law, future contract authority is one of the factors that grantees take into account when developing the multiyear transpottation plans that must be approved by DOT before funds can be obligated. Another consideration is that general funds are often a less efficient source of financial support for infrastructure than are user fees because they provide no incentive for the efficient use of the infrastructure.

CBO has not analyzed the possible effects of creating a separate budgetary cap for highway and transit spending. Such a cap existed under previous authorizations for transportation programs, the Transportation Equity Act for the 21st Century and the Safe, Accountable, Flexible, Efficient Ttansportation Equity Act: A Legacy for Users.

Another approach for dealing with the projected shortfalls in the Highway Trust Fund would be to place more of the responsibility for highway infrastructure on state and local governments, perhaps by facilitating greater use of borrowing by those governments to finance highway projects. State and local governments (and some private entities) can currently use tax-preferred bonds that convey subsidies from the federal government in the form of tax exemptions, credits, or payments in lieu of credits to finance road construction.

**Question.** In the February 2014 baseline, CBO conducted its first comprehensive analysis of rhe labor market effects of the health care law. The analysis found that by 2024, the equivalent of 2.5 million Americans will exit the labor force or work less as a result of the law. CBO also estimates the law will reduce the total number of hours worked by 1.5 to 2 percent during the FY 2017-2024 period and will cause a 1 percent reduction in aggregate labor compensation over the same period. As you previously clarified in response to a question for the record from Budget Committee Member last year: "... reductions in the amount of labor income earned in the economy will lead to reduced income and payroll tax revenues. CBO's baseline economic and revenue projections incorpotate the agency's estimates of the effects of federal policy on economic activity and tax revenues. Hence, those projections account for the ACA, including its effects on labor markets. However, CBO has not attempted to isolate the revenue effect of the labor market changes attributable to the act from other factors that affect economic activity or tax revenues overall." Since the time of your response, has CBO ever attempted to estimate the size of the revenue loss associated with the lahor market effects of the health care law? If so, approximately how large is that effect? And would including that

lower revenue estimate in the cost of the law (through the use of dynamic modeling), as you are now required to do by the House scoring rule, change your overall assessment of the 10-year net deficit impact of Obamacare?

**Answer.** On the basis of its analyses of the ways in which changes in the supply of labor generally affect the overall economy and therefore the federal budget, CBO expects that the reductions in the supply of labor resulting from the Affordable Care Act (ACA) will reduce federal revenues. However, CBO has not attempted to estimate the impact of the overall economic effects of the ACA on the federal budget. If macroeconomic effects had been included in the cost estimate for the ACA that CBO provided in March 2010, the estimated net effect of that legislation on the deficit would probably have been less favorable than that which was shown.

**Question.** CBO projects that the Social Security Disability Insurance trust fund will run out of money by 2017. This will require Congress to act in advance of the insolvency date. In the past, CBO has written that changes in demographics cannot explain the rise in DI enrollment over the last 30 years. Is that still your assessment? If so, why?

**Answer.** Over the past 30 years, the number of disabled workers who receive benefits from the Social Security Disability Insurance (DI) program has increased more than threefold, rising from 2.7 million in 1985 to 9.0 million in 2014. Multiple factors help explain the DI program's rapid growth, and CBO has grouped them into three categories: changes in demographics and an increase in the number of workers; changes in federal policy; and changes in opportunities for employment and in compensation.[8]

The increase in DI enrollment between 1985 and today can be attributed, in part, to changes in demographics and an increase in the number of workers. The aging of the large baby-boom generation (people born between 1946 and 1964), and consequently the aging of the workforce, has led to an increase in the share of workers who enter the DI program. Older workers are far more likely than younger workers to qualify for DI benefits for the following reasons: More older people suffer from debilitating conditions, and the program's qualification standards for older workers are less strict than those for younger workers because older people are assumed to be less able to adapt to new types of work. In addition, the increase in the number of people who are eligible to receive benefits if they become disabled—largely stemming from an increase in the number of women participating in the labor force—has been a factor in the growth in DI enrollment.

Changes in federal policy have also contributed to growth in the DI program over the past 30 years. For example, enactment of the Social Security Disability Benefits Reform Act of 1984 expanded the ways in which people could qualify for the DI program—such as allowing applicants to qualify for benefits on the basis of multiple medical conditions that, taken alone, might not have met the qualifications for participation in the program and allowing symptoms of mental illness and pain to be considered in assessing whether a person qualifies for the DI program. Those changes in policy led to a substantial expansion in the share of DI beneficiaries with mental or musculoskeletal disorders, many of whom enter the program at younger ages than do people with other types of disabilities. In addition, the incremental

8. Congressional Budget Office, *Policy Options for the Social Security Disability Insurance Program* (July 2012), pp. 3–6, www.cbo.gov/publication/43421.

rise in the full retirement age for Social Security that occurred during the past decade has increased enrollment in the DI program in two ways: It has enlarged the potential pool of DI applicants by increasing the age of eligibility for unreduced Social Security retirement benefits; and it has increased the length of time people can receive DI benefits, as DI beneficiaries now shift to the Social Security retirement program later than in previous years.

Finally, changes in opportunities for employment and in compensation have been a factor in the growth in the DI program over the past three decades. For example, short-term economic downturns can have long-run effects on DI entollment. Many people who have been out of work for long periods find it hard to reenter the labor force and may turn to the DI program for support. Once they start receiving DI benefits, only a very small share will permanently leave the program to return to the workforce. In addition, because the earnings of low-wage workers have increased more slowly than average earnings per worker in the economy and the DI program uses average earnings growth to determine changes in benefits, those benefits have risen to be a greater share of the earnings of low-wage workers. That increase in benefits relative to the compensation associated with working has probably increased the number of people seeking DI benefits over the past 30 years. Furthermore, access to health insurance and the cost of obtaining it are factors that may have affected DI enrollment. Disabled beneficiaries receive coverage under Medicare, regardless of their age, generally after a 24-month waiting period. For workers without employment-based health insurance, that eligibility for Medicare may have encouraged them to apply for DI benefits.

**Question.** On Monday, January 26, 2015, *Congressional Quarterly* tan an article with the inaccurate headline "CBO Cuts Estimate of Health Law Cost by $101 Billion." Unfortunately, many other news outlets also inaccurately reported that the total cost of Obamacare had come down by that amount. But CBO's report states on p. 115 that "Those estimates address only the insurance coverage provisions of the ACA and do not reflect all of the act's budgetary effects." Isn't it true that most of the lower net cost of the health care law comes from higher revenues as fewer people are able to keep their employer-sponsored insurance?

Looking at Table B-4 on p. 126, this $101 billion change is a reduction in the *net* cost of only a subset of the law (i.e. the coverage provisions). However, is it the case rhar CBO also concluded that the gross cost of these provisions changed very little since your previous baseline?

CBO's tables also show that the primary factor behind the estimated reduction in the net cost of these coverage provisions is that, on net, an additional 2 million people who liked their employer sponsored insurance are now estimated to lose it under your baseline projections—and will thus have to pay higher taxes on their wages or their health insurance as a result. So isn't it an appropriate takeaway from this change that if you like your health care plan, you can't necessarily keep it?

**Answer.** In a comparison of CBO and JCT's current and previous estimates of the effects of the insurance coverage provisions of the Affordable Care Act, CBO reported a reduction of $101 billion in the estimated net cost of those provisions over the 2015–2024 period. The following differences between the baseline projections released in January 2015 and those provided in April 2014 account for that change:

- A reduction of $9 billion in the estimated gross cost of the coverage provisions, resulting from:
  - A reduction of $68 billion attributable to lower exchange subsidies and related spending and revenues;
  - An increase of $59 billion caused by higher outlays for Medicaid and the Children's Health Insurance Program (CHIP); and
  - A slight reduction in tax credits for small employers.
- An increase of $5 billion in projected net costs stemming from changes in estimated penalty payments and estimated collections from the excise tax on high-premium insurance plans; and
- A reduction in estimated net costs of $97 billion from other effects on revenues and outlays, which consist mainly of the effects of changes in taxable compensation on revenues.

The $9 billion reduction in the estimated gross cost is small (about 0.5 percent) relative to CBO's previous projection of $1,839 billion for the gross cost over the 2015–2024 period. The largest change in the estimates—$97 billion related primarily to an increase in estimated taxable compensation—stems from a combination of improvements in estimating methodology and a downward revision to the number of people who are projected to have employment-based coverage in most years. Less employment-based coverage (about a million fewer people in most years of the projection period) means that taxable compensation in the form of wages and salaries will be greater, or that corporate profits will be greater, leading to higher federal revenues. That change in estimated taxable compensation is also small relative to the total amount of compensation that is provided in the form of employment-based health insurance and excluded from taxable income.

CBO currently projects that the ACA will reduce the number of people with employment-based coverage in 2024 by 9 million on net, compared with what the number would have been if the law had not been enacted. (The difference from 7 million reported in April 2014 is equal to about 1 million rather than 2 million because of rounding.) That net reduction consists of various flows both in and out of employment-based coverage stemming from the ACA. In 2024, 14 million people are projected to not receive an offer of employment-based coverage that they would otherwise have received and 3 million people are projected to decline an existing offer of employment-based coverage. Some of those 17 million people are expected to gain coverage from another source, whereas others will forgo health insurance altogether. That number is partially offset by the 8 million people who are projected to gain employment-based coverage that they would not have had in the absence of the ACA. CBO cannot assess how many of the people affected would have preferred the coverage they would have obtained if the ACA had not been enacted.

**Ranking Member Sanders**

**Question.** CBO's methodology for developing the baseline it uses for its projections are set by law. Last year, this committee examined some of the impacts that climate change would have on the economy and on the federal budget, and we heard testimony from experts at GAO, national security experts, and others who said that there will be growing impacts on federal

spending and the economy that will ultimately drive increases in the debt. Does CBO's baseline incorporate these increasingly significant costs of climate change? How would the fiscal impacts of climate change be affected if, globally, we were able to reduce emissions and make communities more resilient to the effects of climate change.

**Answer.** CBO's baseline projections for the nexr 10 years generally reflect current law. Some of the programs most affected by weather-related disasters—such as federal crop insurance and flood insurance—are mandatory spending programs. For those programs, CBO attempts to incorporate inro its projections all factors that might affect spending under current law, including changes in the way land is used and trends in crop yields, which may be affected by climate change. Reductions in greenhouse gas emissions over the next decade would probably have a very small impact on those programs because the effects of those reductions would primarily be realized beyond the 10-year projection period, CBO anticipates.

Other programs affected by weather-related disasters, such as the Federal Emergency Management Agency's disaster relief program, are discretionary. In CBO's 10-year baseline projections, as specified in law, the amount appropriated for the current year is assumed to be provided in each subsequent year, with an adjustment for inflation. Thus, the baseline incorporates an assumption that funding for disaster relief in each year of the coming decade will be similar ro that provided in the current year.

The Congress has typically responded to large-scale disasters, such as Hurricanes Katrina and Sandy, by changing the law to increase spending—providing emergency supplemental appropriations for disaster relief, for example. (Total appropriations for disaster relief amounted to $135 billion over the 2005–2014 period, much of which was provided in 2005 and 2006 in response to Hurricanes Katrina, Rita, and Wilma.) Under the rules that govern baseline projections, CBO does not artempt to predict the frequency or magnitude of such events or the Congress's response to them.

In the future, lawmakers might inctease funding relative to baseline projections if the effect of climare change on the frequency and magnitude of weather-related disasters became larger. For example, increased damage from storm surges might lead the Congress to pass additional emergency supplemental appropriations for disaster relief or to approve legislation that would provide funding to protect infrastructure that is vulnerable ro rising sea levels. The Congress might also amend existing laws so as to limit federal spending on weather-related disasters. For example, lawmakers might alter the flood insurance or crop insurance programs in a way that would provide insured parties with greater incentive to avoid potential damage. But CBO's baseline projections, which are built on current law, cannor capture such possible changes.

Climate change may also affect the nation's economic output and, consequently, federal rax revenues. However, estimates by researchers suggest that those effects will probably be very small over the next 10 years. For example, one recent study found that the effect of climate change on the productivity of outdoor workers over the 2020–2039 period would probably lie between an increase of 0.03 percent and a decline of 0.38 percent, on the basis of a global emissions scenario that is consistent with a modest shift away from fossil fuels or a slowdown in economic growth.[9] Such estimates are very uncertain, however.

9. Trevor Houser and others, *American Climate Prospectus: Economic Risks in the United States* (Rhodium Group, June 2014, updated October 2014), Figure 7.3, http://rhg.com/reports/climate-prospectus.

**Question.** In its most recent (2014) report on the state of the global economy, the IMF—a longtime advocate for fiscal austerity—came out in favor of substantially increased public infrastructure investment, saying that increased spending on infrastructure could reduce rather than increase government debt burdens over time. Do you agree?

**Answer.** The effects on government debt of increased federal spending on infrastructure—such as highways, mass transit, aviation, rail and water transportation, water resources, and water utilities, which together account for the bulk of federal spending for infrastructure—would depend on the particular spending policy. In general, increases in such spending have an impact on the economy in both the short and the long run:

- In the short run, as is the case for other government purchases, an increase in federal infrastructure spending boosts output by increasing total demand for goods and services. That boost tends to be larger when output is well below its maximum sustainable amount and the Federal Reserve's response to changes in fiscal policies is likely to be limited.

- In the long run, increases in federal infrastructure spending—if not offset by decreases in other spending or increases in taxes—have opposing effects on economic output. The increase in spending raises government borrowing, which tends to "crowd out" private investment, lowering output. However, increased federal spending on infrastructure also generally raises productivity in various ways, which tends to boost output.

The economic effects would "feed back" to the budget and affect the size of deficits and debt. CBO estimates the budgetary implications of the economic effects generated by changes in fiscal policy using a simplified analysis that takes into account changes in taxable income and interest rates, among other things, but does not incorporate a detailed program-by-program analysis, as do CBO's regular budget estimates.

On the basis of CBO's past analyses of changes in federal spending programs, the agency expects that most of the estimated effects on the budget of increased federal spending on infrastructure would probably stem from two factors: changes in output, which would affect revenues by altering the amount of taxable income; and changes in interest rates (resulting from the changes in deficits and debt), which would affect the federal government's interest payments. CBO's estimates also generally account for the influence of other factors on the budget, such as the impact of changes in prices on federal spending for purchases and transfer payments and the effect of changes in the unemployment rate on federal spending for unemployment benefits. However, CBO has not undertaken an analysis of the net effect on the budget of a specific infrastructure policy.

**Question.** CBO's estimate of the cost of the Affordable Care Act is 20 percent lower than it was when you issued your first official estimate and 7 percent lower than what you projected in your April 2014 estimate. That was just eight months ago. Clearly, such projections are already very uncertain. Wouldn't undertaking dynamic scoring add yet another layer of uncertainty?

**Answer.** Many of CBO's projections are very uncertain, so the agency aims for those projections to be in the middle of the distribution of possible outcomes given the baseline assumptions about federal tax and spending policies, while recognizing that there will always be deviations from any such projections. Following a long-standing convention, CBO's cost estimates for individual legislative proposals have not included macroeconomic effects—

except for estimates provided for comprehensive immigration legislation, which would significantly increase the U.S. labor force. (Assuming that such legislation would have no effect on overall output would distort the estimates too severely.) Including macroeconomic effects in cost estimates would add another source of potential variability to those estimates.

**Question.** CBO's Budget and Economic Outlook provides a long-range forecast for the budget deficit as a percentage of GDP, but it doesn't include a forecast for the trade deficit as a share of GDP in each of the same years. Can that be included in future such reports?

**Answer.** CBO's budget projections for the next 10 years are based on a detailed economic forecast. The agency's projection of net exports as a percentage of gross domestic product (GDP) is provided below. CBO can provide this information to the Congress in the future.

**CBO's Projection of Net Exports as a Percentage of GDP, 2015 to 2025**

| | |
|---|---|
| 2015 | -2.5 |
| 2016 | -2.8 |
| 2017 | -2.7 |
| 2018 | -2.5 |
| 2019 | -2.2 |
| 2020 | -2.1 |
| 2021 | -2.0 |
| 2022 | -1.9 |
| 2023 | -1.7 |
| 2024 | -1.5 |
| 2025 | -1.4 |

Source: Congressional Budget Office.
Note: GDP = gross domestic product.

**Question.** At the end of last year, Congress attached H.R. 992 to the omnibus spending bill. This provision allowed systemically important financial institutions to place derivatives trades into their federally-insured subsidiaries, as opposed to having to place these bets in non-insured subsidiaries without access to taxpayer dollars. In other words, it gave large banks an implicit government backing of roughly $7 trillion of notionally valued derivatives. More importantly, as FDIC Vice Chairman Tom Hoenig pointed out, these are the riskiest derivatives, including uncleared credit default swaps and equity derivatives. When CBO did its cost estimates of this legal change, it made the following estimate: "CBO estimates that any impact on the net cash flows of the Federal Reserve or the FDIC over the next ten years would not be significant." Is CBO implying that allowing Wall Street banks to place derivatives bets with taxpayer backing does not risk increasing the deficit? How did you come up with this estimate?

**Answer.** Enactment of H.R. 992, the Swaps Regulatory Improvement Act, modified the Dodd–Frank Wall Street Reform and Consumer Protection Act to allow insured depository institutions to retain some financial instruments known as swaps while remaining eligible for assistance from the Federal Deposit Insurance Corporation (FDIC) and the Federal Reserve.[10]

10. H.R. 922 was enacted as section 630 of title VI of the Financial Services and General Government Appropriations Act, 2015, in division E of the Consolidated and Further Continuing Appropriations Act, 2015.

A swap is a contract between two parties to exchange payments on the basis of the price of an underlying asset or a change in interest, exchange, or other reference rate. Swaps can be used to hedge—or mitigate—certain risks associated with a firm's traditional activities, such as interest rate risk, or to speculate on the basis of expected changes in prices or rates.

In its cost estimate for H.R. 992, CBO concluded that enactment of the legislation would not significantly alter federal spending attributable to bank failures and assistance over the next 10 years. In reaching that conclusion, the agency considered the amount of swap activity, the potential losses, banks' capacity to absorb losses, and the extent to which the federal government might ultimately bear any losses, as follows:

- Most swaps will not be affected by H.R. 992. The provision of Dodd–Frank that prohibited insured depository institutions from retaining swaps did not apply to swaps held for hedging purposes or to swaps involving certain permissible securities. (Such swaps include those that reference interest rates, exchange rates, government securities, and precious metals.) Swaps referencing interest and exchange rates currently make up over 90 percent of all such instruments held by insured commercial banks and savings institutions and will not be affected by H.R. 992.

- Potential losses to banks from their retention of swaps are much smaller than the total notional value of such swaps. The notional value of swaps that will remain with insured depository institutions as a result of the bill is projected to be very large, despite the fact that most swaps will not be affected. Potential losses are much smaller in part because maximum payments on any one contract are generally a small percentage of the notional amount and because multiple offsetting contracts between counterparties—that is, between the entities that have entered into contracts—are common. Swap transactions pose the risk of large losses to banks through two main channels: risks from potential default on obligations of counterparties to the swap transactions and risks that result from either speculation or imperfect hedging. Based on information from the Office of the Comptroller of the Currency (OCC), CBO estimates that potential losses to depository institutions from the failure of counterparties to make payments related to swaps that will be affected by the bill amount to about 0.4 percent of the notional amounts—about $30 billion. (This amount represents a projection of the maximum loss that would be incurred by all banks if all of their counterparties were to fail to make payments over the projected life of their current contracts.) The potential exposure from speculation or imperfectly executed hedging transactions could be larger. For example, a single institution, JP Morgan Chase, suffered more than $6 billion in losses from the activities of the trader known as the London Whale. However, other bank regulations are designed to limit such risks.

- The depository institutions that will be most affected are extremely large and, in most cases, will be able to absorb sizable credit losses on swaps without significantly increasing the risk of failure. The vast majority of swap activity occurs in a few institutions. According to OCC, four banks—Citibank, JP Morgan Chase, Goldman Sachs, and Bank of America—account for over 90 percent of the notional value of swaps housed in commercial banks and thrifts. The largest 25 institutions account for nearly 100 percent. The exposures of those institutions to potential losses on swaps are generally considerably smaller than the institutions' capital. For example, the $6 billion loss suffered by JP Morgan Chase was much smaller than the bank's capital (specifically, its common equity tier 1 capital) of $165 billion and net income of $22 billion in 2014.

- Any federal spending to assist financial institutions that suffer losses on swaps stemming from enactment of H.R. 992 will probably be offset by payments from the banking industry. If a large insured institution involved in swap activity were to fail, it would be closed following the FDIC's resolution procedures. Additionally, if a systemically important holding company of an insured institution were to fail, it could be resolved under FDIC's Orderly Liquidation Authority established under the Dodd–Frank Act. Under current law, any federal spending resulting from the use of FDIC's authorities, net of recoveries, will be recouped through assessments on the industry, resulting in no significant ner effect on the budget over time. Thus, although the swap dealers will probably benefit from increased swap activity under the legislation, any federal costs stemming from that increased activity will probably be recovered from insured banks and their customers.

**Question.** The federal government has many loan and loan guarantee programs – student loans, housing loans, and rural electric loans – on which Americans rely. Has CBO done analysis on how much switching to Fair Value accounting would increase costs to users of loan and loan guarantee programs? If so, could you share this analysis with the committee?

**Answer.** The accounting method that CBO uses to provide its official estimates of the costs of federal credit programs is prescribed by the Federal Credit Reform Act of 1990 (FCRA). That legislation requires such costs to be measured by discounting expected future cash flows associated with a loan or loan guarantee to a present value at the rime of disbursement. The discount rate used for FCRA estimates is tied to Treasury securities rather than to market rates. Thus, although the FCRA methodology accounts for expected losses from defaults, it does not account for the fact that losses from defaulrs tend ro be highest when economic and financial conditions are poor, which is when resources are scarcer and hence more valuable.

Fair-value accounting differs in that it recognizes such market risk—the component of financial risk that remains even after investors have diversified their portfolios as much as possible and that arises from shifts in current and expected macroeconomic conditions—as a cost to the government. To incorporate the cost of such risk, present values in fair-value accounting are calculated using market-based discount rates. Thus, fair-value estimates generally imply larger costs to the government for issuing or guaranteeing a loan than do FCRA-based estimates.[11]

Last year, CBO found that if fair-value procedures had been used to estimate the cost of credit programs in 2014, the total deficit would have been about $50 billion greater than the deficit as measured using current estimating procedures.[12] Much of the difference derived from the valuation of student loans: Under FCRA procedures, those loans generate very large budgetary savings per dollar lent compared with other federal credit assistance; under the fair-value approach, most of those savings disappear.

Switching from a FCRA approach to a fair-value approach to recording costs in the federal budget without making any changes to credit programs themselves would not affect costs for

11. Congressional Budget Office, *Fair-Value Accounting for Federal Credit Programs* (March 2012), **www.cbo.gov/publication/43027**.

12. Congressional Budget Office, cost estimate for H.R. 1872, the Budget and Accounting Transparency Act of 2014 (February 12, 2014), **www.cbo.gov/publication/45109**.

users of loan and loan guarantee programs. However, the use of fair-value accounting could affect Congressional decisions about the volume of loans to be made or guaranteed, the fees charged to borrowers, or other terms associated with any new loans or loan guarantees—perhaps to reduce estimated budgetary costs. Without an adjustment to the caps on discretionary funding, appropriations for other programs might have to be reduced to make up for the higher budgetary costs of credit programs. Further, if a FCRA approach was replaced by a fair-value approach for a purpose other than recording costs in the federal budget—such as part of a requirement that fees on loans to small businesses be set so that those loans would have no cost on a fair-value basis—then costs for users of some programs would be increased.

**Question.** In your 2012 report, CBO analyzed 103 loan and loan guarantee programs, of which almost three-quarters were discretionary programs. The report stated that, overall, discretionary programs scored under the Federal Credit Reform Act have a subsidy rate of -2 percent. However, under Fair Value accounting, many discretionary programs would have a positive subsidy rate, or a cost. How much would a change to Fair Value accounting impact the defense and non-defense discretionary Budget Control Act caps? Wouldn't a change in accounting rules trigger a sequestration?

**Answer.** Last year, CBO analyzed the potential effects of legislation that would have amended the Federal Credit Reform Act of 1990 to require that, beginning in fiscal year 2017, the cost of loans or loan guarantees be estimated on a fair-value basis, using guidelines set forth by the Financial Accounting Standards Board, and recognized in the budget accordingly.[13] A fair-value approach to accounting for the cost of federal loans and loan guarantees would produce estimates of costs that either correspond to or approximate the value of those loans or guarantees to buyers in the private market.

CBO found that if fair-value procedures had been used to estimate the cost of credit programs in 2014, the total deficit would have been about $50 billion greater than the deficit as measured using current estimating procedures. That increase would have been split between the mandatory and discretionary portions of the budget:

- On a FCRA basis, CBO estimated, net subsidies for mandatory credit programs would have reduced the federal deficit by about $20 billion in 2014. On a fair-value basis, those programs would have increased the deficit by about $10 billion, for a swing of roughly $30 billion.

- Using a FCRA approach, net receipts from discretionary credit programs reduced the estimated cost of appropriations in 2014 by about $10 billion. Using a fair-value approach, CBO estimates, those same programs would have required appropriations of about $10 billion, for a swing of roughly $20 billion.

If fair-value procedures were implemented, the budget would record increased budget authority and outlays for mandatory programs; fully funding them on a fair-value basis would require no further Congressional action. However, the estimated net cost of legislative proposals for establishing new mandatory credit programs or expanding existing programs (such as student loans) would generally be larger using fair-value procedures than they would be on a FCRA basis.

13. Ibid.

To account for the higher subsidy costs that would result if future appropriations for federal credit programs were measured on a fair-value basis, H.R. 1872 would have clarified that the caps on discretionary appropriations set forth in the Budget Control Act of 2011, as amended, would be adjusted upward. The Deficit Control Act provides the Office of Management and Budget with authority to adjust caps on discretionary funding to account for "changes in concepts and definitions."[14] Without such an adjustment, appropriations would have to be reduced to make up the $30 billion difference, or sequestration would be triggered. CBO cannot predict whether the Office of Management and Budget would choose to make an adjustment to the discretionary caps (using the authority in the Deficit Control Act) for a change to fair-value accounting. Discretionary credit programs are all categorized as nondefense in the budget, so only nondefense discretionary funding would be affected.

**Senator Baldwin**

**Question.** I am concerned about the impact on federal spending and on access to coverage in states, like my home state of Wisconsin, that have not expanded their Medicaid programs under the Affordable Care Act (ACA). Instead of expanding our BadgerCare program, our Wisconsin Governor kicked thousands of individuals off Medicaid with a promise to transition them to coverage in the ACA's Marketplace. While a number of these individuals obtained coverage, not all of these vulnerable Wisconsinites were able to enroll in the Marketplace and may remain uninsured. Can you please describe the federal budgetary effects as a result of states like Wisconsin that do not expand Medicaid coverage under the ACA?

**Answer.** States that choose not to expand Medicaid coverage under the ACA will have more uninsured people and fewer beneficiaries in Medicaid and the Children's Health Insurance Program—lowering federal costs—and more people receiving subsidies for health insurance through exchanges—raising federal costs—than they would if they had expanded Medicaid coverage. In 2012, CBO projected that, because of the decision by some states not to expand Medicaid coverage under the ACA, the net cost to the federal government of the insurance provisions of the ACA would be reduced by $84 billion over the 2012–2022 period: Federal spending for Medicaid and CHIP would be $289 billion less because of those choices, whereas the estimated costs of tax credits and other subsidies for the purchase of health insurance through the exchanges (and related spending) would be $210 billion more.[15] Another $5 billion in savings would stem from changes in other components of the budget estimates.

Those estimates from 2012 reflected CBO's projections at that time of the approximate shares of the affected population residing in states that would fall into different broad categories—ranging from no expansion to an expansion encompassing the income threshold established by the ACA. CBO has not undertaken a more recent analysis comparing the effects of states' choices with what would have occurred if all states had expanded Medicaid coverage.

**Question.** After the Supreme Court decision in 2012, CBO released updated estimates of the budgetary effects of the health insurance coverage provisions of the ACA, which projected that the average annual cost per Medicaid enrollee in 2022 will be $6,000, while the

14. See sec. 251(b)(1) of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended (codified at 2 U.S.C. §901).

15. Congressional Budget Office, *Estimates for the Insurance Coverage Provisions of the Affordable Care Act Updated for the Recent Supreme Court Decision* (July 2012), **www.cbo.gov/publication/43472**.

analogous cost per exchange enrollee will be $9,000. I am concerned that as a result of states' decisions not to expand Medicaid, federal taxpayers will pay more per enrollee who ends up in Marketplace coverage, but who would otherwise be eligible for Medicaid under the ACA. Can you please provide an updated analysis of the difference in federal costs, per enrollee, for an individual enrolled in Marketplace coverage and an analogous Medicaid enrollee?

**Answer.** CBO has not updated its analysis of costs per enrollee for Medicaid versus subsidies provided through exchanges per enrollee for comparable people. The agency intends to do so during the next few months and to release the results as soon as they are available.

### Senator Grassley

**Question.** In conversations with my staff you have indicated that you are working on a conflict of interest policy that includes disclosures of potential conflicts from external consultants including those who provide input to the Panel of Health Advisors and the Panel of Economic Advisors. Will the documents submitted by these advisors be available to the Speaker of the House of Representatives, House Minority Leader, Senate Majority Leader, Senate Minority Leader or the Chair and Ranking Members of the House and Senate Budget Committees? If so, how? If not, please provide statutory authority for withholding documents from these officials.

**Answer.** Under its current policies, CBO considers whether members and potential members of CBO's panels of advisers are engaged in political activity that might influence their perspective on issues for which CBO is seeking their advice. If someone is known to have accepted a political appointment or joined a political campaign, he or she is generally asked to leave the panel or is not asked to serve on it while that activity is taking place and, depending on the nature of the activity, for some period afterward.

In late 2014, CBO began the process of formalizing and expanding this practice into a policy that will involve sysrematic disclosure to the agency by panelists and people being considered for the panels of substantial political activity, significant consulting work directly related to the policy development work of the Congress, and other significant financial interests. The process of developing the policy is ongoing but has not been completed at this time; the agency is currently consulting with the staff of the budget committees about the details of the policy. The next meeting of one of CBO's panels is scheduled for June 2015, and the agency intends to have the new policy in place before that date.

### Senator Perdue

**Question.** Dr. Elmendorf, could you please provide the following information for the Senate Budget Committee—a projection of the yearly spending outlays from 2026 through 2046 for the following areas: 1. Net Interest, 2. Social Security, 3. Medicare and Medicaid, 4. Federal Share of Federal Employee Retirement.

**Answer.** CBO produces a *Long-Term Budget Outlook* annually. The supplemental data to the most recent volume, provided in the table below, show long-term projections of outlays as percentages of economic output for the following categories of spending: Social Security; Medicare; the combination of Medicaid, the Children's Health Insurance Program, and

**Projected Spending Under CBO's Extended Baseline as of July 2014**

Percentage of Gross Domestic Product

| Fiscal Year | Social Security | Medicare[a] | Medicaid, CHIP, and Exchange Subsidies[b] | Other Noninterest Spending | Net Interest | Total Spending |
|---|---|---|---|---|---|---|
| 2026 | 5.8 | 3.5 | 2.8 | 7.3 | 3.5 | 22.9 |
| 2027 | 5.9 | 3.5 | 2.8 | 7.3 | 3.6 | 23.2 |
| 2028 | 6.0 | 3.6 | 2.9 | 7.2 | 3.7 | 23.5 |
| 2029 | 6.1 | 3.7 | 2.9 | 7.2 | 3.8 | 23.7 |
| 2030 | 6.2 | 3.8 | 3.0 | 7.2 | 3.9 | 24.0 |
| 2031 | 6.2 | 3.9 | 3.0 | 7.1 | 4.0 | 24.2 |
| 2032 | 6.3 | 4.0 | 3.1 | 7.1 | 4.1 | 24.5 |
| 2033 | 6.3 | 4.1 | 3.1 | 7.1 | 4.1 | 24.7 |
| 2034 | 6.4 | 4.2 | 3.1 | 7.0 | 4.2 | 24.9 |
| 2035 | 6.4 | 4.3 | 3.2 | 7.0 | 4.3 | 25.1 |
| 2036 | 6.4 | 4.4 | 3.2 | 7.0 | 4.4 | 25.4 |
| 2037 | 6.4 | 4.5 | 3.3 | 6.9 | 4.5 | 25.5 |
| 2038 | 6.4 | 4.6 | 3.3 | 6.9 | 4.6 | 25.7 |
| 2039 | 6.3 | 4.6 | 3.4 | 6.8 | 4.7 | 25.9 |
| 2040 | 6.3 | 4.7 | 3.4 | 6.8 | 4.8 | 26.0 |
| 2041 | 6.3 | 4.8 | 3.4 | 6.8 | 4.8 | 26.1 |
| 2042 | 6.2 | 4.9 | 3.5 | 6.8 | 4.9 | 26.3 |
| 2043 | 6.2 | 5.0 | 3.5 | 6.7 | 5.0 | 26.4 |
| 2044 | 6.2 | 5.0 | 3.6 | 6.7 | 5.1 | 26.6 |
| 2045 | 6.2 | 5.1 | 3.6 | 6.7 | 5.2 | 26.7 |
| 2046 | 6.2 | 5.2 | 3.6 | 6.6 | 5.3 | 26.9 |

Source: Congressional Budget Office.

Note: The extended baseline generally reflects current law, following CBO's 10-year baseline budget projections through 2024 and then extending the baseline concept for the rest of the long-term projection period.

a. Outlays for Medicare represent net Medicare spending (gross Medicare spending minus offsetting receipts, primarily premium payments by Medicare beneficiaries).

b. Outlays for the category "Medicaid, CHIP, and Exchange Subsidies" represent federal outlays for Medicaid, the Children's Health Insurance Program, and health insurance subsidies provided through the exchanges established under the Affordable Care Act.

exchange subsidies; other noninterest spending; and net interest.[16] Federal spending on retirement programs for federal employees is included in the category of other noninterest spending and is not projected separately.

CBO's most recent long-term budget projections are based on the agency's April 2014 baseline. Updated long-term projections, based on CBO's most recent 10-year baseline projections, will be available this summer.

**Question.** Dr. Elmendorf, on page 133 of "The Budget Economic Outlook: 2015-2025", the CBO projected the impact on the deficit if real GDP growth is 0.1 percentage point lower per year than anticipated. Could you provide the impact to the deficit over the 10-year period if the real GDP increases by 0.5 percentage points and 1 percentage point greater than anticipated?

16. Congressional Budget Office, "Long-Term Data Projections" (supplemental material for *The 2014 Long-Term Budget Outlook*, July 2014), **www.cbo.gov/publication/45308.**

**Answer.** If real (inflation-adjusted) growth in GDP was 0.5 percentage points higher for each of the next 10 years than CBO has forecast, the deficit would be about $1.6 trillion lower over that period; if annual real GDP growth was a full percentage point higher during that same period, the deficit would be about $3.3 trillion lower, CBO estimates.

Those estimates are extrapolations of CBO's "rules of thumb"—that is, of the ways that economic changes might affect the agency's baseline budget projections. Such rules provide a rough sense of how differences in individual variables, taken in isolation, would affect budget totals; they are not, however, substitutes for a full analysis of the implications of alternative economic forecasts. For example, a substantially different rate of economic growth would probably also affect many other economic variables, including interest rates and inflation.

CBO's rules of thumb are roughly symmetrical, so an average growth rate of real GDP that is 0.1 percentage point lower than expected would have about the same budgetary effect as an average growth rate that is 0.1 percentage point higher. In addition to being symmetrical, the rules are also roughly scalable for moderate differences in growth rates, so a difference in economic growth five or 10 times larger than 0.1 percentage point corresponds to a change in the deficit that is five or 10 times larger, respectively.

**Senator Wyden**

**Question.** Americans' paychecks have barely improved during the recovery and the December jobs report if anything represented a step back on the wage front. What does the CBO forecast hold for average wage growth over the next ten years? A decade from now, will middle class workers feel like they've gotten ahead and seen a rise in their standard of living? What does CBO foresee happening to the gap between average incomes and incomes at the very top of the distribution over the budget window? What policies do you think have the most promise for narrowing the income gap over time, without doing harm to the economy?

**Answer.** CBO projects stronger growth in hourly labor compensation over the next several years than was observed in 2014. That pickup is consistent with the agency's projection of firms' stronger demand for workers. To some degree, firms can attract unemployed or underemployed workers without increasing compensation. However, as slack in the labor market diminishes and firms must increasingly compete for workers, CBO projects that growth in hourly compensation will pick up. (When slack exists, labor resources are underused and many workers are unemployed or working fewer hours than they would like.) That increase in compensation will boost labor force participation (relative to what would otherwise occur) and thus the number of available workers, thereby moderating the overall increase in compensation growth.

Specifically, CBO expects the employment cost index for total compensation of workers in private industry to increase at an average annual rate of 3.6 percent from 2015 through 2019, compared with an average of about 2 percent over the past several years. The growth of other measures of hourly labor compensation, such as the average hourly earnings of production and nonsupervisory workers in private industries, is similarly expected to increase. CBO anticipates that earnings will grow faster for higher-income people than for others during the next decade—as they have for the past several decades.

Simultaneously achieving the goals of reducing inequality and not reducing economic output would be difficult and would generally involve a combination of policies. For example, the combination could include an increase in spending on federal programs for lower-income

people, or a reduction in taxes on such people, in ways that would strengthen incentives to work and save or that would increase the productivity of low-skilled workers. Such changes in fiscal policy would increase federal budget deficits and thereby reduce private investment over the long term, so other policy changes would be necessary to avoid reductions in economic output. Those additional policies would need to reduce spending or raise revenues in ways that discouraged work and saving or diminished productivity *less* than the positive effects for low-income people and low-skilled workers created by the other policies. Whether the net effect on incentives or productivity resulted in increased or decreased output would depend critically on the specifics of the policies involved. Other combinations of policies might also achieve those two goals.

**Question.** One of the core tenets of the Budget Control Act of 2011 (BCA), as you know, was the idea that if the so-called Super Committee failed, the resulting sequestration would be divided equally between defense spending and nondefense discretionary spending. That idea of parity is very important to many of us up here, so I just want to clear on this issue of fairness. To maintain the original intent behind the BCA, wouldn't Congress need to keep defense spending within its BCA cap for FY 16 – and beyond – or to permit nondefense spending to exceed its cap by the same amount as the excess in defense spending?

**Answer.** Allowing either defense or nondefense discretionary funding to exceed the amounts prescribed in the BCA would require new legislation. In keeping with its mandate to provide objective and nonpartisan analysis, CBO does not attempt to assess whether new laws would be consistent with the intent of current law.

**Question.** Former Ways & Means Chairman Dave Camp and the Treasury Department have identified among the trillion dollars of tax expenditures that the tax treatment of derivatives is particularly inefficient and abusive. I know you are nor allowed to advocate for specific policies, so let me ask this theoretically: is it possible for lawmakers to eliminate several of the most flagrant tax loopholes without compromising broader tax reforms goals of higher economic growth and improved efficiency? Follow-up: Can a tax reform proposal that broadens the tax base, lowers top tax rates, and raises revenue compared to baseline also boost economic growth?

**Answer.** In CBO's view, it is possible for lawmakers to reduce some tax expenditures—that is, exclusions, deductions, preferential rates, and credits that cause revenues to be lower than they would otherwise be for any underlying structure of tax rates—while also improving economic efficiency and increasing economic growth. Likewise, it is possible for a comprehensive tax reform to broaden the tax base, lower top rates, raise revenues above the amounts projected in CBO's baseline, and boost economic growth. However, the effects of reducing any tax expenditure and the effects of any comprehensive tax reform would depend upon the details of the policy changes. Regarding derivatives in particular, CBO has not analyzed the potential effects of changes to their tax treatment.

**Question.** Since 2010, CBO has continued to lower its future projections of spending by federal health care programs, including Medicare, Medicaid, CHIP, and coverage related provisions of the ACA. All the while, CBO has estimated that the number of uninsured Americans will decrease compared to its projections prior to 2010. Dr. Elmendorf, what impact has this slowdown in spending had on our annual deficits, national debt, and Medicare trust fund balance?

**Answer.** In August 2010, CBO projected that gross federal spending on the major health care programs over the 2013–2015 period would be $2.98 trillion. That category of spending includes Medicare (excluding receipts from premiums and certain payments from states), Medicaid, the Children's Health Insurance Program, and subsidies offered through health insurance exchanges and related spending. In January 2015, including the actual results for 2013 and 2014, the agency estimated that such spending would total $2.80 trillion over that three-year period, about $180 billion (or about 6 percent) less. That lower spending has decreased federal deficits and debt and bolsrered Medicare's finances relative to CBO's earlier projection.

Moreover, CBO currently anticipates that federal health care spending in future years will also be below what the agency had previously projected. That change improves the outlook for deficits, debt, and Medicare's finances. For example, apart from the effects of legislation and revisions to the agency's economic forecasr, CBO has revised downward projected federal spending for Medicare (net of premiums paid by beneficiaries and other offsetring receipts) and Medicaid between 2011 and 2020 by more than $1 trillion since the summer of 2010. Those revisions have reduced projecred expenditures from Medicare's Hospital Insurance (Part A) trust fund. However, CBO and JCT also anticipate that the income flowing into that trust fund in future years will be below what the agency had previously projected because of lower payroll tax revenue. As a result, between August 2010 and January 2015 CBO revised its projection of that trust fund's balance in 2020 only slightly—from $195 billion to $208 billion.

**Question.** Over the past several years, annual Medicare spending growth has been at historically low levels. Does CBO believe this slowdown in the tate of growth compared to prior CBO projections is a temporary hlip or a "level change" in spending trends? What impact has this slowdown had on our long-term budget picture, both in terms of just the Medicare program and also total federal spending?

**Answer.** CBO's projections of Medicare spending are subject to a considerable degree of uncertainty. A particular challenge currently is assessing the extent to which the recent slowdown in the growth of health care spending can be attributed to temporary factors such as the recession or, instead, to more enduring developments. Studies have generally concluded that some of the observed reduction in growth cannot be linked directly to the weak economy, although they differ considerably in their assessment of the relative importance of other factors. In August 2013, CBO released a paper that reviewed the observed slowdown iu growth in Medicare spending between the 2000–2005 period and the 2007–2010 period.[17] That review suggests that demand for health care by Medicate beneficiaries was not measurably diminished by the financial turmoil and recession and that, instead, much of the slowdown in spending growth was caused by other factors affecting beneficiaries' demand for care and by cbanges in providers' behavior.

Accordingly, over the past several years, CBO has substantially reduced its 10-year and long-term projections of spending per person for Medicare, and those reductions have also lowered CBO's projections of total federal spending. For example, over the past five years CBO has reduced its projection of Medicare outlays (net of premiums paid by beneficiaries and other offsetting receipts) in 2020 by about $120 billion, or about 14 percent, reflecting that slowdown. (That amount excludes revisions made in response to legislarive action and to the

17. Michael Levine and Melinda Buntin, *Why Has Growth in Spending for Medicare Fee-for-Service Slowed?* Working Paper 2013-06 (Congressional Budget Office, August 2013), **www.cbo.gov/publication/44513**.

economic outlook.) CBO projects that slower rates of growth will persist for some years to come, although the rate of growth in spending per person is expected to rebound somewhat from its recent very low level.

**Question.** CBO has continued to lower its projections for per-beneficiary Medicaid spending since 2010. How much lower is spending for Medicaid under the January 2015 baseline relative to 2010 and isn't it the case that these reductions are primarily due to lower-than-previously projected per-beneficiary spending growth rather than the 2012 Supreme Court decision making health reform's Medicaid expansion an option for states?

**Answer.** Since August 2010, CBO has lowered its projection of federal Medicaid outlays in 2016 from $416 billion to $360 billion. The change is the result of a collection of factors, including the effects of revisions to CBO's economic projections, the Supreme Court decision that made the expansion of eligibility for Medicaid under the ACA optional for states, federal administrative actions, the availability of new data, and numerous improvements in modeling by CBO and the staff of the Joint Committee on Taxation.

Although the expansion of health insurance coverage enacted in 2010 is substantially increasing the *number* of Medicaid beneficiaries, CBO has reduced its 2016 projection of Medicaid spending per beneficiary. The slowdown in the growth of health care costs that has been experienced by private insurers, as well as by the Medicare and Medicaid programs, has been sufficiently broad and persistent to persuade CBO to significantly lower its projections of federal health care spending per beneficiary, although analysts' views differ as to how much of the slowdown is attributable to the recession and its aftermath and how much to other factors.

**Question.** On p. 114 of the *Budget and Economic Outlook: 2015 to 2025*, CBO notes that it has revised down its estimate of corporate income tax receipts by $169 billion over ten years compared to its August 2014 forecast, owing to the increasing pace of international corporate tax avoidance strategies such as corporate inversions. Can you tell me how large—even just as an order of magnitude—is the anticipated revenue loss over ten years from corporations inverting or re-domiciling overseas? Next, can you tell me how much worse CBO feels the situation has gotten since the August forecast—that is, what portion of that $169 billion downward revision is roughly due to CBO's expectation of a greater volume of corporate inversions over the budget window?

**Answer.** CBO expects that the corporate tax base will erode over the 2015–2025 period as a result of certain strategies that corporations will continue to follow to reduce their income tax liabilities. One strategy that erodes the corporate tax base is to decrease the share of business activity that occurs in C corporations (whose income is subject to the corporate tax) while increasing the share that occurs in pass-through entities such as S corporations (whose income is subject to the individual tax). Another strategy is to decrease the amount of income that is taxed in the United States through a combination of approaches, including corporate inversions and other actions, that allow an increasing share of income to be allocated to foreign affiliates rather than to their U.S. counterparts.[18] CBO expects that the increasing

18. Under a corporate inversion, a U.S. corporation can change its country of tax residence, often by merging with a foreign company. Inversions reduce U.S. corporate tax revenue both because the inverted U.S. corporation no longer must pay U.S. taxes on earnings in other countries and because a corporation can shift additional income out of the United States through the use of intercompany loans and the resulting interest expenses.

adoption of such strategies will result in progressively larger reductions in corporate income tax receipts.

As reflected in CBO's baseline, corporate income tax receipts will be about 5 percent lower by 2025 than they would be without that erosion of the corporate tax base over the next decade. Slightly over half of that amount—about 3 percentage points, or $15 billion in 2025—stems from a combination of strategies that decrease the amount of income that is taxed in the United States.

Since releasing its baseline projections in August 2014, CBO has reduced its estimates of corporate income tax revenues by $169 billion over the 2014–2024 period to reflect technical factors—those unrelated to recently enacted legislation or to changes in the economic outlook. About one-quarter of that reduction reflects updated estimates of the effects of strategies, such as corporate inversion and other actions, that will decrease the amount of corporate income that is taxed in the United States.

**Question.** Dr. Elmendorf, I think all lawmakers are interested in better understanding how dynamic scoring is going to work going forward. To better educate us, I have three questions.

Based on my understanding of the House Rules package, major pieces of legislation will be given a conventional score broken out for each of the ten years in the budget window and a dynamic score, also broken out for each year, and the total score for a bill will be its conventional score plus its dynamic score. But House Rules are less clear on how the long-term budgetary impact of major legislation will be quantified – something we care very much about in the Senate owing to rules like the Byrd Rule meant to arrest legislation that might contribute to long-term fiscal profligacy. All that the House Rules say is that CBO and JCT will provide a "qualitative assessment" of the budgetary impact of the bill for the second and third decade. Can you tell us whether CBO and JCT will be able to give us an actual number or series of numbers for the cost of major legislation in the second and third decade? Or a percentage of GDP with a plus or minus sign? Please be specific in your answer.

Could CBO please provide us with a mocked-up example so that we better understand how these scores will be presented? Please have the example include conventional dynamic scores for the first ten years and the qualitative assessment for the second and third decades.

Can you help us understand how dynamic scoring will work in practice? For example, in terms of design, generally what would a major piece of legislation that is supposed to help students afford college need to do to receive a positive dividend as it were from a dynamic score? Generally, what would a bill that provides job training or expands apprenticeships need to do to receive such a positive dynamic score? Finally, what about a bill that cuts corporate tax rates and pays for the reduction by repealing accelerated depreciation and similar accelerated cost recovery provisions?

**Answer.** This year, the House of Representatives adopted a rule that requires CBO and the staff of the Joint Committee on Taxation to include the budgetary feedback of any macroeconomic effects of some major pieces of legislation in cost estimates for that legislation to the extent practicable.[19] The rule instructs the agencies to include a quantitative estimate of that feedback in estimates for the next 10 years and a qualitative assessment of that feedback for the following two decades. The rule applies specifically to bills that would cause a gross

19. Section 2(c) of H. Res. 5, adopted on January 6, 2015, added clause 8 to Rule XIII.

change in revenues or direct spending greater than or equal to one-quarter of 1 percent of GDP—an amount equal to about $45 billion in 2015—in any year during the next ten years. The rule does not apply to appropriation acts. The rule also states that the Chairman of the House Budget Committee may request that cost estimates for other legislation include macroeconomic effects as well. The rule will affect CBO's presentation of estimates and analysis of different types of proposals.

*Presentation of Estimates.* An example of a possible summary table for a cost estimate that includes macroeconomic effects is shown below. However, CBO anticipates that the form in which the agency provides this information to the Congress will evolve over time depending on what sort of presentation seems most useful. Such cost estimates will include all of the information that typically would be included if macroeconomic effects were not incorporated in the analysis, as well as additional information related to the macroeconomic effects themselves and the uncertainty surrounding those effects. For example, if applicable, CBO would provide separate estimates for on-budget and off-budget effects, including macroeconomic effects to the extent possible. (Off-budget effects include changes in Social Security spending and revenues as well as in spending by the U.S. Postal Service.)

CBO expects that the specificity of the assessments that the agency will provide about the effects of legislation in later decades will vary depending upon factors such as the amount of time CBO has to conduct the analysis, the complexity of the legislation being considered, the capability of the tools that CBO has to assess the legislation's effects, and the agency's judgment about the uncertainty of the analysis.

## Summary of Estimated Budgetary Effects of H.R. X.

By Fiscal Year, in Billions of Dollars

| | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2015-2020 | 2015-2025 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **Changes in Direct Spending, Without Macroeconomic Effects** | | | | | | | | | | | | |
| Estimated Outlays | X | X | X | X | X | X | X | X | X | X | X | X | X |
| | **Changes in Revenues, Without Macroeconomic Effects** | | | | | | | | | | | | |
| Estimated Revenues | X | X | X | X | X | X | X | X | X | X | X | X | X |
| | **Net Increase or Decrease (-) in the Deficit, Without Macroeconomic Effects** | | | | | | | | | | | | |
| Estimated Impact on Deficit | | | | | | | | | | | | | |
| On-budget | X | X | X | X | X | X | X | X | X | X | X | X | X |
| Off-budget[a] | X | X | X | X | X | X | X | X | X | X | X | X | X |
| | **Budgetary Impact of Macroeconomic Effects** | | | | | | | | | | | | |
| Estimated Impact on Deficit | X | X | X | X | X | X | X | X | X | X | X | X | X |
| | **Net Increase or Decrease (-) in the Deficit, With Macroeconomic Effects** | | | | | | | | | | | | |
| Estimated Impact on Deficit | X | X | X | X | X | X | X | X | X | X | X | X | X |

Source: Congressional Budget Office.

Note: Cost estimates for legislation show estimated changes in direct spending and revenues that would result from enacting the legislation but not any estimated interest costs or savings arising from changes in the amount of borrowing by the federal government. To be consistent with that approach, the estimated effects on federal interest payments included in the budgetary impact of the macroeconomic effects of legislation reflect only the effects of changes in interest rates and exclude the effects of changes in the amount of borrowing.

a. Off-budget effects include changes in Social Security spending and revenues as well as in spending by the U.S. Postal Service.

A qualitative assessment of effects in later decades might look something like this:

- Including macroeconomic effects, CBO expects that the legislation would (increase/decrease) the deficit during the 2015–2025 period and would (increase/decrease) it in the following 10 years; those (increases/decreases) in the following 10 years would probably be (larger/smaller) than the ones projected for the 2015–2025 period.

In some situations, CBO might conclude that it has sufficient basis to provide some quantitative information about a subsequent decade, perhaps along the lines of one of the following:

- Including macroeconomic effects, the legislation would (increase/reduce) cumulative deficits by about 0.X percent of GDP over the decade following the 2015–2025 period.

- Including macroeconomic effects, the legislation would (increase/reduce) cumulative deficits by about $X billion over the decade following the 2015–2025 period.

*Analysis of Different Types of Proposals.* CBO has not analyzed the macroeconomic effects of proposals to help students pay for a college education, to provide job training, or to change the taxation of business income. In general, the estimated effects of a legislative proposal on budget deficits will be more favorable if the proposal is expected to lead to greater economic output, holding all else equal.

Broadly speaking, increases in federal spending tend to boost output in the short term by boosting total demand for goods and services. In the long term, increases in federal investment—spending in categories such as physical capital, education and training, and research and development—tend to have two sorts of effects on economic output. Increased federal investment—if not offset by decreases in other spending or increases in taxes—raises government borrowing, which tends to "crowd out" private investment, lowering output in the long term. However, increased federal investment also raises productivity in various ways, which tends to boost output in the long term—although considerable uncertainty exists about the size and timing of the increase in output that results. (Funding for federal investment is usually provided in appropriation bills, which are not covered by the House rule.) Thus, the macroeconomic effects of increases in federal investment would depend on the specific nature of the investment, and the net effects in the long term might differ from those in the short term.

Changes in tax policy that would not affect deficits but would change some tax rates could also affect output, and macroeconomic modeling by JCT and CBO incorporates such effects. For example, changing effective marginal tax rates would affect output: Lower marginal rates tend to increase output, and higher rates tend to reduce output. Moreover, economic activity is affected not only by the rates at which capital investments are taxed but also by how uniformly such investments are taxed. If some capital investments receive more favorable tax treatment than others, additional resources will be directed to those types of investment even if other types would be more productive. Thus, changing the uniformity of taxation can potentially affect productivity and output: Increased uniformity would tend to increase output, and less uniformity would tend to reduce output. The ultimate effect would depend on the specifics of the policy.

**Question.** Last year, Congress acted to modify the TANF program to account for scoring changes related to the TANF baseline. It is unclear to me when CBO notified Congress of these changes and which Committees received notification. What is the process by which CBO notifies Members of Congress when scoring projections of specific programs are expected to change? I understand that the major budget projections are typically issued in January and updated in August of each year, bur for smaller programs or program subsets, is there a formal process through which Members and Committee of jurisdiction are notified of updating scoring techniques or projections? Specifically: Which Committees are notified? Is there a standard time frame CBO uses when making such notifications (e.g., CBO notifies Congress at least one year in advance of the scoring change coming into effect)?

**Answer.** CBO usually publishes three sets of baseline projections each year (in the winter, spring, and summer), all of which are released publicly. In general, for the year following the publicarion of the spring baseline, CBO estimates the costs of legislation using that baseline. It is relatively rare to have a change in baseline treatment for an existing program because the rules governing construction of the baseline are established in law. Nonetheless, new legislation, actions by the Administration, or new information concerning individual programs can sometimes lead to conceptual changes in the baseline projections that CBO prepares.

When CBO is considering a significant change in scoring procedures, or in the way that it will approach baseline projections for a particular program, the agency consults with the Senate and House budget committees and then promptly informs the budget committees and the committees of jurisdiction about any significant change that is made. There is no standard time frame for such notifications; however, CBO attempts to give as much notice as possible when such changes will cause projections of future spending to deviate significantly from the most recent baseline projections. Because CBO does not change the baseline used for budget enforcement purposes during the course of a legislative session (except to update for enacted legislation, certain court rulings, and any definitive new administrative actions such as final rules), the agency has generally informed committees about significant forthcoming conceprual changes before completion of a new set of baseline projections.

When each set of baseline projections is completed, detailed reports showing projections for each budget account are provided to budget committee staff and to any other Congressional staff who request such information. For example, such account-level reports are generally circulated (often by budget committee staff) to the staff of other committees, showing the baseline projections for programs within each committee's jurisdiction. In addition, CBO's analysts communicate regularly with staff on the budget committees, authorizing committees, and appropriations committees.

In the case of the Temporary Assistance for Needy Families (TANF) program, CBO changed its baseline projection in February 2014 for two aspects of the baseline: Welfare Research Grants and the TANF Contingency Fund.

*Welfare Research Grants.* The Social Security Act authorizes TANF and Welfare Research Grants. TANF provides cash assistance, work support, and other services to some low-income families; the Welfare Research Grants program supports research about TANF. Lawmakers provided about $17 billion in funding for TANF and $15 million for Welfare Research Grants in fiscal year 2014 and the same amounts for most of the years in the decade before

that. Those programs had been scheduled to expire numerous times over the past decade and were extended and provided with additional funding. In fiscal year 2015, lawmakers provided about the same amount of funding for TANF as in the previous year but did not reauthorize Welfare Research Grants as a separate program and instead set aside $15 million for research from TANF's funding.

In baselines prior to the one published in February 2014, CBO considered Welfare Research Grants to be part of the TANF program, even though spending for the research grants appears in a different Treasury account within the budget. But in the latter part of 2013, after observing that the Welfare Research Grants were subject to sequestration but TANF was not, CBO concluded that Welfare Research Grants should be considered a separate program. That distinction was important for the baseline projections because the Balanced Budget and Emergency Deficit Control Act of 1985 states that if a mandatory program is scheduled to expire and is expected to have outlays greater than $50 million in the last year of authorization, it should be assumed to continue in the baseline. Thus, when the Welfare Research Grants account was considered to be a part of TANF, it was assumed to continue in CBO's baseline, along with other funding for TANF; as a separate program, its funding was assumed to cease. If a program is assumed to continue in the baseline, then a cost estimate for its extension reports no net effect on the deficit. If a program is assumed to cease in the baseline, then a cost estimate reports that the deficit would increase if it was extended. When proposals for extensions of TANF and Welfare Research Grants were considered after February 2014, CBO estimated a cost of $15 million for extending the research grants for one year.

Because the change to the treatment of the Welfare Research Grants program was conceptual, CBO first consulted—in September 2013—with the staff of the Senate and House budget committees. As the staff of the budget committees raised no concerns, CBO then communicated its intention to change the baseline to the staff of the Senate Committee on Finance and the House Committee on Ways and Means, also in September 2013.

*TANF Contingency Fund.* CBO's February 2014 baseline also reflected a reduction in projected budget authority for the TANF Contingency Fund. Authorization for the Contingency Fund was scheduled to expire at the end of fiscal year 2014, but CBO's baseline incorporated the assumption that it would continue (again, consistent with the rules established by the Deficit Control Act). The baseline projections for the Contingency Fund were based on the expected outlays for the current year, which is the same assumption that CBO had used when the fund was previously set to expire at the end of fiscal year 2009. However, projected spending from the fund in 2014 had been reduced by about $14 million because some states had not spent the funds that had been allocated to them. Therefore, CBO reduced its baseline projection for each subsequent year by that amount. In that case, CBO changed its estimate of future spending but not the methodology for projecting funding for the expiring program. CBO's projections of spending for almost every budget account change at least a bit from one baseline to another, and committees are not notified of such changes in advance.

### Senator Corker

**Question.** Director Elmendorf, in 2009 you sent an analysis to Congress about how provisions within the Affordable Care Act would impact the premiums for Americans. In that analysis you discussed the impact on premiums for those individuals who would be purchasing insurance on the exchange, in the nongroup or individual market. In your

analysis, you stated that the estimate for "the average premium for new nongroup policies would be about 10 percent to 13 percent higher in 2016 than the average premium for nongroup coverage in that same year under current law." You go on to state that this figure is based on the fact that new mandates and regulations for specific levels of coverage would increase average premiums by 27 to 30 percent in 2016, absent the mitigating factors you cite, such as your assumption that young and healthy people would enroll. Do you agree that this analysis suggests that if Congress was looking for ways to reduce the cost of insurance due to the Affordable Care Act, reducing the mandates and regulations could give Americans as high as a 30 percent discount?

**Answer.** The extent of coverage that an insurance policy provides is an important determinant of its premium. Because people often purchased less extensive coverage in the nongroup market under prior law, reducing the federally mandated scope and actuarial value of insurance coverage could reduce premiums in that market substantially. (The actuarial value is the share of costs for covered benefits that an insurance plan pays, on average; plans at the "silver" level specified in the ACA have an actuarial value of about 70 percent, for example.) The amount of the reductions in premiums would depend critically on the details of any alternative, however, and those reductions would probably cause corresponding increases in the average out-of-pocket costs that enrollees incur when they receive care (although the precise ways that insurers and enrollees might respond are difficult to predict). By contrast, in the market for group or employment-based coverage—which accounts for about 85 percent of the private insurance market—the effects on premiums of changing those provisions of the ACA would probably he small or negligihle because such coverage generally met the ACA's requirements before that law was enacted or is exempt from them.

In 2009, CBO estimated the effects on premiums of a proposal that was very similar to the ACA.[20] At that time, the agency found that the provisions of that proposal governing the scope of benefits provided and the actuarial value of the coverage would increase average premiums for policies sold in the nongroup market in 2016 by between 27 percent and 30 percent, holding other factors equal. Although the effects of the ACA as enacted were expected to be similar, and CBO has continued to track nongroup premiums, the agency has not updated its estimate of the impact on those premiums (relative to those under prior law) and doing so would involve taking into account a broad range of factors that have affected the path of premiums in the interim. For example, overall growth in health care spending has been much slower than CBO had expected in 2009, and insurers have been more aggressive than CBO anticipated in designing nongroup plans with limited networks of providers to minimize their costs and premiums.

Reducing the required scope of benefits or actuarial value would reduce nongroup premiums, on average, but the effects would depend on the specific features of the proposal and the ways in which its provisions would interact with other aspects of current law. In particular, many enrollees in nongroup coverage now receive subsidies that limit the share of income they have to pay for coverage when they purchase a specified "silver" plan, so a proposal would need to specify whether and how such subsidies were provided—because that would affect how much people pay for coverage and what type of coverage they choose.

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20. See Congressional Budget Office, *An Analysis of Health Insurance Premiums Under the Patient Protection and Affordable Care Act* (attachment to a letter to the Honorable Evan Bayh, November 30, 2009), **www.cbo.gov/publication/41792**.

Reducing the extent of required benefits and actuarial values also would increase the amounts that enrollees have to pay for their care out of pocket, on average, by amounts roughly corresponding to the decrease in premiums. However, the effects on specific individuals would depend upon their use of health care services. Although premiums for plans offering less extensive coverage would probably be lower for all enrollees, people who used more health care services would tend to pay more in premiums and out-of-pocket costs combined, whereas people who used fewer health care services would pay less, on average. Again, the extent of such effects would depend greatly on the specific features of any proposal to change regulations governing mandated benefits and actuarial values.

**Question.** As federal expenditures on healthcare reach an historic percentage of our increased outlays over the next 10 years, has there been any analysis on the corresponding trend regarding individual healthcare spending? In other words, as the federal government shoulders more and more of the healthcare burden, has individual out of pocket spending decreased at all?

**Answer.** CBO does not track national health expenditures (NHE) as closely as it analyzes the components of those expenditures that are directly relevant to the federal budget, but the NHE projections developed by the Office of the Actuary in the Centers for Medicare & Medicaid Services shed light on these questions. Those projections show that the share of costs paid by the federal government will increase over time; as a result, the *share* of costs paid privately will be smaller than it is today—though the dollar *amount* of those private payments is expected to rise.

Specifically, the Office of the Actuary's projections indicate that the share of health care spending financed by businesses, households, and other private sources will decrease from about 59 percent in 2008 to about 52 percent in 2023, and the share that is financed by federal, state, and local governments will increase correspondingly from 41 percent to 48 percent—with nearly all of that increase reflecting a rise in the share of costs that is financed federally.[21] The share of NHE that is paid either by private health insurance or through out-of-pocket payments made when care is received (but excluding premium payments) is also projected to decline, from about 46 percent in 2008 to about 42 percent in 2023.

A significant share of health care spending in the private sector is subsidized through provisions in the tax code, primarily through the tax exclusion for employment-based health insurance, which is not reflected in the reported totals for NHE.[22] Because of that exclusion, most payments that employers and employees make for health insurance coverage are exempt from payroll and income taxes. CBO estimates that the federal cost, or tax expenditure, associated with that exclusion—including the effects on revenues from both payroll and income taxes—was roughly $250 billion in 2013, equal to nearly one-quarter of spending on private health insurance that year. Including those costs would increase the share of NHE that was financed by the federal government in 2013 by about 9 percentage points. Although

21. See Andrea M. Sisko and others, "National Health Expenditure Projections, 2013–23: Faster Growth Expected With Expanded Coverage and Improving Economy," *Health Affairs*, vol. 33, no. 10 (October 2014), pp. 1841–1850, http://dx.doi.org/10.1377/hlthaff.2014.0560.

22. See Congressional Budget Office, *The 2014 Long-Term Budget Outlook* (July 2014), pp. 26–28, www.cbo.gov/publication/45471.

CBO has not projected the costs of all subsidies for health care provided through the tax code, the agency estimated in 2009 and 2010 that the ACA and similar proposals would increase the federal government's budgetary commitment to health care—defined as the sum of net federal outlays for health programs and tax preferences for health care.[23]

**Question.** Specifically, the new federal mandates and regulations imposed by the Affordable Care Act, have limited the ways insurance companies can differentiate their products and control the cost of healthcare. Deductibles now are one of the few tools available to companies to hold down premium prices, and as a result, higher deductibles are now common on the exchange. Have there been any studies that have looked at how consumers out of pocket costs have changed as a result of the implementation of this law?

**Answer.** Out-of-pocket costs for consumers depend partly on whether they have insurance and partly on the extent of the coverage they have. A variety of studies have tried to examine changes over time in out-of-pocket payments and cost-sharing requirements. For example, as noted above, the Office of the Actuary at CMS develops estimates and projections of national health expenditures, including our-of-pocket payments that consumers make when they receive care. According to its most recent analysis, "out-of-pocket expenditures [were] projected to decline by 0.2 percent [in 2014], largely because of expanded insurance coverage" through Medicaid and nongroup plans purchased via health insurance exchanges (also known as marketplaces).[24]

Comparing the deductibles for exchange plans with deductibles for plans offered in the nongroup market under prior law is challenging because a number of factors may affect any differences thar are observed. Exchange plans generally offer coverage with an actuarial value that equals or exceeds 60 percent, which is roughly the average actuarial value of coverage that was typically purchased in the nongroup market previously.[25] Thar finding suggests that the deductibles for exchange plans may often be lower than was typical in the nongroup market (though higher than was typical in group or employment-based coverage). At the same time, there has been a general shift toward plans with higher deductibles in ptivate insurance markets, which would have to be factored into any analysis of the ACA's effects. According to one recent survey, for example, the share of people under age 65 with privare health insurance coverage who were enrolled in a high-deductible health care plan rose from about 23 percent in 2009 to about 34 percent in 2013.[26] CBO expects that trend to continue but has not specifically analyzed the effects of the ACA on plans' deductibles and other cosr-sharing requirements.

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23. See Congressional Budget Office, cost estimate for H.R. 4872, the Reconciliation Act of 2010 (March 20, 2010), pp. 14–15, **www.cbo.gov/publication/21351**; and *Measuring the Effect of Reform Proposals and the Federal Budgetary Commitment to Health Care* (October 2009), **www.cbo.gov/publication/24986**.

24. See Andrea M. Sisko and others, "National Health Expenditure Projections, 2013–23: Faster Growth Expected With Expanded Coverage and Improving Economy," *Health Affairs*, vol. 33, no. 10 (October 2014), p. 1848, **http://dx.doi.org/10.1377/hlthaff.2014.0560**.

25. Jon R. Gabel and others, "More Than Half of Individual Health Plans Offer Coverage That Falls Short of What Can Be Sold Through Exchanges as of 2014," *Health Affairs*, vol. 31, no. 6 (June 2012), pp. 1339–1348, **http://content.healthaffairs.org/content/31/6/1339.abstract**.

26. Michael E. Martinez and Robin A. Cohen, *Health Insurance Coverage: Early Release of Estimates From the National Health Interview Survey, January–June 2014* (National Center for Health Statistics, December 2014), **www.cdc.gov/nchs/data/nhis/earlyrelease/insur201412.pdf**.

# THE PRESIDENT'S FISCAL YEAR 2016 BUDGET PROPOSAL

**TUESDAY, FEBRUARY 3, 2015**

UNITED STATES SENATE,
COMMITTEE ON THE BUDGET,
*Washington, D.C.*

The committee met, pursuant to notice, at 10:03 a.m., in Room SD–608, Dirksen Senate Office Building, Hon. Mike Enzi, chairman of the committee, presiding.

Present: Senators Enzi, Grassley, Sessions, Crapo, Graham, Portman, Toomey, Johnson, Ayotte, Corker, Perdue, Sanders, Wyden, Stabenow, Whitehouse, Warner, Merkley, Baldwin, King, and Kaine.

Staff Present: Eric M. Ueland, Republican Staff Director; and Warren Gunnels, Minority Staff Director.

## OPENING STATEMENT OF CHAIRMAN ENZI

Chairman ENZI. Good morning. I will call this hearing to order.

Today, we have the testimony from OMB Director Shaun Donovan of the President's budget plan for the upcoming 2016 fiscal year.

When it comes to the budget, we all know that we have lived for too many years with too many blown deadlines, failed submissions, heightened crises, and last-second deals. Together, both parties, both chambers, and both ends of Pennsylvania Avenue have allowed this way of doing business to become the new normal for how we operate. It is long past time to restore regular order to our budget process, and that begins with following the budget timeline laid out in the law.

Yesterday, after six years, the President's budget was released on time. My congratulations to Mr. Donovan, who headed up that effort. I appreciate the work you and your team did to make that happen. Being on time is a first small step toward restoring regular order on the budget and it can help our constituents understand a little better what is happening in Washington.

However, our constituents also understand these truths. I know it from traveling Wyoming and visiting with people and visiting with people around the country. They think we spend too much. They think we tax too much. They think we regulate too much, that we borrow too much, and their biggest worry is that we owe too much.

Every year since the President took office, he has proposed the same approach to the fiscal challenge facing our government. He wants to spend more. He wants to tax more. He wants to regulate

more. He wants to borrow more. And, he wants us to owe more and more and more and more. His plans always end up with the Americans holding the tab, stuck with the deficits and debt as far as the eye can see. And, incidentally, I do not like that word "deficit." It gets confused with debt. Deficit is our overspending.

I promised at our first hearing that I would follow the numbers, look at the President's budget, and here is what those numbers show. First, the tax man cometh. Under the President's proposal, taxes head higher, a total of two-and-one-tenths trillion dollars higher. This boost comes on top of the one-and-seven-tenths trillion in taxes he has already imposed during his Presidency, and I can tell you that nothing good for individuals ever comes from three-and-eight-tenths trillion dollars in additional taxes.

Next, spending explodes. The President wants to add $259 billion of new spending in the next fiscal year and two-and-four-tenths trillion over the next ten years. That is a 65 percent increase in ten years. Let us see. Two-and-one-tenths trillion in higher taxes, two-and-four-tenths trillion in higher spending. That is still overspending. The President hides what he is doing when he talks about reducing the deficit. It sounds like the debt will go down. No, the deficit is the overspending that we do.

Did you ever hear of someone being able to buy something with the interest they saved? So, the interest payments skyrocket. Annual interest costs would more than triple, from $229 billion today to $785 billion in 2025, and I think that is at a pretty conservative interest rate. Interest remains the fastest growing item in the budget, but provides little in the way of benefit for our constituents. Did you ever hear of anybody being able to spend the interest that they have to pay? At the end of his plan, annual interest costs would be larger than the President's proposed spending for national defense, Medicaid, or the combined total of all non-defense agency spending.

Finally, the President's plan adds $8.5 trillion to the debt. Over the next ten years, cumulative overspending would amount to five-and-seven-tenths trillion in new debt, with the Federal debt climbing to $26.3 trillion in 2025. Based on projected population figures, this would mean every man, woman, and child in America would owe almost $76,000 in payments on President Obama's debt. That is compared to $56,000 per person today. That is $20,000 per person more that everybody in America is going to owe. I mean, the child that is born today gets figured into that same cost, that same debt.

Altogether, these were not the numbers I was looking for. I meant it when I said last week that we must confront spending. Bring the overspending to an end and ultimately balance the budget. The President's proposal fails on all three elements of the mission. I will listen to the administration make its case on why it is best to ignore balancing the budget, but with 24 States already agreeing that the solution is to gather together to write a balanced budget requirement into our Constitution and with more States thinking about it, this is a mission we do not dare duck. Yes, 24 States have already passed a Constitutional Convention to balance the budget. More than ten others are in the process of passing that

same one. Twenty-four plus ten is 34. That is enough to have a Constitutional Convention and force us to do it.

We also cannot fail our constituents. Our nation needs a larger and more successful middle class, not a larger, more intrusive and fiscally foolish Federal Government. The latest quarterly GDP figures released Friday—and I do not think GDP really means much to the rest of the nation, what they are interested in is how much we take in and how much we spend and how much more debt that results in—but, the latest quarterly GDP figures released Friday demonstrate firmly that in the United States, more Federal spending, more Federal overspending, called deficits more interest costs and more debt do not yield a robust economy.

Our economy still bobs in the backwater of too slow growth while jobless rate edges down and equity markets head up. The number of people who are underemployed or have abandoned looking for work continues to be too high. As Senator Sanders says, we have a deficit of employment. Wages are stagnant. Household wealth has collapsed. Too many worry that the American dream is no longer theirs and will not be there for their children and grandchildren. Failure of our economy to recover is the President's record over the last six years. He has left too many Americans behind.

But, in looking ahead, families and individuals need a Federal Government with a fiscal plan that helps create the climate for good jobs and good wages. Americans need to have confidence that there is work to be had, jobs to be found, and paychecks to be earned. Most importantly, they need to know that a strong and successful future is theirs again all around the country.

It is not too late for the President to join us in making the future brighter by submitting a new plan that does not mortgage our future to pay for the present. If the President changes course, we can work together to ensure that Americans have the strongest possible economy, so competition to hire employees drives up wages and benefits, so that we have a solid economy and an economy in government.

I said that people do not understand the GDP. They do understand spending more than we take in. We maxed out our credit cards. We do not have a mortgage payment. Maybe we should have a mortgage payment where we monthly pay down some of our debt and then use the interest we save to pay down even more. That is how people buy houses. I looked at the numbers on that. There is no possibility of that at the present time.

We keep coming up with brilliant ideas for new ways to spend to fill in gaps in gifts that we have not been giving. We do not really take a look at what we already have and need to weed out things that do not work. We pretend everything we do is perfection, and with guilty conscience, we try to do more. Instead, we should be doing better.

We have over 250 programs that are no longer in authorization, but we continue to spend the money on them, even though we do not look at them to see what they do and how they operate and what they should be doing and if they even ought to exist anymore. That means we have exceeded the time that we guaranteed we would pay for them. Last year, we had to vote on eleven-hundred billion dollars in spending. I prefer to say "eleven-hundred bil-

lion"—I think it is more honest than one-and-one-tenths trillion. We spent $468 billion more than the eleven-hundred billion. If you overspend what you can control by almost 50 percent, are we not buying like it was a department store sale? Colleagues, that is the sort of change that Americans really believe in.

Senator SANDERS.

**OPENING STATEMENT OF SENATOR SANDERS**

Senator SANDERS. Mr. Chairman, thank you very much.

The good news is that our country has made substantial economic progress over the last six years since President Bush left office. Instead of losing 800,000 jobs a month, as we were during the final months of the Bush administration, we are now creating some 250,000 jobs a month and are seeing steady job growth over the last 58 months. Instead of having a record-breaking $1.4 trillion deficit, as we did when President Bush left office in January 2009, the Federal deficit has been cut by more than two-thirds. Six years ago, the world's financial system was on the verge of collapse. Today, that is certainly not the case.

While we can be proud of what we have accomplished in the last six years, one would be very wrong not to appreciate that there is also a lot of very bad news in our economy, especially for working families. Most significantly, the simple truth is that the 40-year decline of the American middle class continues. Real unemployment is not 5.6 percent, it is 11.2 percent if one includes people who have given up looking for work or people who are working part-time when they want to work full-time. We do not talk about this issue, but youth unemployment today is close to 17 percent, and African American youth unemployment is over 30 percent. Real median family income has declined by nearly $5,000 since 1999.

Incredibly, and I ask my colleagues to listen to this, despite huge increases in productivity, the median male worker, that man right in the middle of the economy, now earns $783 less than he did 42 years ago, after adjusting for inflation. The median female worker now makes $1,300 less than she did in 2007. Shamefully, we continue to have, by far, the highest rate of childhood poverty of any major country on earth.

In the midst of this tragic decline of America's middle class, there is another reality, and this is the main point I want to make this morning, and that is that the wealthiest people and the largest corporations are doing phenomenally well. The result: The United States today has more income and wealth inequality than at any time since the Great Depression. Today, incredibly, the top one percent own almost as much wealth as the bottom 90 percent. Let me repeat that, because I think what Senator Enzi was talking about has got to be put into the broad context, and that is that the top one-tenth of one percent today own almost as much wealth as the bottom 90 percent. Today, one family, the Walton family of Walmart, owns more wealth than the bottom 40 percent of the American people, some 120 million Americans.

In terms of income, what we have seen in recent years is that virtually all new income is going to the top one percent. Last year, the 25 top hedge fund managers earned more income than 425,000 public school teachers, and that gap between the very, very rich

and everyone else grows wider. The fact of the matter is that over the past 40 years, we have witnessed an enormous transfer of wealth from the middle class to the top one percent. In other words, we are witnessing the Robin Hood principle in reverse. We are taking from working people and the poor and giving to the very, very wealthy.

From 1985 to 2013, the share of the nation's wealth going to the middle class has gone down from 36 percent to less than 23 percent. If the middle class had simply maintained the same share of our nation's wealth as it did 30 years ago, it would have $10.7 trillion more in cumulative wealth than it does today.

While the middle class continues to shrink, while millions of Americans are working longer hours for low wages, while young people cannot afford to go to college, while children in America go hungry, we have seen since 2009 that the top one percent has experienced an $11.5 trillion increase in wealth.

Mr. Chairman, what we are talking about is not just a moral issue, it is an economic issue. Seventy percent of our economy is based on consumer spending, and when working people do not have disposable income, when they are not out buying goods and products, we are not creating the jobs that we need.

The debate that we are having this morning will have a profound impact on the lives of the American people. Many of my Republican friends are in favor of cutting Social Security, cutting Medicare, cutting Medicaid, cutting nutrition programs for kids, while providing huge tax breaks for millionaires and billionaires. That is their idea of moving the economy forward. In my view, on the other hand, if we are serious about rebuilding the disappearing middle class, reducing income and wealth inequality, and strengthening Social Security, Medicare, and Medicaid, we need a budget that creates millions of jobs, raises wages, makes college affordable, and demands that the wealthiest people start paying their fair share.

In all of these matters, the President's budget begins to move us in the right direction. At a time when almost all of the new income gains go to the top one percent and when corporate profits are at an all-time high, the President's effort to end egregious tax loopholes that benefit the wealthy and large corporations while providing tax breaks for working families is exactly the right thing to do. At a time when real unemployment is over 11 percent, the idea of increasing substantially investment in our infrastructure and creating hundreds of thousands of jobs is the right thing to do. At a time when 20 percent of our kids are living in poverty, the President's budget triples the Child Care Tax Credit to $3,000 per child and makes an additional billion dollars' investment in Head Start exactly the right thing to do. At a time when more Americans are unable to go to college, the President proposes the first two years of community college to be free, that is exactly the right thing to do.

Let me conclude, Mr. Chairman, by saying this. If we are serious about figuring out exactly how we are going to pay for what this country needs, we might want to take a hard look at why major corporation after major corporation in some years pays absolutely zero in taxes. From 2008 to 2013, General Electric made nearly $34 billion in profit in the United States. Not only did it pay nothing

in Federal income taxes, it received a tax break of nearly—a tax rebate of nearly $3 billion, and the list goes on and on and on.

There is a lot to be done. Our job is to protect the middle class. Let us get to work doing that.

Chairman ENZI. Thank you, Senator Sanders.

Our witness this morning is Shaun Donovan, the 40th Director of the Office of Management and Budget. Prior to taking the role as head of OMB, Director Donovan served as President Obama's first Secretary of Housing and Urban Development. Director Donovan has a long public service career, both in Federal and local roles, including Commissioner of the New York City Department of Housing, Preservation, and Development, and as Acting Federal Housing Administration Commissioner during the transition between President Clinton and President Bush. His private sector experience includes work at the Community Preservation Corporation in New York City and as a Visiting Scholar at New York University. Director Donovan holds both Bachelor's and Master's degrees in public administration and architecture from Harvard.

Director Donovan, as the architect of the administration's budget, we look forward to what you have to say.

For the information of colleagues, Director Donovan will take about seven minutes for his opening testimony.

Director, please begin.

## STATEMENT OF HON. SHAUN DONOVAN, DIRECTOR, U.S. OFFICE OF MANAGEMENT AND BUDGET

Mr. DONOVAN. Chairman Enzi, Ranking Member Sanders, members of the committee, thank you for welcoming me here today to present the President's 2016 budget.

To echo your comments, Mr. Chairman, when I met with so many of you over the summer, one of the key themes everyone echoed was that we needed to get our budget process back into regular order, and I truly hope that this on-time budget that I am presenting today is the first step toward that regular order.

The budget comes on the heels of a breakthrough year for America and builds on our fiscal and economic progress, including the fastest job growth since the 1990s and the fastest sustained period of deficit reduction in 60 years. The budget is a blueprint for the President's vision for middle class economics in the 21st century. This means helping working families by making their paychecks go further, preparing Americans to earn higher wages, and making America the place where businesses decide to innovate, grow, and create good, high-paying jobs.

The budget shows that we do not have to choose between investing in the middle class and being fiscally responsible. First, because we cannot afford a return to mindless austerity, the budget proposes to end sequestration, fully reversing it for domestic priorities in 2016, matched by equal dollar increases for defense. By replacing sequestration with a combination of smart spending cuts, program integrity measures, and common sense loophole closers, the budget makes room for investments in our economy and our national security.

For example, on the domestic side, where sequestration would cut R&D to its lowest level since 2002, adjusted for inflation, the

budget supports cutting edge research like precision medicine, efforts to combat antibiotic resistance, and the BRAIN Initiative, which is helping to revolutionize our understanding of the human brain.

Likewise, rather than cutting inflation-adjusted national security funding to the lowest level since 2006, the budget makes responsible investments to protect our national security, restoring readiness and the investment in modernization needed to ensure America's continued technological edge.

I want to emphasize that every investment in the budget, including both the discretionary investments made possible by reversing sequestration and mandatory and tax changes, are more than paid for through spending or tax reforms. For example, the budget would provide new and expanded tax credits for middle class families and would more than pay for these investments by reforming capital gains taxation and making it more costly for the biggest financial firms to finance their activities with excessive borrowing.

It also uses one-time revenues from pro-growth business tax reform to pay for an ambitious six-year surface transportation proposal that will give States and localities the certainty they need to invest in infrastructure that will spur innovation and accelerate job growth.

Meanwhile, the budget also achieves $1.8 trillion in deficit reduction, primarily by focusing on the key drivers of our budget challenges, health care cost growth and inadequate revenue levels in the face of an aging population. Building on the historically slow rates of health care cost growth in recent years that have already significantly improved our fiscal outlook, the budget includes roughly $400 billion in health savings which grow significantly over time, raising about $1 trillion in the second decade.

The budget also raises about $640 billion in net revenue for deficit reduction from curbing inefficient high-income tax expenditures.

And, this year's budget again reflects the President's support for common sense comprehensive immigration reform along the lines of the bipartisan Senate-passed bill. Immigration reform would reduce deficits by almost $1 trillion over two decades while strengthening Social Security and growing the economy.

As a result of these measures, the budget maintains deficits well below the 40-year historical average during every year of the budget window. It meets the key test of fiscal sustainability, putting debt as a share of the economy on a downward path, showing that investments in accelerating growth and a strong middle class are compatible with strengthening the nation's finances. And, to ensure that our country remains strong and prosperous both now and in the future, it makes smart investments to give every American the chance to contribute to and share in the benefits of growth.

I look forward to working with Congress and this committee in the coming months. Thank you, and I would be glad to take your questions.

[The prepared statement of Mr. Donovan follows:]

**TESTIMONY OF**
**SHAUN DONOVAN**
**DIRECTOR**
**OFFICE OF MANAGEMENT AND BUDGET**
**BEFORE THE**
**SENATE COMMITTEE ON THE BUDGET**

**February 3, 2015**

Chairman Enzi, Ranking Member Sanders, members of the Committee, thank you for welcoming me here today and giving me the opportunity to present the President's 2016 Budget.

This Budget comes on the heels of a breakthrough year for America. Our economy is growing – in 2014, we added more jobs than in any year since the 1990s, and in 58 months we have created over 11 million jobs. Our unemployment rate fell 1.2 percentage points from the previous year, the largest annual decline in the last 30 years. For the first time in two decades, the United States has started producing more oil than it imports, and domestic natural gas production set a new record high in 2014. Today, America is an energy super power. Our manufacturing sector continues to experience its strongest period of job growth since the late 1990s, and our auto industry is thriving. Rising home prices are bringing millions of homeowners back above water, restoring nearly $5 trillion in home equity. The number of uninsured Americans has dropped by an estimated 10 million. And we've brought our deficits below 3 percent of GDP, less than the 40-year average.

This Budget builds on that progress by making needed investments that accelerate economic growth, and ensuring that all Americans have the opportunity to share in that growth. It helps middle-class families get ahead, with a package of tax cuts and targeted investments in child care, early education, and paid leave. It invests in helping workers gain the skills they need for the new economy, through job training, apprenticeships, and the President's proposal to make two years of community college free for responsible students. It builds a 21st century economy, with investments in manufacturing, infrastructure, and research and development. And it makes responsible investments in defense to protect our national security. We cannot afford a return to mindless austerity, so this Budget proposes to end sequestration, fully reversing it for domestic priorities in 2016, matched by equal dollar increases for defense. These investments are more than paid for with smart spending cuts, program integrity measures, and commonsense loophole closers. We don't have to choose between investing in our middle class and fiscal responsibility. This year's Budget supports the President's ambitious vision for supporting growth and opportunity, and does so while meeting key tests of fiscal sustainability: reducing deficits to below 3 percent of GDP, stabilizing debt as a share of the economy and putting it on a declining path. It achieves these goals by replacing mindless sequestration cuts with smart reforms, paying for all new investments, and achieving $1.8 trillion in deficit reduction primarily from reforms to health programs, the tax system, and our broken immigration system.

**Middle Class Economics for the 21st Century**

In last month's State of the Union, the President laid out his vision for middle class economics: restoring the link between hard work and opportunity, and ensuring that every American has the chance to share in the benefits of economic growth. To achieve this, the Budget helps working families make their paychecks go further, prepares hardworking Americans to earn higher wages, and creates the infrastructure that allows businesses to create good, high-paying jobs and thrive.

***Helping Middle-Class Families Get Ahead.*** Middle class economics for the 21st century means helping working families afford the cornerstones of economic security – child care, college, healthcare, a home, and a secure retirement, while also making sure that work pays.

Access to child care and early education not only supports healthy child development, but also supports parents struggling to balance work and family obligations. The Budget streamlines child care tax benefits and triples the Child and Dependent Care Tax Credit (CDCTC) for families with children under the age of five, while making the full credit available to middle class families. It provides $82 billion to make quality, affordable child care available to all eligible low-and moderate-income working families with young children through the Child Care and Development Fund (CCDF), expanding access to more than 1.1 million additional children under the age of four by 2025.

The Budget expands access to high-quality care for tens of thousands of additional infants and toddlers through Early Head Start and the Early Head Start-Child Care Partnerships, and provides over $1 billion in additional funding for Head Start to make sure children are served in full-day, full-year programs that research shows lead to better outcomes. Finally, it continues to support the President's Preschool for All initiative designed to ensure that all four-year olds have access to affordable, high-quality preschool, while also including additional discretionary funding for Preschool Development Grants that help pave the way for the broader Preschool for All goal.

When both spouses work, the family incurs additional costs in the form of commuting costs, professional expenses, child care, and, increasingly, elder care. To support and reward work, the Budget proposes a new $500 "second earner" tax credit, which will benefit 24 million dual-earner couples. It also proposes to expand the Earned Income Tax Credit for workers without children and non-custodial parents, while making permanent important EITC and Child Tax Credit (EITC) improvements first enacted in 2009. The Administration continues to support raising the minimum wage so hard-working Americans can earn enough to support their families and make ends meet -- raising the minimum wage is good for workers, their families, and for the economy. The President took an important step in this effort by signing an Executive Order (EO) to increase the minimum wage to $10.10 for those working on new and replacement Federal contracts. 17 States and the District of Columbia have passed increases in their minimum wage since the President called for an increase, and he stands ready to work with the Congress to pass legislation to increase the minimum wage for the rest of the workforce as soon as possible.

The Budget also recognizes that too many American workers must make a painful choice between caring for their families and a paycheck they desperately need. Last month, the President called on Congress to pass legislation that would allow millions of working Americans to earn up to seven days of paid sick leave per year. To support this proposal, the Budget provides $2 billion for a Paid Leave Partnership Initiative, which will allow up to five States to receive funds to cover the initial set up and half of the benefit costs of a paid leave program for three years, and a $35 million State Paid Leave Fund, to provide technical assistance and support to States that are still building the infrastructure they need to launch paid leave programs.

Since the full implementation of the Affordable Care Act (ACA) began, about 10 million Americans have gained health coverage. The Budget fully funds ongoing implementation of the ACA, which is helping to expand coverage, enhance competition, and increase affordability. The Budget also proposes a four year extension of the Children's Health Insurance Program (CHIP) through 2019, ensuring continued, comprehensive, affordable coverage for children of working parents who are not eligible for Medicaid. As the President recently announced, the Federal Housing Administration reduced annual premiums by half of a percent in January 2015, easing access to credit for housing and saving homeowners an average of $900 annually. The Budget also dramatically expands access to employer-based retirement savings options, including by automatically enrolling workers without employer-based retirement plans in Individual Retirement Arrangements (IRAs) through payroll deposit contributions at their workplace, giving 30 million additional workers access to a workplace savings opportunity. It would also ensure that long-term part-time employees can participate in their employers' retirement plans, and provide tax incentives to offset administrative expenses for small businesses that adopt retirement plans.

***Helping Americans Upgrade their Skills.*** Americans must be prepared with the skills and knowledge necessary to compete in the 21st Century economy, and the Budget invests in what works to improve student outcomes and to ensure our workforce has the skills it needs.

The Budget continues the work to make America a leader in elementary and secondary education, by promoting equity and opportunity for all students in elementary and secondary education and supporting teachers and school leaders. The Budget proposes a $1 billion increase from the 2015 enacted level for Title I, the Department of Education's largest K-12 grant program and the cornerstone of its commitment to supporting low-income schools with the funding necessary to provide high-need students access to an excellent education, and makes critical new investments in efforts to help develop and support teachers throughout their careers.

By 2020, an estimated two-thirds of job openings will require some postsecondary education and training, and the President is committed to making a college education affordable and accessible for everyone. The Budget invests $60 billion in the President's recently-announced America's College Promise initiative, which creates new Federal-state partnerships to provide two years of free community college to responsible students, while promoting key reforms to improve the

quality of community college offerings to ensure that they are a gateway to a career or four-year degree. If all states participate, an estimated 9 million students could benefit from this proposal. The Budget also ensures that the Pell Grant program remains a strong source of support for low- and moderate-income college students. Beginning in 2009, the Administration has increased the maximum Pell Grant by more than $1,000, to $5,775 in school year 2015-16. Since 2013, Pell Grants have been adjusted for inflation annually, but unless Congress acts, this will end in 2017 and the value of Pell Grants will start to erode. The Budget addresses this, supporting the continued indexing of Pell Grants. In addition, the Budget simplifies, consolidates, and expands education tax credits, cutting taxes for 8.5 million families and students, simplifying taxes for the more than 25 million families and students claiming education tax benefits, and providing students working toward a college degree with up to $2,500 of assistance each year for five years. Building on recent bipartisan legislation, the Budget also includes a proposal to significantly simplify the Free Application for Federal Student Aid (FAFSA).

As the economy changes, we must invest in training and employment programs that help American workers gain the skills they need to find good jobs. The Budget builds on the bipartisan Workforce Innovation and Opportunity Act (WIOA), increasing funding for core WIOA grants and providing $1.2 billion for in-person employment services that help unemployed workers find a job or the training they need to prepare for one. It provides $16 billion over ten years to double the number of workers receiving training through the workforce development system, with a focus on industries that are expected to experience significant growth in the coming decades, such as health care, energy, advanced manufacturing, and cybersecurity. Building on the success of the Trade Adjustment Assistance Community College and Career Training grants, the Budget includes $200 million to fund State expansion of postsecondary programs based on defined competencies for high-demand jobs, with strong employer partnerships. The Budget also acts on the findings of the Vice President's job-driven training review, emphasizing employer connections and expanding funding for evidence-based strategies like apprenticeship, a cost-effective pathway into the middle class. The Budget invests $2 billion to achieve the goal of doubling Registered Apprenticeships across the United States over the next five years.

***Creating a 21st Century Economy.*** Since 2010, America has put more people back to work than Europe, Japan, and all advanced economies combined. But creating a sustainable 21st century economy requires building the most competitive economy in the world, a place where businesses want to locate and hire. To ensure America remains a magnet for jobs, the Budget builds on investments in manufacturing and innovation including through clean energy technology programs and tax policies that position America as a global clean energy leader with a strong and modern energy infrastructure. To fix the Nation's roads and bridges and create more middle class jobs, it continues the progress toward building a 21st Century infrastructure. And to ensure our long-term competitiveness and growth, it provides robust investment in research and development (R&D).

The President has placed a high priority on bringing back the American manufacturing sector, which has added more than 750,000 new jobs over the past 58 months. Building on progress made in 2015 that included enactment of bipartisan legislation authorizing a network of manufacturing institutes, the Budget funds this network to bring together universities, the private sector, and the Government to invest in the development of new technologies and capabilities. Specifically, the Budget funds 45 manufacturing institutes across the country, including $350 million in discretionary funds to support seven new institutes in the Departments of Commerce, Agriculture, Defense, and Energy, and $1.9 billion in mandatory funding for the remaining 29 institutes. In addition, the Budget provides $2.4 billion for Federal R&D that directly supports the development and commercialization of advanced manufacturing technology, and calls on the Congress to work with the President to launch a public-private Scale-Up Fund to help emerging American-made advanced manufacturing technologies reach commercial scale production.

21st century businesses require 21st century infrastructure. To spur economic growth and encourage States and localities to invest in modern infrastructure, the Budget includes a $478 billion surface transportation reauthorization proposal. This proposal would ensure the health of the Highway Trust Fund for another six years and provide funding for needed additional investments by levying a one-time 14 percent transition toll charge on the untaxed foreign earnings that U.S. companies have accumulated overseas. The proposal will allow for increased investment to repair existing highways and bridges, while modernizing our infrastructure with new investments in bus, subway, rapid transit, light rail, and passenger rail systems. In addition, the Budget permanently authorizes the competitive TIGER grant program, which funds multi-modal, multi-jurisdictional projects that spur innovation and accelerate job growth. In addition to improvements to transportation infrastructure, the Budget proposes to expand broadband access by doubling funding for the BroadbandUSA initiative, which can help communities plan and deploy new community broadband systems, and for the USDA Rural Utilities Service, which provides broadband access in rural communities. Building on the success of the recent FCC auctions, which contributed more than $20 billion to deficit reduction and fully funded FirstNet, the Nation's first interoperable broadband public safety network for first responders, the Budget also continues to advance the President's goal of making available 500 megahertz of spectrum for commercial use by 2020 through actions such as freeing up Federally-held spectrum, fueling the expansion of wireless broadband.

Our long-term economic competitiveness depends upon continued robust investment in R&D, as we look to science and engineering to address our biggest challenges, from enhancing access to clean water and energy to ensuring the security of our Nation. Federal funding for R&D has helped lead to new products, capabilities, and industries, resulting in economic growth and the creation of highly-skilled jobs and products that benefit every American. The Budget provides $146 billion for Federal R&D, a 6 percent increase over 2015, including significant investments in basic research, which has the potential to drive the great discoveries of the 21st century. Specifically, the Budget provides $31.3 billion to support biomedical research at NIH, an amount sufficient to fund 10,000 new research grants and increase resources devoted to curing Alzheimer's, cancer, and other diseases. It also includes $1.2 billion to support a government-

wide effort to combat antibiotic-resistant bacteria, and $215 million to launch a Precision Medicine initiative to develop treatment approaches tailored to individual patients. To spur innovation and scientific advancement, the Budget proposes to reform and make permanent the Research and Experimentation tax credit, creating a single formula with an 18 percent credit rate to incentivize private sector R&D. In addition, the Budget invests more than $3 billion, a 4 percent increase over 2015, to equip more students with the 21st century skills they need to excel in science, technology, engineering, and mathematics (STEM).

Our long-term economic competitiveness also depends on our ability to tackle the challenge posed by our changing climate – the impacts of which are increasingly visible across the American landscape. Along our Eastern seaboard, a number of cities now flood regularly at high tide. The vast majority of the largest fires in modern U.S. history have occurred in just the last decade. In parts of the Midwest, higher temperatures will increase irrigation demand and exacerbate current stresses on agricultural productivity. And along the Mississippi and Missouri River Basins, numerous studies indicate increasing severity and frequency of flooding leading to disruptions to the Nation's inland water system. For the Federal Budget, this means escalating costs of disaster relief, flood and crop insurance, wildland fire management, and a host of other programs. And for those of us charged with making sound investment decisions, providing stewardship of the Federal budget over the long term, and supporting American economic competitiveness – taking action on climate is an imperative. This Budget does that, supporting action on climate by investing in cutting carbon pollution and in preparedness and resilience — providing necessary tools, technical assistance, and on-the-ground partnership to communities that are dealing with the effects of climate change today.

**Responsible Investments in Our National Security**

Today the United States is strong and well-positioned to seize the opportunities of a new century, but we must still safeguard our interests against the risks of an insecure world. This is a strategy-driven Budget that confronts global challenges with strong and sustained American leadership, directly supporting the President's forthcoming *National Security Strategy*.

The Budget requests $561 billion in base discretionary funding for national defense, including $534 billion for the Department of Defense (DOD), an 8 percent increase over FY 2015, as well as $46 billion in base discretionary funding for the Department of State and Other International Programs (OIP). These levels provide a responsible and sustainable alternative to current law, allowing for the restoration of readiness and investment in modernization needed to ensure America's continued technological edge. At the same time, the Budget continues to balance defense spending with our priorities here at home, calling for a smaller but more modern and ready military, and reiterating the need for reforms to force structure, compensation, and infrastructure to generate efficiencies critical to enhancing our national security.

The Budget funds the completion of the U.S. military's transition in Afghanistan from a prolonged combat mission to a mission of training, advising, and assisting the Afghan National

Security Forces and maintaining a necessary counterterrorism capability to continue targeting the remnants of al Qaeda. As we move beyond the large ground wars in Iraq and Afghanistan, we have responsibly drawn down our Overseas Contingency Operations (OCO) budget by $129 billion, from a peak of $187 billion in FY 2008 to the Administration's request of $58 billion this year. Furthermore, the Budget proposes to transition all enduring OCO costs to the base budget beginning in FY 2017 so that we can more fully and responsibly budget for our national security.

The Budget supports our continued fight to degrade and ultimately defeat the Islamic State of Iraq and the Levant (ISIL). In response to Russia's aggressive acts, it includes proposals for political, economic, and military support to NATO allies and partner states in Europe and to increase resilience within the governments and economies most targeted by Russian coercion. It also continues the progress made to reassert American leadership in Asia and the Pacific, aligning resources and activities to strengthen U.S. alliances, forge deeper partnerships with emerging powers, and pursue a productive relationship with China. Lastly, the Budget honors our commitment to America's veterans, providing a significant increase to ensure continued high-quality and timely health care, both through the Veterans Affairs system and via implementation of the Veterans Choice Act. The Budget also supports efforts to ensure veterans receive their earned benefits quickly and efficiently, to end veteran homelessness, and to help veterans and their families get good jobs, education, and access to affordable housing.

While our homeland is more secure, we must continue to learn and adapt to evolving threats and hazards. The Budget continues our risk-based, Whole of Community approach to homeland security, bringing together all levels of Government with other elements of our society to make sure America is resilient in the face of adversity. The Budget funds our Global Health Security Agenda and also our domestic preparedness efforts to more effectively respond to potential future outbreaks like Ebola that could follow a similarly devastating, costly, and destabilizing trajectory. Cyber threats targeting the private sector, critical infrastructure, and the Federal Government demonstrate that no system is immune to infiltration by those seeking to steal commercial or Government secrets or perpetrate malicious activity, and the Budget provides $14 billion to support cybersecurity efforts across the Government to strengthen U.S. cybersecurity defenses and make cyberspace more secure. These resources will allow the Government to more rapidly protect American citizens, systems, and information from cyber threats. Today's Border Patrol has the largest deployment of people, vehicles, aircraft, boats and equipment along the southwest border in its 90-year history. While our borders are more secure than ever before, the Budget continues investment in border security by maintaining U.S. Customs and Border Protection front line operations, and also provides $1 billion to support a comprehensive strategy for Central America designed to address challenges such as the lack of economic opportunity, the need for institutional reforms and the extreme violence that have resulted in an influx of migration from the region.

**Achieving Fiscal Sustainability and Promoting Sustainable Growth**

This year's Budget supports the President's ambitious vision for increasing growth and opportunity, and does so while meeting key tests of fiscal sustainability: reducing deficits to

below 3 percent of GDP, stabilizing debt as a share of the economy, and putting it on a declining path. It achieves two goals by replacing mindless austerity with smart reforms, paying for all new investments, and obtaining $1.8 trillion in deficit reduction primarily from health, tax, and immigration reforms.

***Ending Mindless Austerity.*** In 2014, we began to move away from manufactured crises and austerity, helping to lay the groundwork for stronger growth and job market gains. The Bipartisan Budget Act of 2013 ("Murray-Ryan") reversed a portion of sequestration and allowed for higher investment levels in 2014 and 2015. Over the last two years, we have seen the gains that are possible from coming together on a bipartisan basis to reverse mindless austerity. Not only has the Murray-Ryan agreement contributed to an improving job market and accelerating growth, but it created room for important investments in critical domestic priorities like early education programs, allowing for the creation of Preschool Development Grants and a 14 percent increase in Head Start, while also providing needed funds for national security.

Returning to the mindless austerity of sequestration in 2016 would bring discretionary funding to its lowest level, adjusted for inflation, since 2006. This is despite the fact that, since 2006, the U.S. population has grown by 7 percent, and costs in some key areas have grown much faster than inflation; for example, VA medical care costs have nearly doubled. Failing to make the investments described in the Budget would weaken America's security and our economy at a time of accelerating growth.

The Budget proposes to end sequestration, fully reversing it for domestic priorities in 2016, matched by equal dollar increases for defense. These investments are more than paid for with smart spending cuts, program integrity measures, and commonsense loophole closers – including, for example, targeted reforms to crop insurance programs; program integrity investments across a range of programs; and closing the "carried interest" tax loophole.

The proposed increases in the discretionary budget caps will make room for a range of domestic and security investments that will help move the Nation forward – including a number of the investments discussed above. The contrast between what results from mindless sequestration versus what can be achieved under the President's Budget is particularly stark in a few key areas:

- *Research and Development.* Under the 2016 sequester levels, assuming roughly current funding patterns, research funding adjusted for inflation would reach its lowest levels since 2002 – other than when sequestration was in full effect in 2013. The President's Budget would increase funding by nearly 6 percent over 2015, including investments in precision medicine, the Brain Initiative, and other areas.

- *Early Learning.* When sequestration last took full effect in 2013, 57,000 children lost access to Head Start, with enrollment falling to the lowest level since 2001. Researchers have established that supporting children during this critical stage yields benefits that far outweigh the costs of the investment. The President's Budget makes major investments in early learning on the discretionary as well as the mandatory side, including making

sure children can be served in full-day, full-year Head Start programs that research shows lead to better outcomes for kids.

- *National Security.* The Joint Chiefs have been very clear that a return to sequestration levels would significantly reduce the military's ability to fully implement the President's defense strategy. The military would be unbalanced and eventually too small and insufficiently modern to meet the needs of our strategy, leading to greater risk of longer wars with higher casualties for the United States and our allies and partners.

***Paying for all new investments.*** Every investment in the Budget – not only the discretionary investments made possible by reversing sequestration, but also the new and expanded tax credits for middle-class and working families, and mandatory investments that will expand access to community college and preschool – is fully paid for through spending or tax reforms. In particular, the Budget pays for many of its investments in helping middle class families get ahead through three important reforms to the tax system. First, it would eliminate what may be the largest single loophole in the tax code – a provision known as "stepped-up basis" that lets wealthy households avoid taxes on hundreds of billions in capital gains taxes each year. Second, it would raise the top capital gains and dividend rate for high-income households to 28 percent, the rate under President Reagan. Third, it reforms financial sector taxation to make it more costly for large, highly-leveraged financial firms to finance their activities with excessive borrowing, reducing risks to the broader economy.

***Deficit Reduction from Health, Tax, and Immigration Reform.*** While the Budget's new investments are paid for with smart reforms across a range of programs, as well as commonsense tax loophole closers, the $1.8 trillion in deficit reduction in the Budget is achieved primarily by focusing on the key drivers of our Budget challenges: health care cost growth and inadequate revenue levels in the face of an aging population. Specifically, the Budget includes:

- *$400 Billion in Health Savings.* Over the last few years, we've seen historically slow rates of health care cost growth, which are already yielding fiscal dividends. If we could maintain a substantial share of that slow-down, it would make a dramatic difference to the fiscal outlook going forward. The Budget includes about $400 billion in health savings that build on the ACA – complementing the Administration's other efforts on delivery system reform. Notably, the Budget's health savings grow over time – raising about $1 trillion in the second decade, and extending the Medicare Hospital Insurance trust fund solvency by approximately 5 years. Since the ACA's enactment, the Trustees' estimate of Medicare solvency has already improved by 13 years.
- *$640 Billion in Net Deficit Reduction from Tax Reforms.* The Budget raises about $640 billion net revenue for deficit reduction from curbing high-income tax expenditures in addition to those discussed above. These savings come from limiting tax benefits that are not efficient in achieving social goals, raising revenue without raising tax rates.
- *$160 Billion in Savings from Immigration Reform.* This year's Budget again reflects the President's support for commonsense, comprehensive immigration reform along the lines

of the bipartisan Senate-passed bill. In part because it helps balance out an aging population, immigration helps both the Budget – by almost $1 trillion over two decades – and the Social Security Trust Fund, closing about 8 percent of the Trust Fund shortfall and moving insolvency out two years. It also strengthens the economy, both by increasing the size of the labor force and by raising productivity.

Through these policies, the President's Budget further reduces the deficit and accomplishes the key fiscal milestone of stabilizing debt as a share of the economy and putting it on a downward path. The Budget maintains deficits well below the 40-year historical average of 3.2 percent of GDP during every year of the budget window. A key test of fiscal sustainability is whether debt is stable or declining as a share of the economy, resulting in interest payments that consume a stable or falling share of the Nation's resources over time. The Budget meets that test, showing that investments in growth and opportunity are compatible with also putting the Nation's finances on a strong and sustainable path.

**Creating a 21st Century Government**

In addition to achieving key metrics of fiscal responsibility, the Budget continues the Administration's efforts to make Government more effective and efficient. The President is committed to creating a Government that makes a significant, tangible, and positive difference in the economy and the lives of the American people, and to driving lasting change in how Government works. Consistent with our efforts to maximize the impact of taxpayer dollars, the Budget fully supports the President's Management Agenda, a comprehensive and forward-looking plan to modernize and improve government to ultimately deliver better, faster, and smarter services to citizens and businesses, making it more efficient every day.

To keep pace with the innovation and user experiences that the public expects, the Administration is working to leverage transformative IT to deliver world-class services to the American people. Building on last year's launch of the U.S. Digital Service, a small team of our Nation's best digital experts working to build the Federal Government's digital capacity, the Budget scales and institutionalizes this new approach to technology by providing funding to 25 agencies for the development of their own high-impact agency digital services teams. In addition, we continue to invest in PortfolioStat, a data-based review of agency IT portfolios that has helped the Government achieve more than $2.2 billion in savings over the past three years alone. The Budget proposes to streamline acquisition, opening contracts to small and innovative businesses, expanding benchmarking efforts and shared services platforms, and maximizing the Government's purchasing power through a new Category Management approach to procurement. It continues efforts to shrink the Federal real estate footprint, and invests in fostering a culture of excellence and developing the workforce the Federal Government needs for the 21st century.

Consistent with these efforts, the President is again renewing his request for reorganization authority, which would allow the Administration to submit plans to consolidate departments and agencies for fast track consideration by the Congress in order to cut costs. The Budget outlines a set of cross-government reorganizations that would make the Government more efficient and effective, including the consolidation of the two primary food safety agencies into one agency

responsible for inspections, enforcement, and outbreak response. The Budget also embraces evidence-based approaches, investing in evidence-building efforts, scaling successful interventions, and promoting greater use of data and research in policymaking and program management to achieve results. And the Budget invests in continued efforts to open data to drive economic growth, unlock opportunities for entrepreneurs, and open the door to innovative research that can improve program outcomes.

**Conclusion**

The President's 2016 Budget makes smart, responsible investments that will build on economic progress to date to accelerate our economic growth, while protecting our national security. It ensures that every American has the chance to share in the benefits of growth -- helping working families make their paychecks go further, preparing hardworking Americans to earn higher wages, and creating a thriving 21st century economy here at home. It does all this by rejecting mindless austerity and reversing sequestration, while still making progress in meeting the Nation's fiscal goal by focusing on the true drivers of debt and deficits. And it shows how we can build on the progress that has been made over the last five years and ensure that our country remains strong and prosperous, both now and in the future. I look forward to working with the Congress and this Committee in the coming months. Thank you and I'd be glad to take your questions.

Chairman ENZI. Wow. You did not even come close to seven minutes.

Mr. DONOVAN. I think I have come under my budgeted time.

[Laughter.]

Chairman ENZI. We do appreciate that. Now, we will turn to questions.

Last week, when CBO Director Elmendorf testified, he did a good job of simply answering the questions asked by Senators so that members on both sides had more questions that they could ask and get answers. I hope you will follow that model this morning, Director, so that we can all have as much asked and answered as possible.

As a reminder, I will alternate recognition between Republican and Democratic Senators, following seniority for those who were here when the hearing was gaveled to order. After that, I will recognize members based on order of arrival. If you are not here when your name is called, I will skip you but pencil you in at the end of the question list to be recognized after everyone who was in attendance at the gavel has the opportunity to ask Director Donovan questions.

With that, Director, I will begin with my first question. You testified that stabilizing the debt as a share of the economy and putting it on a declining path is a key test of fiscal sustainability. But, debt still goes up every year in the President's budget in dollar terms and shows little movement as a share of the economy. And, again, that is GDP, and I do not think people understand GDP. They do understand that we spend more than we take in, even though we are getting record revenue. So, why is it a sufficient goal to merely tread water on debt as a share of GDP?

Mr. DONOVAN. First of all, Senator, I think as any family would look at it, their finances are based on what they earn, and a key measure of what this country earns—

Chairman ENZI. Please turn your microphone on.

Mr. DONOVAN. I am sorry. Thank you. I apologize. I think, like any family in America, the key way they think about their finances is based on what they earn, and so GDP is really the measure of what this country earns. It is the size of our economy. And, most economists on both sides of the aisle really think of looking at these numbers as a share of GDP as the correct measures.

The other point I would make is that, as Director Elmendorf no doubt testified, under current projections under current law, over the next ten years, debt as a share of GDP would grow substantially to—in our baseline, we show it growing to almost 81 percent of GDP. And, so, with this $1.8 trillion of deficit reduction that our budget would achieve, we actually help to not just stabilize, but also begin to bring down the debt by the end of the window, and that is a substantial difference from our current path.

Chairman ENZI. In looking at it, the President's budget never reaches balance. At its low point, in 2017, the overspending is $463 billion, and that grows steadily from there, reaching $687 billion in 2025. To secure the middle class and any hope for future generations, we need to pay down the debt, and that is not possible with overspending this large. Can we pay down the public debt, that is,

have the dollar amount of debt outstanding be less than the amount in the year earlier without balancing the budget?

Mr. DONOVAN. Again, Senator, the key metric for fiscal sustainability that is not only the measure that we use in the administration but that is, I think, widely accepted is that deficits below three percent of GDP are critical for long-term sustainability. That is a measure that we met for the first time this year after record reductions in our deficits, over a two-thirds reduction since the President came into office. And, that will keep us in every year of the budget window below the 40-year average for deficits that this country has faced. And, so, we think we are hitting that key test of sustainability.

Chairman ENZI. Okay. Most of the people that I deal with think that if you spend more than you take in, that you have made a mistake. But, the Analytical Perspectives volume of the budget documents has an interesting table on page 32 entitled, "Trends in Federal Debt Held by the Public." That table shows interest costs as a percent of total outlays will increase steadily under the President's budget. Can this trend continue forever without compromising our ability to provide government services?

Mr. DONOVAN. I think what the long-term fiscal outlook chapter shows, in addition to what I have already said, is that we would stabilize the debt as a share of the economy not just over the ten-year window, but over the 25-year window, as well.

And, as I think we all recognize, what we are facing in this country is a real demographic challenge with the aging of the Baby Boom. The key thing that we need to do to ensure that we have long-run fiscal sustainability is focus on health care costs. We have seen the lowest growth in health care costs in 50 years over the last few years. We have many, many measures, including over $400 billion in savings from Medicare and Medicaid proposed in the budget that increase over time.

And, we need to recognize that we need to grow our workforce and our economy, and immigration reform is perhaps the single most important thing we can do there, and that will add to the sustainability over Social Security over time. And, so, we think we are attacking through this budget the key drivers of long-term deficit and debt.

Chairman ENZI. My time has almost expired. I heard your comment about health care costs going down. Last year, I had the Head Start folks come to me and complain that their budget was being cut seven-and-three-tenths percent instead of two-and-three-tenths percent. So, I checked on it and found that they were keeping most of the money in Washington instead of where the kids were and it got reversed and they got all of their money. But, what they found was their health care costs have gone up so much that they still could not add the kids back into the program. So, we have got a lot things we need to work on.

My time has expired. Senator Sanders.

Senator SANDERS. Thank you, Mr. Chairman.

Mr. Donovan, in case you have not been made aware, we have a philosophical divide on this committee of some degree. Many of my Republican colleagues believe that what is best for the country in the future is basically to cut, cut, cut, cut, cut Social Security,

Medicare, Medicaid, nutrition, et cetera, et cetera. Others of us do not think that that is what is best for working families in this country. So, I want to mention something to you.

My staff did some research, and what we found is that it turns out that major profitable corporation after major profitable corporation not only paid zero in a given year in Federal taxes, but, in fact, got rebates from the IRS. Just some examples.

From 2008 through 2013, General Electric made nearly $34 billion in profits in the U.S., and what was its tax break—what was its tax burden? Zero. In fact, it received a tax refund of nearly $3 billion.

Verizon, from that same period of time, made over $42 billion in the U.S. It received tax refunds of $732 million. In other words, they did not pay any taxes. They actually got rebates.

Now, I think the President's budget begins to address some of these issues. Can you talk to us, in your view, about whether or not it is appropriate that one large major profitable corporation after another pays zero in Federal income taxes?

Mr. DONOVAN. Well, Senator, I think we could all agree on a bipartisan basis that our current corporate tax code is more complicated than it needs to be, that it has a broad range of loopholes that create not just unfairness across companies, but also, frankly, make our economy less efficient and hold back economic growth.

And, so, we do support, and the budget lays this out, reform of our business tax system that would not only make it more fair, but in the long run would increase economic growth, and we would do that by closing a broad range of loopholes and actually lowering the basic rate from 35 percent down to 28 percent.

We think a particularly important piece of this is around international tax reform. The President has spoken out very clearly that the trend of inversions of companies, you know, buying small companies overseas and putting a domicile, relocating there, is a serious problem. This budget would not only close those loopholes to try to stop to the maximum extent possible companies moving overseas, it also creates more broadly an international tax system which would really make it more fair and level the playing field, bringing jobs back to the U.S.

Senator SANDERS. Thank you. Mr. Donovan, there will be, I suspect, a major debate coming forward on Social Security, and I happen to believe not only that we should not cut Social Security, but we should expand benefits. I suspect my Republican colleagues disagree. But, the first order of business done by the House Republicans was to pass a rule which could result in a 20 percent reduction in benefits for people who receive disability benefits, laying the groundwork for either cuts in disability benefits or, in fact, for Social Security for older people.

Your budget did not do that. You did what has been done 11 times in the past. It is what we call readjust. Social Security has enough money to pay all benefits for the next 18 years. You simply took money from one account and into the other. Why did you do that?

Mr. DONOVAN. Well, as you said, Senator, this small reallocation of Social Security taxes is the simplest, most direct way to ensure that, on a combined basis, both Social Security Trust Funds have

reserves available through 2033. This is a step that has been taken on a bipartisan basis under Democrats and Republicans. It has actually been done both ways, from Disability to the other Trust Fund and back to Social Security. And, so, we think this is the most simple and critical way—and remember, these are benefits that have been earned by folks paying in over time. We should not put them at risk of getting a 19 percent cut in their benefits after they paid into the system over their working years.

Senator SANDERS. Okay. Mr. Chairman, my time is almost out. I will yield the floor.

Chairman ENZI. Senator Grassley.

Senator GRASSLEY. I think the President's budget is an ideological statement based on the faith of government making decisions as opposed to individuals making decisions. I think it is based on a proposition that 535 people here in Congress are a heck of a lot smarter than 137 million taxpayers, and that gets to the issue of increasing taxes or not.

Quite frankly, I think the dynamics of the American economy—it is going to advance the economy much faster if you have 137 million taxpayers decide whether to spend or save and how to spend it and how to save it as opposed to those of us here in the Congress of the United States and the President of the United States making that decision.

And, it is not a question of bigger government or smaller government. It is a question of what does the most to expand and grow our economy, because what this country needs is not more tax rates, or more taxes. We need more taxpayers. And, that is going to happen by the capital investment that individuals make, not what the government spends. Private investment is going to really grow the economy.

We have a 50-year average that has said that if you have a one-dollar tax increase, it gives license to Congress to spend $1.13. That is not going to do anything about the deficit. A license to spend more money brings us further into the hole. You cannot raise taxes high enough to satisfy the appetite of Congress or any President, not just this President, to spend money. If a tax increase would go to the bottom line to reduce the deficit, that would be one thing. I think we might look favorable upon that. But, that is not going to happen.

And, I think you see that deficits matter. The President's budget speaks to deficits mattering. They have consequences, because the President's own budget shows that the cost of interest is going to go up from a little less than $300 billion a year to $800 billion a year.

So, we have a spending problem, not a taxing problem, and I do not see in this budget, and I suppose I could say this even about Republican budgets, that there does not seem to be a shame in increasing deficits, in this case, under this budget, by $8 trillion over a ten-year period of time.

So, this gets me to what the President has said publicly about the middle class. The President seems to believe that we need to deficit spend today and for the next ten years in order to, in his words, "invest in initiatives to help the middle class." However, CBO has analyzed in great detail the long-term consequences of

deficit spending. They found that in future years, a growing portion of people's savings will go towards buying government debt rather than towards investing in productive capital goods. That crowding out of investment would reduce the size of the nation's productive capital resources that produce economic benefits over time. The smaller capital stock would result in lower wages and incomes, making future generations worse off. Now, that is not my finding, that is CBO's finding.

So, two questions that you can answer at the same time. Does the President think the nonpartisan Congressional Budget Office is incorrect in stating that future generations will be worse off by taking no action to reduce deficits and debt? And, , would not reducing the debt burden of future generations be more prudent than ten more years of deficit spending and growing debt?

Mr. DONOVAN. Senator, we do take the spending and deficits and debt seriously. That is why we have taken action over the full six years of this President's time in office and achieved the fastest deficit reduction since immediately after World War II and brought deficits down below our 40-year average. In addition, we make further changes in this budget, both on the spending side and in other areas, that would reduce our debt by $1.8 trillion—our deficits by $1.8 trillion over those ten years. And, so, we do take that seriously.

But, we also take seriously that this country needs to invest in the things that are going to grow our middle class. We cut taxes for 44 million families by an average of $600 through this budget, and we do ask that where we have places in our tax code that are not only unfair but actually discourage economic growth, that we make changes to our tax code, as well, whether it is returning to the capital gains rate of 28 percent that was effective when President Reagan was in office, or to get rid of inefficiencies like the so-called capital gains stepped-up basis, where we are actually encouraging families, the wealthiest families, to hold assets in unproductive ways, and when an average American would have to pay tax on that because they could not hold it until their death, we are allowing the wealthiest families to basically hold those assets and never be taxed for capital gains.

And, so, we do believe that we need to focus on our deficits and debt. We do in this budget. We continue to make strong progress like we have over the last few years. But, we also recognize that we have to invest in our future, as well.

Senator GRASSLEY. Thank you, Mr. Chairman.

Chairman ENZI. Senator Wyden is not here. Senator Stabenow.

Senator STABENOW. Thank you, Mr. Chairman, and welcome, Director Donovan.

Mr. DONOVAN. Thank you.

Senator STABENOW. I have been on this committee for a while, and when I think about since 2009, you guys inherited a very big hole and have been stepping forward out of that hole for the last six years and I want to congratulate you. I remember when we were on this committee talking about the Simpson-Bowles Commission, a bipartisan commission that said we needed to cut $4 trillion in order to be able to get a handle on and stabilize the debt as a

share of the economy, and step by step by step, we are now at $3.3 trillion of the four. I would suggest that is pretty good.

And, the fact that we are now looking at less than two-thirds of the annual deficit, of what you inherited in 2009—less than two-thirds—less than two-thirds—I would suggest that is pretty good, too.

Eleven-point-two million jobs—I would like very much to have more—and nearly three million last year. But, I could not agree with you more that the only way that works is to stop talking about trickle-down economics and actually do something that makes sure the next steps are laser focused on the middle class.

So, before I ask my question, though, I also want to say that we talk a lot about debt and about how we should never spend more than we have. I would just suggest, I have a mortgage. When something is an important investment, we spend more than we have. We have a mortgage for a house. We have a car payment. And, as somebody who makes a lot of automobiles, I would welcome more people doing that.

[Laughter.]

Senator STABENOW. We put our kids through college, unfortunately with too much debt on college. Many, many colleagues here, colleagues on the other side of the aisle, felt going to war twice, and not paying for it, was a priority.

So, the issue is really how do we manage our debt and move forward and not have it overwhelm us. But we certainly set priorities for when we—for our families—choose to take on debt. So, it is a question of how we manage that.

I would like to move to the topic of health care and, first of all, to congratulate you on adding dollars for medical research and the BRAIN Initiative. One of the ways that we can bring down costs that will save millions of lives is to focus on brain research. One out of five Medicare dollars is spent on Alzheimer's—one out of five—one out of five. And, so, I am very encouraged and believe we should even be doing more in that area.

And, I want to talk about health care as part of bringing down costs. The latest CBO projections show that more Americans are finding full-time work and getting health care coverage. We know that fewer Americans are going into bankruptcy because of medical bills, a good thing. Tax credits that we passed are helping people afford coverage. People who already have insurance are actually getting what they are paying for now and cannot get dropped, and can get coverage even if they have a preexisting condition.

But, we are seeing an ongoing debate, and very soon, we will see even more of that here in the Senate, to reverse that, stripping insurance coverage from working Americans that will increase the debt. The House has voted over 50 times to repeal health reform. The Supreme Court is considering whether or not to have a process that would put millions of people into health care—without health care. So, could you talk about how the health care law has helped to drive down Medicare spending as well as the health care costs for Americans?

Mr. DONOVAN. Senator, I appreciate you focusing on this because it really is the single most important focus for, if we want to talk about long-run deficits, but also a critical thing for middle-class

families is affordable health care. And, the Affordable Care Act is working. We have now more than ten million less—fewer uninsured Americans, and more broadly, millions and millions of Americans who had health care before, health care insurance, but have actually seen, whether it is keeping their kids on their plans, not being kicked out because of preexisting conditions, and a broad range of things. So, we really have made progress.

On the fiscal side, what we have seen is the lowest health care cost growth in 50 years, and that has already improved our long-run fiscal picture dramatically. Just take CBO's numbers, where they say, just from improvements we have seen over the last few years, we are going to spend $190 billion less on Medicare and Medicaid in the year 2020 thanks to the lower growth in health care costs that we have already seen.

I think we can work together on a bipartisan basis to build on that. We have $400 billion in Medicare and Medicaid savings built into our budget. And, for the first time, we are including a permanent SGR, or "doc fix" proposal in our bill, fully paid for. It builds on bipartisan legislation and it adds provisions that would go even further in terms of what we call delivery system reform, making sure that we pay doctors and hospitals based on the quality of care that they are providing, not just the quantity of care that we are providing.

So, I think this is an area where we have made a great deal of progress. More people are covered. They are getting better coverage. And, in fact, we can build on that through this budget and work that we can do on a bipartisan basis this year.

Senator STABENOW. Thank you.

Chairman ENZI. Senator Sessions.

Senator SESSIONS. Thank you, Mr. Chairman. I appreciate your leadership and look forward to working with you.

I agree with Senator Sanders that the middle class is really hurting. Working Americans today are not doing well. Since 2007, the median income in America is down $4,000 for income for a family. This is catastrophic. This is absolutely one of the most dangerous trends we have seen in some time and it has accelerated over the last decade. It has accelerated under your President's, our President's watch, Mr. Donovan.

The problem is your policies. Tax more, spend more, borrow more, regulate more, Obamacare more, an immigration policy that dominates the market with workers from abroad when we do not have enough jobs for American workers, pulling down wages of Americans. That is what has caused this problem, in my opinion, and that is where we disagree, Senator Sanders. We have got a problem, but your ideas will not work. They will never work.

Now, Mr. Donovan, reckless spending endangers the future of the republic. As Mr. Elmendorf has told us, we remain on an unsustainable debt course. Let me ask you this simple question. Does your budget spend more or less than we agreed to with President Obama in the Budget Control Act of 2011?

Mr. DONOVAN. Our budget overall reduces spending relative to current law—

Senator SESSIONS. I just asked a simple question. You work for the taxpayers, Mr. Donovan. I am asking you, on their behalf, a

simple question. Does your budget spend more money next year than the current law of the Budget Control Act allows?

Mr. DONOVAN. Overall, our budget reduces spending compared to current law.

Senator SESSIONS. Overall, your budget spends $74 billion more next year than allowed by current law, is that not true?

Mr. DONOVAN. I think what you are focused on, Senator, is discretionary spending, and I think that there is broad agreement that sequestration—

Senator SESSIONS. That is what the Budget Control Act covers—

Mr. DONOVAN. —that sequestration is hurting our military readiness. The Joint Chiefs of Staff testified to that this past week. And, it is hurting our ability to invest in the things to grow our economy—

Senator SESSIONS. You work for the American people, Mr. Donovan. I ask you, do you propose spending more money next year on discretionary accounts than was agreed to in the Budget Control Act, yes or no?

Mr. DONOVAN. We are—

Senator SESSIONS. Can you not answer that question?

Mr. DONOVAN. I believe I have answered it, Senator.

Senator SESSIONS. No, you have not answered—

Mr. DONOVAN. We are proposing to reverse sequestration, and our budget fully pays for those increased investments on the discretionary side with mandatory spending reductions and cutting wasteful spending in the tax code.

Senator SESSIONS. Well, one of the ways you fix a budget problem is when you agree to a spending limit, you stick to it. So, I am going to ask you one more time, let us just see if we can get this straight. The American people need to know. Do we spend—do you propose to spend more next year than the Budget Control Act would allow?

Mr. DONOVAN. We propose to lift the sequestration caps, which have been harmful to our military readiness, that have been harmful to economic growth. We more than fully pay for those with reductions in spending on the mandatory side and reducing wasteful spending in the tax code.

Senator SESSIONS. So, you intend to spend more than we agreed to? That is all I want you to say. Will you say that?

Mr. DONOVAN. Our budget proposes—

Senator SESSIONS. Why will you not say that?

Mr. DONOVAN. —more than 400—

Senator SESSIONS. What is it about this that allows you to continue in that way?

Mr. DONOVAN. Senator, I think there is pretty broad bipartisan agreement—

Senator SESSIONS. We are going to discuss—

Mr. DONOVAN. —that discretionary spending is not driving our deficits, and, in fact, our discretionary spending, even with the increases on the discretionary side we propose in our budget—

Senator SESSIONS. So, you will not give—

Mr. DONOVAN. —remains—

Senator SESSIONS. —the American people for whom you work—

Mr. DONOVAN. —remains—

Senator SESSIONS. —a simple answer to that question.

Mr. DONOVAN. It remains—

Senator SESSIONS. I asked you one—

Mr. DONOVAN. —at the lowest level as a share of our economy—

Senator SESSIONS. My time is running out—

Mr. DONOVAN. —on record.

Senator SESSIONS. Let me ask you one more question. Under your statement that you gave us earlier, you said that the immigration policies of this President would make Social Security more sustainable over time. Now, is it not true that everybody in Social Security does not pay in enough money to justify the withdrawals that they will take over their lifetime, and by adding millions of more people unlawfully here to the Social Security rolls, will that not make Social Security less sustainable over time than it is today, yes or no?

Mr. DONOVAN. Just yesterday, the Actuary for the Social Security Administration confirmed that the President's executive actions that he took late last year would improve the prospects for Social Security.

Senator SESSIONS. Over what period of time?

Mr. DONOVAN. Over the—

Senator SESSIONS. Over the life of the individuals? You are not counting the times that these individuals would be drawing their benefits, Mr. Donovan. You are counting a short-term window in which they would pay in, creating a short-term surplus of money or additional flow of money, but you are not counting when they draw out. It is going to make the Social Security hole deeper. It is going to make it harder for us to save Social Security and Medicare and you know it. And you are suggesting to the American people directly contrary—directly different from that and it is wrong.

Mr. DONOVAN. Senator, you do not need to take my word for it. The Actuary of the Social Security Administration—

Chairman ENZI. The Senator's time has expired.

Mr. DONOVAN. —along with CBO, projects that the actions the President took will reduce deficits, not increase them.

Chairman ENZI. Senator Whitehouse.

Senator WHITEHOUSE. Thank you very much, Chairman.

Director Donovan, good to have you here.

Mr. DONOVAN. It is good to be here.

Senator WHITEHOUSE. Could you please tell us a little bit about the part of your budget document that is called "Federal Budget Exposure to Climate Risk" and what you see and anticipate in terms of costs that the taxpayers will bear from our failure to address the climate change problem.

Mr. DONOVAN. Senator, what we tried to do for the very first time in this budget is to very specifically quantify, as much as possible, what we have seen over a number of years and what we expect to see going forward in terms of direct increased costs. There are many other areas that are perhaps more speculative, more indirect costs, but we tried to focus on programs like disaster assistance through FEMA or flood insurance. Crop insurance is another area where we have seen substantially increased claims as a result of more extreme weather.

And, I think the basic analysis is that it is foolish for us not to act and both take further steps to reduce climate change, reduce greenhouse gas emissions, but also to prepare our communities for the more extreme weather that we are seeing. Not only will those save lives, but they will save dollars, as well.

FEMA shows that where we invest in protecting our communities, we typically get a four-to-one return in terms of future savings relative to the dollars that we spend today. So, climate change is a wise fiscal—focusing on climate change is a wise fiscal policy, as well as for other reasons.

Senator WHITEHOUSE. Turning to health care, I think most people agree that health care cost is really what is driving our long-term debt and deficits. Do you agree with that?

Mr. DONOVAN. It is the key measure of what is driving them, yes.

Senator WHITEHOUSE. And, we run a health care system in the United States that is grotesquely expensive per capita compared to any other industrialized nation. Do you have any expectations about what the increases recently announced in Medicare, particularly for the amount of the payments in Medicare that would be taken off of wasteful and expensive fee-for-service payments and onto more efficient quality-based payments, will result in?

Mr. DONOVAN. We have not included in the budget specific savings that come out of the delivery system reform improvements that—

Senator WHITEHOUSE. But you expect—

Mr. DONOVAN. —Secretary Burwell announced. Those—there is significant—if you think about it this way, significant potential additional savings, literally hundreds of billions, if not trillions, of dollars of long-run savings that could come out of those delivery system reforms. Unfortunately, it is just too early at this point to be able to reliably include those in the budget. So, we have included over $400 billion of savings that we think is directly quantifiable, but I think you point rightly to the fact that if we keep pushing on delivery system reform, the bipartisan SGR, the "doc fix" that we have included, we have lots of potential to dramatically increase savings and lower cost growth in the future.

Senator WHITEHOUSE. And, finally, with respect to the plan that the budget announces to go after offshore parking of funds by corporations to avoid American taxation, so-called repatriation, your program appears to have three elements to it. One, it is mandatory. Two, it is—there is a 14 percent opportunity to repatriate the money. And, future efforts to park revenues offshore as to avoid taxation will be faced with a 19 percent tax. Can you explain why those are important policy considerations when we go about dealing with repatriation.

Mr. DONOVAN. Absolutely. First of all, you are exactly right. Unlike the voluntary tax holiday that some have proposed, which we oppose, we are proposing a mandatory toll charge of 14 percent on the roughly $2 trillion of earnings that are overseas and have not been taxed. When you do it as a voluntary measure, you encourage future offshoring of profits, and, in fact, CBO would likely score that with a substantial cost, not revenue.

Our plan, on the other hand, raises enough money to fund a six-year reauthorization of the Highway Trust Fund at 40 percent

higher levels than we are currently funding. So, it is a significant opportunity to invest in the middle class and infrastructure.

Second—

Senator WHITEHOUSE. My time has expired, I am afraid, so I will leave the witness hanging. If there is anything you would just like to add by way of response—

Mr. DONOVAN. I would just say, I think it is critical that we have a policy that fixes this system going forward, as well, creates a level playing field, and encourages American companies to locate here and to bring jobs back here, as well, and our system would do that.

Senator WHITEHOUSE. Thank you.

Chairman ENZI. Senator Crapo.

Senator CRAPO. Thank you, Mr. Chairman, and thank you, Mr. Donovan, for being here today.

I want to go back to an issue that the Chairman raised with you, which is the question of whether this budget helps to reduce our national debt, and I believe your answer to that question was focused on the size of the debt in relationship to the economy, or to GDP, which I understand. I understand the argument and I understand the analysis. It is something that we have talked about a lot in budget circles over the last few years.

The question I have, though, is does that really justify a budget that continues to, frankly, borrow hundreds of billions of dollars every year and to spend that money in an effort to, as you indicated, to stimulate the economy and invest in things that should help the taxpayers and the people of America but never balance. I think my question is this. Is it possible for us, or any nation, to simply spend in deficit every year perpetually, borrowing money and never balancing, and to keep ourselves in a prosperous posture? Can we spend ourself perpetually into prosperity on borrowed money?

Mr. DONOVAN. So, Senator, I think that, you know, we have obviously talked a lot about this issue of what the right measure is. I think a different way, maybe, to look at it that I think has been key for us in looking at this issue, the most important measure of a budget is whether it invests in the things that are going to grow our economy going forward and meets our obligations to our seniors. I think we do have to recognize that we are facing right now an unprecedented demographic challenge in terms of the Baby Boom retiring, and I think it is particularly important when you look at it in that context that over the next not just ten years, but 25 years—which our budget does—that the key tests of sustainability is, first, to make sure that debt as a share of GDP is stabilized and is coming down.

Senator CRAPO. So, are you saying, though, that if we have our debt in relationship to GDP going down, that we are in a sustainable budget posture?

Mr. DONOVAN. I think at a time when we are facing unprecedented demographic challenges, that that is the key fiscal test.

Second—

Senator CRAPO. Let me go over—because our time is so short, I wanted to go over some numbers with you, just to show you what I am looking at in this budget. Using your numbers, as we look at

non-defense discretionary spending, currently, it is about 14.9 percent of the Federal spending outlays, and that is projected under your budget to drop to just ten percent of annual outlays by 2025. If you look at defense discretionary spending, which is today about 15.7 percent of annual outlays, it is projected to drop to about 10.5 percent of total Federal outlays in 2025. But, if you look at interest expenses on our spending, which are today about six percent of total Federal spending, they are projected to rise—to double, more than double, to 12.7 percent of Federal spending in 2025.

My point is, we are seeing our defense spending, our discretionary spending being squeezed, and we are seeing the interest on the national debt double over the period of this budget window, and that dynamic, it seems to me, is one that shows the inability to just continue to mount a national debt that will squeeze out the potential spending that you talk about that may be needed in other areas. Is that not something that we must address by controlling the spending, and, frankly, by balancing the budget?

Mr. DONOVAN. Well, Senator, I think we agree that it is critical that we make progress on the deficit and the debt. We have actually made substantial progress during the President's time in office. I also think it raises the issue that this is something we cannot just look to the spending side, for exactly the reasons you just described. We are already at discretionary spending levels as a share of the economy that are as low as they have been on record, and we think that is where we have to look to the revenue side, as well. And, I hope that we can work on a bipartisan basis to have a balanced approach to deficit reduction.

Since 2011, we have achieved 80 percent. Four out of every five dollars of deficit reduction—and our measure is over $4 trillion of deficit reduction thus far—four out of five has come from spending reductions. And, even with our budget, three out of five dollars of deficit reduction would come from spending reductions, and so—

Senator CRAPO. Well, thank you—

Mr. DONOVAN. —we believe we need to look at both sides of this equation, as well.

Senator CRAPO. I understand, and my time is up. I will just say, I am a member of the Bowles-Simpson Commission, as you know, and worked with others, the Gang of Six and others, to try to find a solution here. When we were working on that, the national debt was down around $11 trillion. It is $18 trillion today, and under the budget window that we are talking about here, it is going to go to $26-plus trillion. I just do not see how we can make the argument that as long as the economy keeps growing, we are okay. I just do not see that we can avoid trying to balance our budget and control this debt.

Chairman ENZI. Senator Warner.

Senator WARNER. Thank you, Mr. Chairman, and Mr. Donovan, it is great to see you. It looks like you have made a smooth transition from HUD Secretary to OMB Director.

I want to actually pick up on certain things that Senator Crapo said, but maybe with a slightly different tinge.

First, I want to commend you for getting rid of sequestration, which I have always called stupidity on steroids—

[Laughter.]

Senator WARNER. —because, as Senator Crapo pointed out, even with sequestration—remove domestic discretionary at the end of the time period, it is down to ten percent of spend—it would be much lower than that without removing the—getting rid of sequestration. And as somebody, again, who still for a few more years can pride myself on saying I have been in business longer than I have been in politics, investing in business, you never—you invest in businesses based on their investment in workforce, plant and equipment, and staying ahead of the competition. For government, that is education, infrastructure, and research. And, our current American business plan is a faulty one, and part of that is driven by sequestration. So, I commend you for getting rid of that.

I would argue, though—and I do acknowledge bringing the deficit down as a share of GDP is in the appropriate range. I do not believe 72 percent debt level at the end of ten is sustainable. Again, just a few quick factoids, which I know you know, but some of these, I think my colleagues might be interested.

You know, at 18 trillion, 100 basis point, one percent increase in interest rates takes $120 billion a year off the top. That is greater than the whole Department of Homeland Security and Department of Education combined.

At the end of ten years, even within this budget window—and this is where, I think, our colleagues on both sides may not want to be here at that point—we will be spending more on interest than we will on total defense or total domestic discretionary.

And, while I commend—and I believe revenues have to be part of the mix. I remember spending a very long New Year's Eve with great colleagues, but they were not necessarily the people I wanted to spend New Year's Eve with—to fight to get $600 billion in revenue so that we did not go over the proverbial fiscal cliff and go into unknown financial abyss. I might point out, we fought all that for $600 billion. We have had two one-time sources of revenue that have more than topped that number. We are at $420 billion in extraordinary profits from the Fed. Now, we can argue about Fed policies being good or bad, but I do not think anybody thinks those kind of profits are going to be able to be projected forever. And, while CBO and OMB count the money differently, a bill that you, Senator Crapo, and Senator Corker and many others have worked on on the repayments on Fannie and Freddie, $220 billion at this point, you booked that as revenue. So, if you get rid of those $650 billion-plus of extraordinary one-time revenues, our deficits are actually worse than the appearance would look at this point.

Now, where I would differ with many of my colleagues on both sides, one, I do believe entitlements have to be taken on. I think that has to be a question. But, you have got to get to the revenue side, and this is where I may not agree with all of the methodologies or all of the spending purposes, but revenues have to be part of the mix. CBO has recalculated the numbers, and I think Senator Enzi understands, you have got to have a reference point, and percent of GDP is what everybody at least agrees is the common area.

Anybody who says, well, we have got to look back at 50-year averages—50-year averages on revenues are 17.4 percent—we have never balanced the budget on that. And, no matter what you cut, with the demographic bulge you pointed out, you are going to have

to get revenues up. The only time we balanced the budget in the last 50 years has been when revenues under the new calculation are between 18.8 and 19.9, and you at the end of ten get to about 19.3, somewhere in the midpoint.

So, I think this is a debate that is going to continue. I think we have a little bit of breathing room because of hard actions you have taken and the Congress has taken. But, anyone that thinks that we are going to be able to solve this problem without revenues being a significant portion of the mix and that any kind of look-back alone basis is going to get us there, because even with entitlement reform, we have this demographic bulge—so, I am running out of time. I wanted to make that statement.

The quick point I will make is you have raised repatriation as a one-time payment for infrastructure. Congressman Delaney and Senator Blunt and I are looking at that. I would simply ask you to comment on that, as well as there are some more modest proposals. We had a bipartisan five-and-five BRIDGE Act last year that also dealt with infrastructure financing. And, do you think we need to consolidate those infrastructure financing programs we have got in a single place?

Mr. DONOVAN. So—

Senator WARNER. Maybe you can take it for the record.

[Laughter.]

Mr. DONOVAN. Good. I will be happy to do that.

Chairman ENZI. Thank you for doing that.

Senator GRAHAM.

Senator GRAHAM. Thank you, Mr. Chairman.

I would expect when we do our budget, and I know we will under Senator Enzi's leadership, that you will probably like our budget about as much as we like yours.

[Laughter.]

Senator GRAHAM. But, at the end of the day, there seems to be some common ground here. The idea that sequestration needs to be fixed, I agree with you, Mr. Donovan. At the end of the sequestration as we have it today under the Budget Control Act, what percent of GDP will be spent on defense?

Mr. DONOVAN. I do not have that number in front of me. If you do, you tell me, but—

Senator GRAHAM. Well, it depends on who you talk to. Between 2.3 percent and 2.7 percent. In terms of historical averages since World War II, what have we been spending on defense?

Mr. DONOVAN. Significantly higher than that.

Senator GRAHAM. Yes. So, I think that is the—do you agree that the threats in the world do not justify going to 2.7, 2.3 percent?

Mr. DONOVAN. We fully agree, and this budget makes clear that sequestration is a threat to our military readiness and we ought to reverse it.

Senator GRAHAM. Back to Senator Sessions' questions, you do spend more than the Budget Control Act cap. You say you spend—you account for it by offsetting and mandatory. I think Senator Portman may challenge that a bit. But, there is a desire by some of us on the committee to replace sequestration, at least most of it, with a revenue component and a mandatory reform component. I just want to be in the camp of saying that I am not going to sup-

port a budget that continues to gut the military. And, it is just not the military. It is the CDC, the NIH, and a lot of other programs. So, I support the idea you are trying to achieve. I just do not know if I agree with the methodology.

About the workforce, how many workers do we have per retiree today in the workforce?

Mr. DONOVAN. Uh—

Senator GRAHAM. It is three.

Mr. DONOVAN. Okay.

Senator GRAHAM. Okay. When I was born in 1955, it was 16. Unless there is a baby boom among 60-year-olds, I think we are in trouble. In 20 years, it goes to two. Does that make sense to you?

Mr. DONOVAN. Absolutely.

Senator GRAHAM. That we are living longer and having fewer children. A lot of Western nations face this problem, is that correct?

Mr. DONOVAN. Absolutely.

Senator GRAHAM. Does that not cry out for rational immigration reform? Where do the new workers come from?

Mr. DONOVAN. I could not agree with you more, Senator.

Senator GRAHAM. So, those who say, on our side or any other side, that we are glutted with workers, you are not looking at America the way it is, and you are obviously not running a business, because if you are in the business world, you are having a hard time getting high-skilled workers. And, if you are in the manual labor world, you are having a hard time getting workers. So, I just reject the idea that we do not need workers. We do. We just need to pick the workers. We need a rational way of choosing an economic-based immigration system rather than just chaos.

When we talk about America in the future and the challenges we face, probably the biggest challenge domestically is the retirement of the Baby Boom population. Do you agree with that?

Mr. DONOVAN. Yes, I do.

Senator GRAHAM. There are about 80 million of us, and that is why you need immigration to replace us in the workforce. But, is it fairly accurate that by 2042, if nothing changes, we will be spending all the money we collect in taxes just to pay for the Medicare-Social Security bill?

Mr. DONOVAN. Sounds about right.

Senator GRAHAM. So, just pause for a second. Unless something changes, all the money we are going to collect in taxes in the future, whether it is 17.5 or 19-point-whatever, is going to go to pay for two government programs, Medicare and Social Security. There will be no money left to invest in infrastructure. There will be money left to invest in the military unless you have massive borrowing. Do you agree with me that the challenge of our generation is to find a way to change that dynamic, to make Medicare and Social Security sustainable without taking all the revenue?

Mr. DONOVAN. I guess I would put a few caveats on that. One, we need to do that in a way that keeps our promises to those who have paid into the system—

Senator GRAHAM. I agree with that. We are not talking about divesting people. We are talking about long-term structural changes, means-testing benefits, adjusting the age of retirement. But, we

also need revenue. So, what I am willing to do is work with you and other members of the committee to find a way to structurally adjust these entitlement programs.

In terms of revenue, if you took all the money the top one percent made, every penny of it, would it balance the budget?

Mr. DONOVAN. Uh—

Senator GRAHAM. The answer is no.

Mr. DONOVAN. I do not think that it would—

Senator GRAHAM. If you took every penny out of the Defense Department, would it balance the budget?

Mr. DONOVAN. It would not.

Senator GRAHAM. Okay. So, you are not going to tax your way into prosperity and you are not going to cut your way into prosperity. You eventually have to reform entitlements to sustain an America that is not going to become Greece. Does that make sense?

Mr. DONOVAN. It does, and, in fact, our budget has $400 billion of savings in Medicare and Medicaid. And, I could not agree with you more that immigration reform is perhaps the single most important thing we can do to improve the solvency of Social Security going forward. It saves close to a trillion dollars over 20 years in terms of reducing deficits.

Chairman ENZI. Senator Merkley.

Senator MERKLEY. Thank you, Mr. Chair, and thank you for your presentation, Mr. Donovan.

If we step back to the central theme of the budget, you are laying out a vision in which, right now, under our economy, we have high income inequality, high wealth inequality, all new income is going to the one percent or a fraction of the one percent, and you are saying, and correct me if I am wrong, because I want to summarize this, that we can proceed to invest more in education, ranging from early childhood right on through higher education, we can invest more in infrastructure, we can invest more in R&D, and that your budget presents a way to pay for these so that you actually have a net decrease in the deficit from current law.

Mr. DONOVAN. That is absolutely correct.

Senator MERKLEY. Well, I want to applaud you and the President for laying out a vision that changes the path our nation is on right now. Imagine that you have a family, a large family of 100 people, and that family is working together, but all the income that comes into that family goes to just one member of that family. I think the other—the balance of the family would feel that that was not an equal opportunity arrangement. Would you agree?

Mr. DONOVAN. I would.

Senator MERKLEY. And, it would be an arrangement in which, well, that one member of the family would prosper greatly, but everyone else who has basic challenges and hopes and opportunities would find those doors or opportunities closing because all the revenue from that family is going to just one member.

And, I look at the conversation from my constituents who are seeing the incredible inflation in tuition for higher education, and they are looking at that and they are saying, why is it that our father's generation, our father and mother's generation, managed to provide lower-cost higher education to us so that we might thrive, the middle class might thrive, and that we have been failing in

that? And, you are saying we need to correct that. We may need to open the doors of opportunity to higher education.

Mr. DONOVAN. Absolutely right. In fact, the President's proposal to make two years of community college free is really based on the idea—many thought decades ago that we could not make high school universally available. We need to make at least two years of community college universally available and this is a critical step in terms of doing it, if we are going to prepare our workforce for the future.

Senator MERKLEY. I had a chance to give a commencement speech to three community colleges last year and I think that the working class families who were represented there, both those who were going through college and the families who came to celebrate their graduation, would believe that that was a pretty good idea, to open those doors of opportunity wider.

Mr. DONOVAN. Absolutely, and, look, it has to begin, as you know well, Senator, from the very beginning, whether it is quality pre-K programs, ensuring that American families can pay for child care. That is why we expand the Child Care Credit up to $3,000 per family. So, it is a broad range of investments right up through college and training and apprenticeships, which are doubled under our budget, that are critical.

Senator MERKLEY. And, let me go back to one part of the plan and my family of 100 members that I was speaking of, where one member of the 100 is getting all of the new revenue that the family is generating. But, also, that one member out of the 100 is getting fabulous tax breaks, and you are proposing that some of that wasteful spending in tax giveaways needs to be adjusted for a fundamental issue of fairness and to invest those revenues instead in a better deal for the middle class.

Mr. DONOVAN. That is exactly right. As our tax system stands today, there is hundreds of billions of dollars each year in capital gains that avoid taxation because of this, the current system for what we call stepped-up basis in capital gains.

Similarly, on the capital gains rate, all we are saying is let us go back to the 28 percent rate that the country had under President Reagan, and we think that that will establish—those are two steps of many that could begin to establish more fairness in the tax code.

Senator MERKLEY. Thank you very much.

Chairman ENZI. Senator Johnson.

Senator JOHNSON. Thank you, Mr. Chairman.

Mr. Donovan, welcome back. I want to spend a little bit of time, some short answers on things that I think we agree on. You talked about economic growth. Senator Sanders did. That is a major component of solving this problem, economic growth, correct?

Mr. DONOVAN. That is correct.

Senator JOHNSON. From 2009 to last fiscal year, can you also confirm we have actually increased revenue to the Federal Government by $916 billion per year?

Mr. DONOVAN. I do not have that number—

Senator JOHNSON. Would you agree it went from $2.1 trillion to $3 trillion, over $900 billion. Eight-hundred-and-seventy-four billion of that was just due to meager economic growth. Only $42 bil-

lion was attributed to that fiscal cliff tax deal. So, I am just trying to point out that economic growth really does provide the revenue Senator Warner was talking about. We need to concentrate on that.

To personalize this, look, it is important for us to point out why debt is such a problem. If you are a family in debt over your head, it is kind of hard to grow your personal economy, is it not, because the debt collectors are knocking on the door and anything past subsistence spending is really spent to service the debt, is that correct?

Mr. DONOVAN. I guess I would say if you are not investing in education and other critical things for your family—

Senator JOHNSON. But, if you are in debt over your head—

Mr. DONOVAN. —hard to grow your—

Senator JOHNSON. —you do not even have the money to invest in that, as Senator Graham was talking about, because so much of your income is being spent just servicing the debt. I mean, is that not what happens with a family? And the same thing is true on a national basis.

Let me ask you one other thing. If you are going to solve a problem, is not the first step to solve a problem admitting you have one and then properly defining it? Would you agree with that?

Mr. DONOVAN. I guess I would say our budget does take on the key drivers—

Senator JOHNSON. I am not talking about your budget—

Mr. DONOVAN. —of the long-term debt—

Senator JOHNSON. I am just talking about solving your problem. You have got to admit you have one and properly define it, correct?

Mr. DONOVAN. Uh—

Senator JOHNSON. Let us go to the charts. I would think that we do not have just a ten-year budget window problem, although I realize that is what your budget is confined to. We have a 30-year demographic problem. You talked about that. The Baby Boom generation, we are retiring 3,000 to 10,000 people today. We have made all these promises and we really do not have a way to pay for them.

And, by the way, I have to challenge Senator Sanders. We want to save Social Security and Medicare. That is our goal. We want to save it and make it sustainable for future generations.

But, this is a chart of the CBO's alternate fiscal scenario in terms of deficits over the next 30 years. Does this look pretty accurate to you? About $9 trillion—you are saying about $8 trillion in the first ten years, which is the budget window we are talking about now, but then $31 trillion in the next decade, $87 trillion in the third decade, for a whopping total of $126 trillion of deficits over the next 30 years. That is pretty accurate according to CBO's alternate fiscal scenario, correct?

Mr. DONOVAN. Well, I think that is before our policy, which, as I said earlier—

Senator JOHNSON. Well, let us—

Mr. DONOVAN. —not just over the ten-year window, but over the 25-year window—

Senator JOHNSON. Let us talk about the—

Mr. DONOVAN. —would stabilize debt as a share of GDP, which is, again, this does not measure it as a share of the economy. CBO says that the right way to measure it is as a share of the economy.

Senator JOHNSON. So, now, if you take a look at that $126 trillion, that is comprised of about $15 trillion of deficits in Social Security, about $35 trillion of deficits in the Medicare program, and then $71 trillion of interest on the debt, okay. So, again, talking to, or responding to what Senator Graham was talking about, interest starts dwarfing all the other problems.

Let me go to the next chart here, because I realize these are projections, so we really have to kind of compare how likely is this, and all I really have to go on is history. So, what we have done is we have just taken total Federal spending over the last 30 years compared to this 30-year alternate fiscal scenario just for reasonableness. So, entitlements over the last 30 years, we spent about 7.9 percent of GDP on entitlements. We are looking at about $13.3 trillion, and, by the way, when I was working with Sylvia Burwell, the White House figures about $14 trillion. Defense the last 30 years, about 4.1. The alternate fiscal scenario is 3.5. All other spending, 6.4 over the last 30 years. The alternate fiscal scenario is six. And then, of course, interest is a plug. To me, if anything, the alternate fiscal scenario might be understating the size of the problem.

My question to you, in your budget deliberations, are you looking at the 30-year problem? And, if you are, what has the President included in his budget to address the long-term unsustainability of both Social Security and Medicare, because those are what drives the debts, which does produce $71 trillion of interest payment.

Mr. DONOVAN. So, the three key things that I think we could all agree are really driving these deficits and debt over the long term, health care costs, a lack of enough workers, as we talked about earlier, relative to the number of retirees that we have, and having adequate revenue, and all of these key things that we attack in our budget, the impacts grow over time. And, so, whether it is the capital gains reforms and others that grow substantially in the second decade and beyond, immigration reform, which grows from $160 billion of deficit reduction in the first decade to $700 billion in the second decade and more beyond that, or many of the health care changes, the $400 billion in the first decade grows to a trillion dollars in the second decade. So, we are absolutely focused on making smart choices that would grow in impact over time with a focus on the deficit—

Senator JOHNSON. You are talking about a trillion and we are looking at $126 trillion.

Thank you, Mr. Chairman.

Chairman ENZI. Senator Baldwin.

Senator BALDWIN. Thank you, Mr. Chairman, and Mr. Chairman, I would ask that I be allowed to offer a longer statement for the record, but I wanted to jump—

Chairman ENZI. In writing?

Senator BALDWIN. Pardon?

Chairman ENZI. In writing?

Senator BALDWIN. Yes.

Chairman ENZI. Without objection.

Senator BALDWIN. The writing does not count against the time clock here.

So, thank you, Director Donovan. I am pleased to see that the President's overall budget focuses on an issue that every one of us cares about deeply here, which is ensuring that every American has a chance to share in the benefits of economic growth in this nation.

Before I get to a couple of specific questions on areas relating to that growth, I wanted to outline two areas which I believe fall short that have not been given much attention, and I hope that our committee will give it great attention as we move forward.

You know, the Great Lakes are 84 percent of North America's surface fresh water and over 20 percent of the world's surface fresh water, but yet for a second year in a row, the administration has recommended cutting funding for the Great Lakes Restoration Initiative, this time by $50 million. I know for myself and many of the other Senators who represent the Great Lakes, this is really a nonstarter. We have the warning signs all around us right now, whether it is what we saw last summer in Toledo, the threat of invasive species, and the Great Lakes are such an incredibly important asset. So, I look forward to working with the committee on that, but I feel like this is a way in which the budget has fallen short.

Another area that I wanted to just quickly touch on is Critical Access Hospitals. You know, rural access to—the administration has placed a priority on access to health care, yet rural access is a major challenge. Many of us represent States with many rural areas, and the economics of rural health care are unique. And, the cuts that have been proposed for Critical Access Hospitals, I think, will create real harm in our communities.

Now, back to some specifics on ways in which this budget can spur economic growth. We have seen the stock market surging back in recent years, but wages have remained stagnant, as the Ranking Member outlined in his opening remarks, in many cases fallen in adjusted dollars. And while this is obviously a huge problem in the aggregate, when you listen to the stories of hard working families who are trying to get ahead, it is heartbreaking.

In my State, one of the key engines of economic growth, one of the key ladders to accessing the middle class is our manufacturing economy, our manufacturing sector. And, I was pleased to see that there is continued focus in this area in the administration's budget proposal. It was two years ago in this committee that I offered an amendment on the issue of Manufacturing Institutes across the country. It was accepted on a voice vote and in our last fiscal year 2015 funding legislation. It is now signed into law, authorizing these Manufacturing Institutes across the country. I was proud to support that effort.

You also have an initiative called the American Made Scale-Up Fund to help emerging American made advance manufacturing technologies reach commercial scale production in the U.S.

So, I want to talk—I would like you to talk about the seven new Institutes that have been proposed in the President's budget. What areas are you going to focus on here? And, secondly, can you explain the American Made Scale-Up Fund? How does the administration envision this coming about, and how do you make sure that it is not duplicative of other existing Federal programs?

Mr. DONOVAN. Senator, thank you for asking about this. This really has been a bright spot in our recovery, more growth in manufacturing jobs than we have seen in decades in the U.S. And, specifically, thank you for recognizing the great bipartisan work that was done—we were very excited about it—to get these Manufacturing Institutes authorized.

What this budget would do is provide both discretionary and mandatory funding to get up to the full 45 Institutes that the President called for initially, and those are the Departments of Commerce, Agriculture, Defense, Energy would all be engaged in Institutes that are specifically targeted to areas that they are working on, whether clean energy, new agricultural advances, and others.

In terms of this Start-Up Fund, what it is really targeted to that we have not done in other ways—we do great basic research in this country, and, in fact, the budget proposes to scale up our investment in basic research. What is missing, we think, is a public-private effort that would really take the most promising technologies and get them to scale where we could really do manufacturing at a scale that would create new industries and drive large-scale job growth. So, the idea of this Start-Up Fund is to provide a credit subsidy, to use the technical term in our budget, that would allow us to raise private capital towards these promising technologies and scale them up to really put them into practice and create hundreds of thousands of jobs.

Chairman ENZI. Senator Ayotte.

Senator AYOTTE. Thank you, Mr. Chairman.

I wanted to ask you, does interest do anything for us? The interest that we pay, does it do anything productive for us?

Mr. DONOVAN. No.

Senator AYOTTE. Okay. So, if it does nothing productive for us, are you not concerned at all as we look at the budget proposal when we get to 2021, which is not too far off, that we are already spending more on interest than defense? We have already had the discussion previously that as we look at 2025, interest payments essentially are exceeding defense and non-defense payments. We are in a position where that is a huge chunk of 12 percent that does nothing for us, on what we are spending that money?

Mr. DONOVAN. So, I think the fundamental point you are making is that the budget needs to take steps that reduce our debt so that interest payments are lower than they would otherwise be, and—

Senator AYOTTE. But, my question is, are you concerned at all when you look at the over-tripling of the interest doing nothing for us over the ten-year window, which, as I understand, goes from $229 billion we are spending in interest now to $785 billion of doing nothing for the American people—no infrastructure, no education, no defending the nation, nothing?

Mr. DONOVAN. And, that is exactly why our budget focuses on and achieves $1.8 trillion in deficit reduction—

Senator AYOTTE. Well—

Mr. DONOVAN. —and in the long run, puts debt as a share of the economy on a—stabilizes it and puts it on a declining path.

Senator AYOTTE. Well, let me just make clear for the American people that are watching this hearing, that you think that stabi-

lizing in a good scenario is tripling-plus our interest payments over ten years, getting us in a position where we are spending more on interest than we are defending the nation, getting us in a position where we are spending more on interest than we are on education, infrastructure, protecting the environment, and all the other things that the Federal Government does. You and I just have a disagreement on whether this is a productive way to look at things, and I know that the American people will decide themselves on what they think about that.

I wanted to ask you about the solvency—we have talked about the demographic problems that we have with Medicare and Social Security, and the numbers that I have gotten the demographic challenge as we look at it is very immediate. It is more than a demographic challenge when it comes to the Social Security Disability Fund, because as I understand it, the Trustees have said that the fund will be exhausted in 2016, which is next year. Does the President's budget do anything to address the structural issues or the fact that this Disability Fund is going to be fully exhausted next year? And, I am worried because the people who really need this, if we ignore this, they will only be able to pay them 81 percent of disability benefits. Do you do anything about that in the budget?

Mr. DONOVAN. We are very concerned, as well. The most simple, direct step that we can take, a step that has been taken many times before under both parties, is a small reallocation of the payroll tax, and we ought to take that step and make sure that those who have earned these benefits get those benefits. In addition—

Senator AYOTTE. I do not mean to interrupt you, because I do not have a lot of time, but I just want to be clear: What you are doing is basically ignoring the fact that it is exhausted and transferring the money?

Mr. DONOVAN. Senator—

Senator AYOTTE. Let us just be honest. When you say "a small reallocation," that is transferring the money, and yet it is a system that already, as we look overall, is going insolvent. So, we are transferring the money from one pot to another. We are not solving the problem.

Mr. DONOVAN. Senator, if you would let me finish, please. The combined funds remain solvent until 2033. But, we are taking steps. On the disability side specifically, we have a number of steps in the budget that will ensure that those who actually are due the benefits get those, and a number of pilots and other efforts that will ensure that anyone who can work is able to. And, so, we do take steps there.

And, in the longer run on Social Security, again, the demographic challenges, comprehensive immigration reform is one of the most important steps that we can take to make sure that Social Security is solvent going forward.

Senator AYOTTE. As I look at this budget, I do not see steps in here that are going to solve this problem by 2016 or any real meaningful steps. But since you have just said that they are in there, I would like a specific answer to my question for the record. Thank you.

Mr. DONOVAN. Happy to do that.

Chairman ENZI. Since Senator Kaine is not here, Senator King.

Senator KING. Thank you, Mr. Chairman.

I would echo a lot of the comments of my colleague from New Hampshire and point out that that interest may not do much for us, but it is doing great things for the Chinese, who are using it to build airports and highways and such.

I find myself in agreement with both sides of the debate, and I would suggest, Mr. Chairman, it would be a useful exercise to convene this committee in a workshop to get us all together to have the kind of discussion that we are having in the context of this hearing about revenues, debt, deficit, interest, and threats to the economy. I think we could all benefit from sharing those views.

I agree with my colleagues who talk about debt and deficit. We cannot ignore interest. And the fact that has been pointed out numerous times today, that even under your projection, CBO projections, interest will exceed defense, interest will exceed—it will almost equal Social Security, it is a gigantic expenditure that really does nothing for us and it is going to eat up all the programs that everybody likes. Whether you like defense or Head Start or whatever, it is going to crowd those programs out. So, I agree with that. I think that is a very—the debt and the deficit is a serious problem, and to me, lowering the deficit is progress, but it is not an answer because the hole is still getting deeper. So, I think we really need to think about that.

On the other hand, as Senator Johnson pointed out, the best way to get out of this mess is through economic growth, and there are several strategies for economic growth that involve spending money. Infrastructure is probably the most important one. Abraham Lincoln at the age of 23, when he first ran for the Illinois legislature, put out a pamphlet talking about investing in roads and waterways. There was something called the American Plan in the 1800s. Henry Clay was a big advocate. And, it was an infrastructure plan, because that is the basis upon which the economy depends, and we are doing a woeful job of underfunding our infrastructure at this time.

The other big way to grow the economy is through education. The biggest economic stimulus program of the Federal Government in the history of the United States was the G.I. Bill after World War II, which sent millions of people to college for the first time and really expanded—it was the basis for the expansion of the middle class. Both of those things involve money and expenditures.

So, how do we get out of the problem? How do we grow the economy, make the expenditures that we have to make, at the same time, not digging ourselves deeper into the deficit hole? And, it seems to me that there are three or four strategies that we ought to put together into a comprehensive strategy.

One is, we do have to look at Federal expenditures and make sure they make sense and that they are not duplicative. The idea that every Federal expenditure made is perfect and good and useful and effective and efficacious just—you know, that does not pass the straight face test. So, we have to look at that.

Number two, we have to look at the structural health care costs. That is one of the biggest drivers of the deficit, is health care costs. It is not National Parks. It is not defense. It is the sheer cost of health care costs. This fellow Steven Brill has written a whole book

about how ridiculously expensive it is to be treated in this country, twice as expensive per capita as anywhere else in the world. The reason health care costs are so expensive is that they are expensive—

[Laughter.]

Senator KING. —and we need to focus on structural changes, which I know the Affordable Care Act does, at least in some areas of pilot programs, but that has to be a national priority. If we just continue as we are and let health care costs, fee-for-service, continue to drive the kind of escalation, which, unfortunately, may recover shortly, we will never get out of this hole.

And, then, the next strategy is some kind of revenues. We cannot deal with the demographic problem if we do not look at revenues. My concern—and I am interested in a Balanced Budget Amendment. I think that something that puts some constraint makes sense. On the other hand, if you add the Balanced Budget Amendment and the No-Tax Pledge, it creates a ratchet effect that you will never solve any of these problems and you will eventually squeeze out everything else, as you pointed out, payments to the elderly.

There has got to be some relief built into that, and that is where I think we need to have some discussion about revenues. And, I do not know what the right number is, whether it is 19 percent, 20 percent, but we have to take account of the fact that we have got this pig in the python, which is the retirement of the Baby Boomers, and that is going to end at a certain point. By the way, somebody said, in the long run—a famous philosopher once said, in the long run, we are all dead. But, the demographic reality of the next 25 years has got to be dealt with and we cannot just say, well, we are going to maintain taxes at historical levels and, therefore, meet all the obligations to the national defense and cover the costs of our commitments to the elderly.

So, it seems to me it has got to be a combined strategy of acknowledging the problem, number two, smart reductions in expenditures, health care cost reductions, revenues, probably from tax expenditures, and investments in proven job growth strategy, like infrastructure and education.

I apologize. There is not a question in there, Mr. Donovan. I did want to make one point. Congratulations on getting us a budget on time. That has not happened before in recent history, and I think you are due some credit for that. Thank you.

Mr. DONOVAN. Thank you. Mr. Chairman, could I take a moment? Is that—

Chairman ENZI. His time has expired. You can send us your answer.

Mr. DONOVAN. Happy to do that.

Chairman ENZI. Senator Corker. We are going to have a vote that we are trying to get everything in before.

Senator CORKER. Thank you, Mr. Chairman, and I appreciated Senator King's comments. I do want to say, I do not want to volunteer to die quickly to solve the Social Security problem—

[Laughter.]

Senator CORKER. —but I know that is a part of the solution. So, to our—

Senator KING. I did not mean it that way.

[Laughter.]

Senator CORKER. To our OMB head, thank you for bringing the budget in on time. I do think the focus on percentage of GDP, the 74.2 percent and keeping it steady—what we see happening year after year after year is people do not take into account things that happened like happened in 2008 and 2009, and so even though that is what you project to occur, obviously, that is under somewhat rosy circumstances and, likely, things will happen in the interim. That is what happens in the world that we govern.

I happen to think that a balanced budget is one that keeps our nation strongest. I think that, you know, the greatest threat to our national security today is really our inability to grapple with these issues.

The CBO Director was in here saying that, look, debt and deficits harm the standard of living of Americans, and yet as projected in your budget, that just continues ad infinitum. It also slows growth, especially when you get to where we are in the cycle, where we are having an almost full recovery. That hurts the standard of living of Americans.

So, basically, the way this budget is laid out, what we are doing, if we were to take this up, is we would be hurting the standard of living of Americans over time more and more and more.

I am a little disappointed that you guys took a powder, if you will, on the highway program. Basically, we have not solved one single problem since I have been here—not one. You know, we keep kicking the can down the road. I have been here eight years. You have been here six. We have not solved one single problem.

And, instead of solving the infrastructure problem, you all took some easy money. It probably will not work that way, but I do wish that you all had looked at that in a more serious way and put it on a steady pattern. And, I think all of us know, putting a lot of money quickly into infrastructure, more than it has been in the past, usually, candidly, leads to waste and not planning things out in an appropriate way.

Spending has been, over the last 50 years, at 20.1 percent, and under current law, mandatory spending will be at 14.2 percent at the end of ten years, in your budget 14.8, and that, obviously, as everyone has said, creates huge problems. For 50 years, revenues have been 17.4 percent and spending has been at 20.1. That has been with Republican Congresses, Republican Presidents, Democratic Congresses, Democratic Presidents.

And, so, I actually agree, we have a revenue problem and a spending problem. And, as Senator Johnson mentioned, the best way to generate revenues is through robust economic growth. But, we certainly have a problem on both sides. It is my belief that we need to go through in good periods times of balanced budgets and actually surpluses, and then in bad times, there may be a need to have some deficits. But, what we continue to do is bank on deficits forever.

So, I just have one question. I know this is, generally speaking, sort of the wish list, some people might say an ideological budget. I do not want to be pejorative when I say this, but I saw a large stack of budget documents on a table this morning on the front

page of one of the papers and I thought, you know, how sad, wasteful. I mean, those are all going to sort of be in the circular file after today. A lot of work, but it is an aspirational budget that is not going to be adopted and you know that. It says some things that you would like to see happen.

My question is this. Republicans can pass a budget—have to pass a budget, have to pass it in both bodies, and if we do it alone, the likelihood is we will nibble at some of these issues but we will not solve the problem because the President then will override the things that we may put forth. So, for us to really deal with these issues with a President who has only two years left and has had the opportunity to sort of lay out what he would like to see happen, but knows it is not, do you discern any desire on the behalf of the administration to sit down with all of us and work towards a budget proposal that is painful to all, but really solves the problem?

Mr. DONOVAN. Senator, absolutely, and, in fact, we constructed our budget building on, really, what was a bipartisan precedent in Murray-Ryan, which said we know discretionary spending is too low. We know that, in the long run, that our challenges are on the mandatory and on the revenue side. And, what we ought to do—and this is what our budget does—is more than fully pay for a dollar-for-dollar increase on the defense and non-defense side in discretionary spending with reductions on the mandatory and new revenues.

That is the model that we used. We think it is a model that we can build on. It is what got us back to regular order on budgeting. It is what helped grow our economy and create more jobs, because we got rid of mindless austerity and manufactured crises. And, we stand ready, because of the model that we have used in our budget, to do exactly that kind of bipartisan discussion this year and use it to build on to solve our short-run and long-term challenges.

Senator CORKER. Thank you, Mr. Chairman.

Chairman ENZI. Senator Perdue.

Senator PERDUE. Thank you, Mr. Chairman.

Mr. Donovan, thank you, as well, for providing this budget on time. I am the rookie here, and the benefit of that is I am your last Senator.

Mr. DONOVAN. Me, too, Senator.

Senator PERDUE. You have run out of Senators here today.

I would like to submit a couple of questions later, though, in writing.

I just have one question, and that is the severity of this debt and your opinion that it is sustainable at about 95 percent of GDP. First of all, I personally disagree that GDP should be the denominator. I think revenue should be the denominator. But, I want to read you a quote and put this in context, this question. This is a quote from President Obama, June 3, 2008. "The problem is that the way Bush has done it over the last eight years is to take a credit card from the Bank of China in the name of our children, driving up our national debt from $5 trillion for the first 42 Presidents. Bush 43 added $4 trillion by his lonesome, so that we now have over $9 trillion of debt that we are going to have to pay back. That is $30,000 for every man, woman, and child. That is irresponsible."

Let me put it in context. In the year 2000, our debt-to-GDP was 55 percent of GDP. In 2010—or 2008, actually—we added $4 trillion to roughly a $6 trillion debt, and since 2008, we have—in the last six years, we have added $8 trillion to that debt, and this budget takes it up to $26 trillion. You know, the problem is, right now, at $18 trillion, if interest rates—and this is the way—I am really concerned about the forecast of interest rates, because if you look at the sensitivity analysis and you took interest rates just to the 30-year average, we would already be paying close to a trillion dollars in interest today. I just do not think that is sustainable on a $4 trillion revenue source, roughly.

And, so, when I look at this thing—and that is one problem. The second problem is these future unfunded liabilities that Senator Johnson highlights so eloquently and we really do not address. You commented a couple times that the Social Security-Medicare problem really accelerates in the second decade, and I am really concerned that if you look at this thing, those $100-plus trillion of liabilities added to the $18 trillion we have right now, we can characterize it any way you want to, but if you look at it per household, which is really the way things get paid in this country, that is over a million dollars per household in America today. Frankly, I do not personally think that is sustainable. Social Security, Medicare and Medicaid, pension benefits for Federal employees, and our interest payments, these are all contributors. We have talked about it. But, a million dollars per household brings it home for me and my constituents.

So, my question is this. Looking at the second decade and the third decade and kicking this can down the road, how should we look at a debt that is 95 percent of GDP, some five or six times our revenue, as being sustainable?

And, let me give you one little anecdote. You know, it occurs to me that this is a national security issue, Mr. Donovan, and I do not say that lightly. Right now, we have these treaties with a lot of countries around the world. One of those is Taiwan, and that treaty says that if the country of Taiwan is invaded by the country of China, we have to go to Taiwan and defend Taiwan against China. The problem when borrowing this much money every year, to do that, we have to borrow the money from China to go to Taiwan and defend Taiwan against China. That is an anecdote that is not lost on my constituents and they want to know when we are going to balance this budget and how we get after the long-term imbalance of these mandatory expenditures coming in the second and third decade.

So, my question is simply this. The word "sustainability" is very tricky. I get it. You said this is sustainable at 95 and declining. I disagree. I do not think it is sustainable, but I would love to get your opinion about why that is sustainable, given the vagaries of the capital markets around the world and the volatility of interest rates that we have seen over the last 30 years.

Mr. DONOVAN. So, first of all, Senator, recognize that when we came into office, we were facing enormously difficult fiscal circumstances and we have brought down the deficit by more than two-thirds with a broad set of steps, and that the steps that we have already taken have substantially reduced long-run deficits

and debt, whether it is bringing down health care costs, a range of other steps that we have taken on economic growth. As I said earlier, we agree that we need to focus on those long-term steps, and reducing the growth in health care costs—

Senator PERDUE. With the time remaining—I am sorry to interrupt, but would you—you still think that 95 percent of GDP, that that debt, that that is sustainable. I am talking in the second and third decade out here past our projections in this budget.

Mr. DONOVAN. Our budget is not at 95 percent of GDP. Under current law, it would rise up to 81 percent of GDP. Our budget changes that, brings it down in the ten-year window to 73 percent and would actually keep it stabilized throughout the 25-year window, which is really, as we talked about earlier, when these demographic challenges are hitting us most strongly. And, that is why I say it is sustainable.

Senator PERDUE. Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Senator Portman, who used to be in your position.

Mr. DONOVAN. As he reminded me at my confirmation hearing. Congratulations. You have been nominated to the worst job in Washington.

[Laughter.]

Mr. DONOVAN. But, it is also the best.

Senator PORTMAN. Exactly, and my worst day was the day you are experiencing right now.

[Laughter.]

Senator PORTMAN. And, then, let me just start by saying you are doing a fine job defending a budget that I think is very difficult to defend, because I just do not think it comes close to meeting the challenge. And, look, I think you have done a good job defending it, but I think we have to set the record straight on a few things.

This notion that this budget, as you said earlier, is all about—in response to Senator Corker's question—following the Ryan-Murray proposal of less mandatory spending and breaking the caps and more discretionary spending. It is not. I think, perhaps because you wanted the last few years to look good, this is the reality, and I will give you the numbers. I am not really asking you a question here, because these are what the numbers are.

Spending on the discretionary side actually goes from 6.5 percent now down to 4.5 percent of GDP. Defense actually goes from 3.5 percent down to 2.3 percent. And, I know it makes your numbers look better after 2022 and 2023 and 2024. So, it is $2 trillion in new taxes. It is a trillion dollars in new spending. You said in response to several of the questions, including Senator Sessions, that, no, mandatory spending is less. It is more. It is $885 billion more in mandatory spending. I am happy to share the charts with you, but that is what it shows.

So, I like your theory that you say you guys are following, but the budget does not meet that standard, and I know we are going to have some big differences in these two budgets, but we have got to figure this out. I mean, I think it is very obvious what the problem is and I think you guys skirt it, and I will ask you a bunch of questions.

One, you are talking about you need to raise more revenue, and you do. You have over $2 trillion in new taxes. Over the first 50 years—over the last 50 years, is it true that our taxes as a percent of GDP have been just under 18 percent? Is that about right?

Mr. DONOVAN. Roughly right, but as I think it was said earlier, at the only time that we balanced our budget, at a time our economy was growing quickly, we actually had revenues that were up as high as 20 percent. And, so, particularly with the demographic challenges we are facing, we think that the revenue levels that we have are the right ones.

Senator PORTMAN. So, just before we had this recession, 2008, 2009, we had deficits of 1.2 percent of GDP, $161 billion, and we had 18 percent in revenue to GDP. And, by the way, this whole notion that you guys have done so much better than you expected to do, the CBO baseline that you inherited in 2009, which already took into account the recession, as you know—in fact, it included all the war funding. In other words, it had much higher levels of spending on defense than we have actually had. The baseline there that CBO gave you had deficits that were half of what have occurred, $3.4 trillion versus $6.7 trillion. This year's $468 billion deficit is exactly double what CBO projected for 2015 during that time.

So, I mean, I do not think, by the standards that were set by the baseline then, again, including the recession taken into account and all this war spending, that it is fair to say this has been a breakthrough, that everything is going great, we have made all this progress. But, look, I think, let us continue on these questions, because I think the problem is pretty obvious, and I know you know what it is and we all know what it is and we are not addressing it.

So, you take revenue up to 19.7 percent of GDP. Am I correct that discretionary spending, what we call other mandatory spending, are also falling as a percent of the economy over the long term?

Mr. DONOVAN. Well, I—

Senator PORTMAN. That is a yes or no. It is yes. You know that. It is falling.

Mr. DONOVAN. Well, I think it makes the point that we are finding places, particularly on the mandatory side, where we are reducing spending, and I think—

Senator PORTMAN. Well—

Mr. DONOVAN. —I wanted to respond to your earlier point that, in fact, we are reducing spending on the mandatory side. We are making room on the discretionary side, but with $400 billion of reductions in Medicare and Medicaid, tens of billions of dollars in program integrity savings—

Senator PORTMAN. So, let me just say—

Mr. DONOVAN. —crop insurance, a broad range of programs—

Senator PORTMAN. —on all those health care entitlements, which, as you know, is the issue, as well as Social Security and interest on the debt, that is where the whole issue is, you take it from increasing 105 percent, health care entitlements over the next ten years, to increasing 99 percent over the next ten years. I mean, obviously that is where the issue is. So, discretionary spending goes

down. It is 6.5 percent now. For all you on both sides of the aisle saying, this is great, we are going to do more discretionary spending, it does not have more discretionary spending. It has less.

Mr. DONOVAN. I—

Senator PORTMAN. It has less for both defense and non-defense. Health care entitlements do go from 105 percent to 99 percent. But, you know, it is 7.8 percent of GDP now. It rises to 9.8 percent. I know the discussion earlier was about the 20-year number. That is really scary, because it is just unsustainable.

So, to sum up, we are heading toward record high tax revenues. In fact, on individual revenues under your budget, individual tax revenues go to their highest level of GDP ever, and, you know, that is just what it is. Near record low discretionary levels and falling, other mandatory. So, the variables driving the deficit are entirely the record levels of debt we are talking about, are entirely these incredibly important, vital programs that we have got to save for future generations. And, if we do not do that, Mr. Chairman, I am afraid we will have let down the people who voted us to represent them.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

That, to your relief, concludes our questions for this morning.

[Laughter.]

Chairman ENZI. I want to thank you for agreeing to testify this morning. We appreciate your time here with us as well as the work that you have done to submit a budget to for Congress by the legal deadline. And, we now get to work on a budget resolution by the legal deadline of April 15, and I look forward to working with my colleagues on that.

I want to remind my colleagues that they can turn in questions for Director Donovan, but they are due no later than 6:00 today, and they have to be in writing at the Committee Clerk's office, which is Dirksen 624. And, then, I am sure that Director Donovan will respond within seven days.

So, with no further business before the committee, we stand adjourned.

Mr. DONOVAN. Thank you.

Chairman ENZI. Thank you.

[Whereupon, at 12:04 p.m., the committee was adjourned.]

(Signature)

Statement for the Record
From Senator Perdue
For Director Shaun Donovan
OMB Hearing
February 3rd, 2015
Senate Budget Committee

Statement:

Chairman Enzi and Ranking Member Sanders, thank you for calling this hearing to discuss the President's Fiscal Year 2016 budget request. There is not a more important issue for us to address than the budget and how it relates to our national debt.

I have said many times that this is a full-blown crisis. The President's budget submission turns a blind eye to that crisis and continues to drive us deeper and deeper into debt. The president seems determined to take us past the point of no return.

The President has talked for years about growing the middle class as if to say growing the middle class is the same thing as growing our economy. It is not. The President has also insisted that we can grow our way out of our problems. I agree that growth is the answer, but that assumes the economy actually grows, and that policies are in place to encourage that growth.

Since this President took office, his policies have contributed to a drop in income for the middle quintile of earners from $53,000 to $47,000, median income dropping by 5% down to $51,000, and net-worth of the bottom sixty percent declining by 19 percent while the top ten percent grew by 9 percent. Over the past 6 years, 4 million women fell into poverty and food

stamp participation grew from 27 million to 47 million. That does not represent economic growth, nor have his supposed growth policies had any substantive effect.

While the President likes to tout that his plans have cut the deficit in half, he forgets that deficits will continue to be unsustainable and even grow again once he leaves office. We are not only facing the burden of a $18 trillion debt, but over the next 30 years, our children must confront the approximately $100 trillion in future unfunded liabilities of Social Security, Medicaid/Medicare, Pensions, and payments on interest. The historical debate has always been whether tax increases or spending cuts will solve the debt crisis. I firmly believe that we can only solve our debt problem through the following:

1. Cut out unnecessary discretionary spending and reallocate towards priorities.
2. A long term fix on mandatory spending.
3. Grow the economy.

Mr. Donovan, I would propose that the reason the President's plan has so many tax hikes is because you have run out of ideas to grow the economy and the only financial means you have to advance the President's agenda is new taxes.

This Committee will be tasked with creating a new budget, a budget that brings sanity to our economy and ends deficit spending. I would also like to make debt payments a component of that budget, but that is a discussion for another day. Mr. Donovan, because the president did not propose a budget that provides a realistic view of our current economy and our spending problems I will be seeking further input about why the President made this proposal.

Thank you Mr. Chairman.

## Chairman Enzi

**As indicated below, please provide additional detail on Budget table S-8, Bridge from Balanced Budget and Emergency Deficit Control Act (BBEDCA) Baseline to Adjusted Baseline, as indicated below:**

**a. The split between revenues and outlays for the line labeled "Continue tax benefits provided under the American Taxpayer Relief Act,"**

**b. The adjustments for discretionary program integrity funding and associated mandatory benefit savings included in the line labeled "Set discretionary budget authority at cap levels," and**

**c. The split between mandatory sequestration for 2017-2024 and discretionary cap reductions for 2016-2021 in the line labeled "Reflect Joint Committee enforcement."**

A. The split between receipts and outlays for the line "Continue tax benefits provided under the American Taxpayer Relief Act" can be found in Table 12-2, "Adjustments to the Balanced Budget and Emergency Deficit Control Act (BBEDCA) baseline estimates of governmental receipts," in the "Governmental Receipts" chapter of the Analytical Perspectives volume (page 158).

B. The components of the line "Set discretionary budget authority at cap levels" are detailed in the attached table. The adjustments for program integrity include setting discretionary funding at levels consistent with the Budget Control Act (BCA) program integrity base and cap adjustment levels (for 2016 for SSA program integrity and for 2016-2025 for HCFAC program integrity), and reflecting the benefit savings that would result from the specified SSA and HCFAC cap adjustments.

C. The components of the line "Reflect Joint Committee enforcement" are also detailed in the attached table. These components include discretionary cap reductions and mandatory sequestration. Discretionary cap reductions include the reductions in the 2016 caps pursuant to the discretionary preview report issued with the President's Budget, and cap reductions for 2017 through 2021 that would be ordered in future preview reports for those years. Mandatory sequestration includes Joint Committee sequestration that would be issued in sequestration orders for 2017 through 2021, as well as the extension of mandatory sequestration into 2024 as provided for in legislation enacted subsequent to the BCA. Mandatory sequestration for 2016, which was implemented in the sequestration order issue with the 2016 Budget, is already included in the BBEDCA baseline and is therefore not part of the baseline adjustment.

Detail for lines in Summary Table S-8

**Adjustments for provisions contained in the Budget Control Act**
(in billions of dollars)

| | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2016-2020 | 2016-2025 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Set discretionary budget authority at cap levels:** | | | | | | | | | | | | | | |
| Discretionary Adjustment for BCA caps: | | | | | | | | | | | | | | |
| Non-Defense | --- | --- | 2 | -0 | -2 | -2 | -4 | -6 | -6 | -6 | -6 | -6 | -6 | -37 |
| Defense | --- | --- | 27 | 38 | 41 | 41 | 42 | 42 | 42 | 42 | 43 | 43 | 189 | 400 |
| Subtotal, Adjustment for BCA caps | --- | --- | 29 | 38 | 39 | 39 | 38 | 36 | 35 | 36 | 36 | 37 | 183 | 363 |
| Discretionary Adjustment for Program Integrity Cap Adjustment Funding | --- | --- | 0 | -1 | -1 | -1 | -1 | -1 | -1 | -1 | -2 | -2 | -5 | -13 |
| Mandatory Adjustment for Program Integrity benefit savings | --- | --- | -1 | -3 | -2 | -2 | -2 | -2 | -2 | -2 | -2 | -2 | -9 | -18 |
| **Total, Set discretionary budget authority at cap levels** | --- | --- | **28** | **34** | **36** | **36** | **35** | **33** | **32** | **32** | **33** | **34** | **169** | **333** |
| **Reflect Joint Committee enforcement:** | | | | | | | | | | | | | | |
| Discretionary, Reductions for Joint Committee enforcement: | | | | | | | | | | | | | | |
| Non-Defense | --- | --- | -22 | -32 | -35 | -36 | -35 | -34 | -14 | -4 | -1 | -1 | -160 | -214 |
| Defense | --- | --- | -33 | -46 | -50 | -52 | -52 | -53 | -20 | -7 | -3 | -2 | -233 | -318 |
| Subtotal, Discretionary Reductions for Joint Committee enforcement | --- | --- | -55 | -78 | -85 | -87 | -88 | -87 | -33 | -11 | -5 | -2 | -393 | -532 |
| Mandatory Reductions for Joint Committee enforcement | --- | --- | -0 | -11 | -18 | -19 | -20 | -21 | -21 | -27 | -29 | -1 | -68 | -167 |
| **Total, Reflect Joint Committee enforcement** | --- | --- | **-56** | **-89** | **-103** | **-106** | **-107** | **-108** | **-55** | **-38** | **-33** | **-3** | **-461** | **-698** |

## Chairman Enzi

**Comparing the rules of thumb for an increase in interest rates shown on page 17 of the *Analytical Perspectives* volume with the comparable table shown on page 133 of CBO's January 2015 *Budget and Economic Outlook*, there is significant difference in how the two agencies estimate the effect on revenues of a one percentage point increase in interest rates. CBO sees the effect as reducing revenues near term, while OMB sees the effect as consistently increasing revenues. One might expect the estimates to be different, but it is curious that the signs are different. What is the explanation for this difference?**

CBO's rule of thumb incorporates only the effect of interest rate changes on Federal Reserve remittances to the Treasury, whereas OMB's rule of thumb incorporates the effect of interest rate changes on individual income taxes and corporate income taxes, as well as Federal Reserve remittances. CBO estimates a one percentage point increase in interest rates would reduce revenues in the near term, because the Federal Reserve's higher interest payments to banks on their reserves would initially outstrip higher interest earnings on its securities portfolio. OMB estimates the same increase in interest rates would consistently increase revenues due to net increases in individual income taxes, corporate income taxes, and the Federal Reserve's interest earnings on its interest earnings on its securities portfolio.

## Chairman Enzi

**How much spending is included in the President's budget in FY2016, for the five years including FY2016 through FY2020, and for the ten-year budget window for adapting to, researching, and mitigating climate change? Please include money requested for the development and promulgation of regulations under the President's Climate Action Plan and provide total spending by agency.**

In order to secure America's energy future and protect our children from the impacts of climate change, the Budget invests in clean energy, improving energy security, and enhancing preparedness and resilience to climate change. OMB intends to provide Congress with a climate change spending report this summer that will detail climate-related spending and tax expenditures by category and agency across the Federal Government. Major components of climate spending in the President's Budget for FY 2016 include $2.7 billion for the U.S. Global Climate Research Program, $7.4 billion for clean energy technology programs, $1.29 billion for international climate leadership efforts, and a number of strategic investments in climate resilience. The Budget also provides for $4 billion in mandatory spending for the Clean Power State Incentive Fund, a permanent and expanded Renewable Energy Production Tax Credit, and the creation of a Carbon Dioxide Investment and Sequestration Tax Credit.

Outyear investments for the Clean Power State Incentive Fund, the Renewable Energy Production Tax Credit, and the Carbon Dioxide Investment and Sequestration Tax Credit can be found in Table S-9 of the President's Budget. OMB does not currently have outyear estimates for climate-related discretionary spending.

The following list provides additional detail on a number of the investments identified above:

- Approximately $2.7 billion for the U.S. Global Climate Research Program (USGCRP), advancing scientific knowledge of the integrated natural and human components of the Earth system.
- $7.4 billion in clean energy technology programs across the Federal government. These programs conduct research, development, and deployment efforts that stimulate the evolution and use of clean energy sources as well as energy-efficient technologies, products, and process improvements. These technologies are critical to cutting carbon pollution, enhancing environmental stewardship, increasing U.S. energy independence, and advancing American leadership in clean energy.
- $239 million to support efforts at the Environmental Protection Agency to cut carbon pollution through commonsense standards, guidelines, development of regulations related to the Clean Power Plan, and implementation of voluntary programs. Part of this sum is included in the $7.4 billion total for clean energy technology described above.
- An incentive fund for States choosing to go beyond the Clean Power Plan, which will be finalized this summer. The Clean Power State Incentive Fund will provide $4 billion to support States exceeding the minimum requirements established in the Clean Power Plan for timing of State plans and the pace and extent of carbon pollution reductions from the power sector.
- $1.29 billion to advance the goals of the Global Climate Change Initiative, supporting the President's Climate Action Plan by promoting leadership abroad and supporting important multilateral and bilateral engagement with major and emerging economies.
- $400 million for National Flood Insurance Program (NFIP) Risk Mapping efforts, an increase of $184 million over current funding levels. This increase will further support efforts to help communities and businesses

understand what areas pose flood risks and how to better prepare for those risks. The Budget also proposes $175 million for NFIP mitigation grants, which lower the risk of flood damage to policy holders' properties. The budget also provides $200 million for FEMA's Disaster Mitigation Grant Program, which will help mitigate the effects of future disasters.

- $20 million to continue expanding and improving the recently-released online Climate Resilience Toolkit.
- $4 million to support a resilience corps pilot program at the Corporation for National and Community Service. This pilot program will support roughly 200 AmeriCorps members to assist communities in planning for and addressing the impacts of climate change. The Budget also includes $2 million for NOAA to train the corps members.
- $31 million for the Army Corps of Engineers to provide local communities with technical and planning assistance regarding the development and implementation of nonstructural approaches to manage and reduce flood risk.
- $50 million for American Indian Tribes and Alaska Native Villages and new funding totaling $7 million for Insular Areas (including territories and freely associated states) for understanding, planning for, and implementing actions that support community resilience in the face of a changing climate.
- $108 million for USDA's Forest Service, EPA, and the Department of the Interior's U.S. Geological Survey for research related to the role of lands and associated resources as carbon sinks.

## Chairman Enzi

**The United States government has not yet completed construction of the Yucca Mountain nuclear waste facility. This failure is expected to trigger legal claims against the government and payment of these claims will be made from the Judgment Fund. The President shows these future legal claims against the United States in his baseline treatment of the Judgment Fund. Please provide OMB's estimates in each of the upcoming years of the budget window for how much the government will have to pay for failing to fulfil our contractual obligations under the Nuclear Waste Policy Act?**

The Federal Government did not meet its contractual obligation to begin accepting used nuclear fuel by 1998. As a result of litigation by contract holders, the Government was found in partial breach of contract, and is now liable for damages to some utilities to cover the costs of on-site, at-reactor storage. To provide more accurate budget projections, the baseline for the Judgment Fund now reflects a more complete estimate of potential future costs of these liabilities. These estimates are based on a rough average calculation of aggregate liabilities and do not include estimation of potential new liability or case-by-case rulings. The below table shows the more complete estimate used in the budget window baseline.

Judgment Fund Nuclear Waste Estimated Liability ($ in millions)

2014 - $369

2015 - $376

2016 - $383

2017 - $390

2018 - $398

2019 - $405

2020 - $413

2021 - $421

2022 - $429

2023 - $437

2024 - $445

2025 - $445

## Chairman Enzi

**The President proposed the elimination of the so-called fossil fuel preferences in the tax code and reform of the royalty system for oil and gas development on federal lands and waters. At the same time, Americans are enjoying a dramatic decrease in the cost of gasoline for transportation purposes as U.S. production of crude oil remains higher than it has for many years.**

**A. Does OMB estimate that the elimination of these fossil fuel preferences will result in higher or lower gasoline prices for Americans at the pump all things else being equal? Please provide the magnitude of the estimated impact in dollars and cents.**

**B. Is it the administration's position that the elimination of these fossil fuel preferences will increase or decrease US dependence on foreign oil? Please provide the magnitude of the estimated impact in barrels per day.**

**C. Is it the administration's position that the elimination of these preferences will increase or decrease domestic oil production? Please provide the magnitude of the estimated impact in barrels per day.**

The President agreed at the G-20 Summit in Pittsburgh in 2009 to phase out inefficient subsidies for fossil fuels to reduce greenhouse gas emissions. The oil, gas, and coal tax preferences the Administration proposes to repeal distort markets by encouraging more investment (and thus production) in the fossil fuel sector than would occur under a neutral tax system. We have not estimated the exact impact of removing these distortions on fuel prices, oil imports, or domestic production. But removing these preferences should have a minimal impact on prices at the pump, which depend on world market prices. Removing the preferences will also reduce dependence on oil and gas, including foreign oil and gas, by removing distortionary barriers to the development of a clean energy economy.

## Chairman Enzi

**The President's proposal would increase loan volume significantly in the Perkins Loan program (with the same interest rates "unsubsidized" Stafford loans), while converting it into a direct loan program run by the Department of Education. The change would allow the program to be scored under Federal Credit Reform Act (FCRA) procedures, which means the program would be scored not as having an annual discretionary cost, but as saving $7.1 billion in mandatory funds over ten years. And the budget states clearly that the "savings" would be used to help pay for Pell Grant increases. At one time, Congress needed to choose how to apportion limited federal student aid dollars between loans and grants. But since unsubsidized student loans save the Government money under FCRA accounting, the Government can, in theory, continually increase student grant aid and pay for it by increasing student loan volume. Why does the President think it appropriate to use FCRA loan program savings to manufacture savings to spend elsewhere? Does the budget proposal fill the existing Pell Grant shortfall? If not, does it just propose to keep pushing the shortfall beyond the budget window?**

Under FCRA accounting, the cost of a credit program equals the expected present value cost or savings to Government. Therefore, when credit program policies generate savings, it is appropriate to use these savings, like other savings, to offset costs.

Discretionary Pell program costs have been declining since a peak in the 2010/11 award year, the result of legislative changes and declining enrollment. We now estimate that a shortfall will emerge in 2018, if Congress maintains the current appropriations level for the program. The Budget proposes to maintain the Pell appropriation at its current level in FY 2016 to ensure that students have access to Pell Grants at current award levels.

## Chairman Enzi

**More than one in five dependent undergraduates whose parents' income exceeds $100,000 attend public two-year colleges, according to data recently released by the Department of Education's own National Center for Education Statistics *(Profile of Undergraduate Students: 2011-2012,* October 2014), Web Tables, Table 1.3, p. 14, NCES 2015-167). If community college tuition were free for those with adjusted gross income up to $200,000, how much do you expect this would increase community college attendance, and how many students would be redirected from attending other institutions, such as vocational schools or four-year colleges?**

America's College Promise will ensure that students who attend community colleges at least half-time, maintain a 2.5 GPA in college, and have an adjusted gross income of less than $200,000 will have their tuition eliminated. Once all 50 States participate, this program could significantly impact as many as 9 million community college students. The cost of college is out of reach for many middle-income students, forcing them to take on significant debt. In the 21st century, the first two years of post-secondary education or training should as available, accessible, and expected as high school.

This proposal would support high quality community college programs that either provide a pathway to careers for students or to a degree at a four-year institution. Providing a way for students to earn two years of academic credit for free would effectively cut in half the cost of a four-year degree. Furthermore, the proposal requires academic programs at community colleges to be aligned with four-year colleges so that it creates a pathway for a students to successfully complete a four-year degree. In addition, the President's proposal allows States that have ended tuition at community colleges for eligihle students to also use their Federal grants to bring down costs at four-year colleges and universities.

## Chairman Enzi

**In last year's budget proposal, the President proposed to make the Pay as You Earn (PAYE) student loan repayment available to all borrowers. Then, last June, the President signed a Presidential Memorandum ordering the Secretary of Education to set in motion the process of expanding PAYE-which allows borrowers to limit their payments to 10-percent of their discretionary income -- so that it is available to all borrowers, including those whose loans were taken out before the program was initiated. The Department of Education's Budget Justifications states that this expansion, although it has not occurred yet, has been incorporated into the budget baseline. The Budget Appendix indicates that loans repaid through PAYE and other income-based repayment programs are dramatically more costly to the Treasury than other loans. How much does the baseline assume the PAYE expansion will cost? Are there further administrative changes with significant cost implications that the Department of Education is currently considering making to the student loan programs?**

The baseline assumes the PAYE expansion will cost $9.3 billion to extend the repayment plan to all existing direct loans. The Department of Education regularly makes changes to the management of the student loan portfolio to protect both borrowers and taxpayers, but recently announced that the 2015 negotiated rulemaking agenda will include two items that affect the loan programs: 1) preparing proposed regulations to establish a new Pay as You Earn repayment plan for those not covered by the existing Pay as You Earn Repayment Plan in the Federal Direct Loan Program; and 2) establishing procedures for Federal Family Education Loan (FFEL) Program loan holders to use to identify U.S. military servicemembers who may be eligible for a lower interest rate on their FFEL Program loans under section 527 of the Servicemembers Civil Relief Act (SCRA).

## Chairman Enzi

**The President's budget proposes to limit to $57,500 the amount of loan forgiveness an individual can receive under the Public Sector Loan Forgiveness (PSLF) program, a student loan repayment program that provides loan forgiveness after ten years of full-time employment in an eligible public service or nonprofit job. How many borrowers does the Administration now expect to have loans forgiven under PSLF, and how many of them will have their forgiveness total impacted (reduced) by the $57,500 cap?**

The President's Budget proposes to limit PSLF for loans made in the future. For loans issued in 2016, the Administration estimates that 15 to 20 percent of borrowers participating in income-based repayment plans will have loans forgiven under PSLF. Of those borrowers participating in PSLF, an estimated 15 to 20 percent will have their forgiveness total reduced due to the $57,500 cap. Over the budget window, under credit reform scoring, the $57,500 limitation, combined with disallowing payments made under non-income driven plans to apply to PSLF, would save $2.3 billion.

## Chairman Enzi

**The projected cost of the outstanding $700 billion federal direct student loan portfolio was re-estimated upward by $22 billion (FY 2015 re-estimate) "due primarily to greater enrollment in income-driven repayment plans, like IBR" according to the *Budget Justifications* for the Department of Education. Please provide data showing original projections for enrollment in these plans, and current enrollment projections.**

Please see attached.

**Repayment Plan Distribution PB2015 Compared to PB2016**

| PB2015 | | | | | | | |
|---|---|---|---|---|---|---|---|
| **Stafford** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** |
| Standard | 65.07% | 71.36% | 71.36% | 71.36% | 70.75% | 70.68% | 70.64% |
| Extended | 6.72% | 5.43% | 5.43% | 5.43% | 5.38% | 5.38% | 5.38% |
| Graduated | 14.08% | 9.93% | 9.93% | 9.93% | 9.84% | 9.83% | 9.83% |
| IBR | 14.13% | 13.29% | 13.29% | 13.29% | 14.03% | 14.11% | 14.16% |
| **Unsubsidized** | | | | | | | |
| Standard | 60.72% | 65.03% | 65.03% | 65.03% | 64.38% | 64.30% | 64.26% |
| Extended | 7.70% | 6.37% | 6.37% | 6.37% | 6.31% | 6.30% | 6.30% |
| Graduated | 16.15% | 13.28% | 13.28% | 13.28% | 13.15% | 13.14% | 13.13% |
| IBR | 15.43% | 15.31% | 15.31% | 15.31% | 16.16% | 16.26% | 16.31% |
| **PLUS** | | | | | | | |
| Standard | 60.44% | 65.22% | 65.22% | 65.22% | 64.68% | 64.62% | 64.58% |
| Extended | 8.96% | 9.19% | 9.19% | 9.19% | 9.12% | 9.11% | 9.10% |
| Graduated | 20.94% | 12.59% | 12.59% | 12.59% | 12.49% | 12.48% | 12.47% |
| IBR | 9.66% | 12.99% | 12.99% | 12.99% | 13.71% | 13.79% | 13.84% |
| **Consolidated** | | | | | | | |
| Standard | 41.00% | 48.73% | 42.84% | 46.73% | 41.61% | 41.41% | 40.82% |
| Extended | 5.14% | 3.59% | 6.47% | 7.17% | 4.84% | 4.87% | 4.60% |
| Graduated | 14.52% | 15.90% | 11.08% | 8.83% | 8.96% | 8.96% | 8.93% |
| IBR | 39.34% | 31.78% | 39.61% | 37.27% | 44.59% | 44.76% | 45.65% |

| PB2016 | | | | | | | |
|---|---|---|---|---|---|---|---|
| **Stafford** | **2008** | **2009** | **2010** | **2011** | **2012** | **2013** | **2014** |
| Standard | 71.69% | 74.70% | 76.93% | 76.93% | 76.93% | 76.93% | 76.93% |
| Extended | 2.03% | 1.65% | 0.91% | 0.91% | 0.91% | 0.91% | 0.91% |
| Graduated | 12.23% | 10.09% | 9.53% | 9.53% | 9.53% | 9.53% | 9.53% |
| IBR | 14.04% | 13.56% | 12.63% | 12.63% | 12.63% | 12.63% | 12.63% |
| **Unsubsidized** | | | | | | | |
| Standard | 61.95% | 65.46% | 67.73% | 67.73% | 67.73% | 67.73% | 67.73% |
| Extended | 5.21% | 4.10% | 2.74% | 2.74% | 2.74% | 2.74% | 2.74% |
| Graduated | 14.89% | 12.30% | 10.92% | 10.92% | 10.92% | 10.92% | 10.92% |
| IBR | 17.95% | 18.15% | 18.61% | 18.61% | 18.61% | 18.61% | 18.61% |
| **PLUS** | | | | | | | |
| Standard | 67.31% | 67.66% | 67.79% | 67.79% | 67.79% | 67.79% | 67.79% |
| Extended | 7.50% | 6.71% | 5.32% | 5.32% | 5.32% | 5.32% | 5.32% |
| Graduated | 19.13% | 16.39% | 11.97% | 11.97% | 11.97% | 11.97% | 11.97% |
| IBR | 6.06% | 9.24% | 14.92% | 14.92% | 14.92% | 14.92% | 14.92% |
| **Consolidated** | | | | | | | |
| Standard | 42.45% | 41.79% | 42.51% | 47.41% | 46.09% | 27.17% | 20.08% |
| Extended | 5.21% | 5.61% | 3.71% | 1.77% | 2.39% | 1.31% | 2.48% |
| Graduated | 16.35% | 17.99% | 15.86% | 10.05% | 10.16% | 7.02% | 5.16% |
| IBR | 36.00% | 34.60% | 37.92% | 40.78% | 41.37% | 64.51% | 72.28% |

Note: The PB 2016 consolidation income-based repayment take-up assumption also incorporates a modelling change to better account for income-based repayment plan take-up in graduate student PLUS. The costs of IDR for graduate PLUS borrowers had been accounted for in a different payment plan. In other words, some (but not all) of the change in the consolidation section is better presentation, not an increase in cost.

## Chairman Enzi

**According to the *Budget Appendix* tables, more than one in five Stafford and Unsubsidized Stafford loans currently being issued are expected to end up in default. With more than $1 trillion in federal student loan debt outstanding - and average loan balances of graduates continuing to increase - does the Department expect to continue to rely increasingly on loan forgiveness expansion as an alternative to borrower repayment of loans?**

Helping students avoid default through income-based repayment plans will ultimately serve taxpayers well by ensuring the responsible repayment of student loans. This strengthens the economy by encouraging more young people to go to college and by keeping loan repayments manageable by pegging them to a student's ability to pay. In addition, the Budget proposes to reform income-driven repayment plans to ensure that program benefits, including loan forgiveness, are targeted to the neediest borrowers. Specifically, the Budget proposes to establish a 25-year forgiveness period (increased from the current law 20-year forgiveness period) for borrowers with balances above the aggregate loan limit ($57,500) for independent undergraduate students (graduate loan borrowers would be most likely to have balances above this amount and be subject to the longer repayment period); and to cap PSLF at the aggregate loan limit for independent undergraduate students to protect against institutional practices that may further increase student indebtedness, while ensuring the program provides sufficient relief for students committed to public service.

## Chairman Enzi

**The President's budget includes $400 billion in displayed net mandatory health care savings. The President also call for an extension of CHIP funding, a permanent Medicare "doc fix", an immigration plan that would increase health spending and new Medicare spending as a result of turning off the BCA sequester. When you add these elements of the President's budget to the $400 billion in displayed net mandatory health savings, what is the new net health savings amount?**

The Budget includes about $400 billion of specified net health savings that grow over time, extending the life of the Medicare Hospital Insurance Trust Fund by approximately five years, and building on the Affordable Care Act with further incentives to improve quality and control health care cost growth. This includes a proposal to accelerate physician participation in high-quality and efficient health care delivery systems by repealing the Medicare Sustainable Growth Rate formula and reforming Medicare physician payments in a manner consistent with the reforms included in recent bipartisan, bicameral legislation.

These savings are estimated against the Budget's adjusted baseline, which assumes that large reductions in Medicare physician payment rates required by law under a formula, commonly referred to as the "sustainable growth rate" (SGR), do not take place. This formula has called for reductions in physician payment rates since 2002, which the Congress has routinely overridden for more than a decade. Including this adjustment to baseline spending allows the Administration to better represent current policy.

Outside of the $400 billion in net health savings, the Budget also proposes to extend funding for the Children's Health Insurance Program (CHIP), which ends in 2015, through 2019, ensuring continued, comprehensive, affordable coverage for children enrolled in CHIP. This proposal is paid for through an increase in tobacco taxes that will help reduce youth smoking and save lives.

The Budget continues to propose commonsense, comprehensive immigration reform that would strengthen border security, modernize the legal immigration system, and provide a path to earned citizenship. The Congressional Budget Office (CBO) estimates that the 2013 Senate-passed immigration bill, S. 744, would have reduced deficits by almost $1 trillion over 20 years. The Budget includes an allowance for the budget effects of immigration reform based on the CBO cost estimate.

Finally, the Budget includes $185 billion in net costs to replace mandatory sequestration government-wide. The policy estimates for the President's Budget for Medicare include the effects of the proposal to replace mandatory sequestration, along with the effects of all of the Budget's health savings proposals.

## Chairman Enzi

**The Highway Trust Fund faces severe financial challenges. Since 2005, spending has exceeded revenues because gas-tax levels plateaued while spending grew. To make up for funding shortfalls, the trust fund has required large general fund transfers totaling more than $60 billion since 2008. Although trust fund solvency has been temporarily extended until May 2015, there is still no long term solution. CBO projects that the Highway Account of the Highway Trust Fund will not be able to meet all of its obligations sometime during the latter half of Fiscal Year 2016 and that about $173 billion will be required between now and 2025 to keep the trust fund solvent.**

**How does the President's budget alter the long-term outlook for the Highway Trust Fund? Should we eliminate the Highway Trust Fund altogether and fund all highway improvement programs with discretionary funds? What gas tax rate is required to ensure the solvency of the Highway Trust Fund indefinitely?**

The Budget incorporates the existing Highway Trust Fund into a new, multimodal Transportation Trust Fund (TTF). Assuming the surface transportation spending levels proposed for FY 2016 through FY 2021, the budget provides sufficient revenue to ensure TTF solvency for that same six-year period. Just like the Highway Trust Fund, the TTF is proposed as a vehicle to provide fiscal resources and multi-year certainty for transportation investments across the Nation. The Budget uses transition revenue from pro-growth business tax reform to offset the cost of President's six-year surface transportation proposal beyond what existing gas tax receipts can cover. The proposal fills both the gap between baseline receipts and baseline spending for the six-year period of the reauthorization and all of the outlays associated with programmatic increases during the reauthorization.

Beyond the reauthorization window -- i.e., after FY 2021 -- the Budget assumes that spending returns to baseline levels based on what was enacted in 2015. Other fiscally responsible solutions will be required beyond the six-year reauthorization period.

## Chairman Enzi

**The President's Budget, like last year, proposes making spending from the Land and Water Conservation Fund mandatory. How many additional acres of land will be acquired by the federal government if funding from the LWCF is made mandatory?**

The number of acres acquired through LWCF programs depends greatly on the mix of funding between programs and on the mix of land acquisition projects. Over one-third of the LWCF funding in the President's 2016 Budget would support grant programs to help State and local governments and private landowners to preserve parks, manage forests, and conserve wildlife habitat.

As for land acquisition projects, many involve conservation easements that allow private landowners to keep the lands working while still providing ecological benefits. Other projects provide hunters, anglers and hikers with better access to existing public lands; the Budget sets aside $20 million in mandatory and discretionary funding for just this purpose. A number of projects involve only a few acres, but have high costs, because they are protecting Civil War battlefields or smaller parks in rapidly urbanizing areas. In many cases, acquisitions support simpler, more efficient land management and address urgent threats to some of America's most special places. Often, projects are proposed in response to State and local priorities.

Given these variables, it is not possible to predict the number of acres that would be acquired if funding from the LWCF is made mandatory. However, the Departments of Agriculture and the Interior will work in cooperation with local communities, rely on willing sellers, and maximize opportunities for easement acquisitions.

## Chairman Enzi

**According to the Centers for Medicare and Medicaid Services' Budget Justification, CMS has spent $4.5 billion on 152 full-time employees for the Obamacare exchanges. Please provide a detailed breakdown of these expenditures by line item, and per employee.**

As shown in the CMS Congressional Budget Justification, CMS obligated $4.5 billion for the State Exchange Grant program from FY 2012 through FY 2014. The vast majority of this funding was provided in grants to States. In FY 2014, of the $784 million obligated, $743 million was for State awards, and $43 million went to the administration of the program, which includes FTE, contracts, and other support costs.

## Sen. Johnson

**Please clarify your answer to my colleague, Sen. Sessions: The Budget Control Act of 2011 (BCA), which President Obama signed into law, caps discretionary spending in 2016 for defense at $523 billion and for nondefense categories at $493 billion, for a total of $1,016 billion. Your budget proposes discretionary spending in 2016 for defense at $561 billion and for nondefense categories at $530 billion, for a total of $1,091 billion. Is $1,091 billion greater than $1,016 billion? Answer yes or no.**

When President Obama signed the BCA in 2011, the law specified a discretionary spending cap for 2016 of $1,107 billion. If the Congress takes no further action, the failure of the Joint Select Committee on Deficit Reduction means that sequestration levels will return in full in 2016, bringing discretionary funding to its lowest level since 2006, adjusted for inflation. A return to sequestration levels would result in insufficient resources for critical investments in areas including research and development, early learning, and national security.

The President's Budget builds on the approach taken in the Bipartisan Budget Act of 2013 (BBA) by proposing to end sequestration, fully reversing it for domestic priorities in 2016, matched by equal dollar increases for defense. These increases in the discretionary caps are more than fully paid for with a balanced package of mandatory spending cuts, program integrity measures, and commonsense tax loophole closures.

## Sen. Johnson

**Again to clarify your answer to Sen. Sessions, you said that while your budget increases discretionary spending, you offset the increases "with mandatory spending reductions." When Sen. Sessions asked whether your budget increases discretionary spending for FY2016 by more than is permitted in the Budget Control Act, you replied, "We more than fully pay for those with reductions in spending on the mandatory side." FY2015 spending is projected at $3,759 billion on your summary table S-5, while FY2016 spending is projected to be $3,999 billion, or $240 billion higher. If you fully paid for the discretionary increases with reductions in spending on the mandatory side, please explain how total spending rose. Which category of mandatory programs on Summary Table S-5 shows a reduction in spending between FY2015 and FY2016?**

In response to Senator Sessions, I stated that the Budget proposes to lift the sequestration caps which have been harmful to our military readiness and economic growth, and that the Budget more than fully pays for those increases "with reductions in spending on the mandatory side and reducing wasteful spending in the tax code." Summary Table S-5 shows receipts and spending under 2016 Budget policies in each year of the budget window. Assessing the effects of the President's Budget (as with any budget proposal) is best accomplished by comparing the receipt and spending levels with receipt and spending levels under the baseline, rather than comparing changes in receipts and spending from year to year, which are due to many factors other than the budget proposals.

Summary Table S-2 shows how the President's policies would impact deficits relative to the baseline. As the table shows, the Budget more than pays for all new initiatives, including sequestration relief, and reduces the deficit by $1.8 trillion over ten years (not including savings from reduced spending for Overseas Contingency Operations) compared to what would happen in the absence of the President's policies.

## Sen. Johnson

**When you discussed the BCA sequester, you said that such discretionary spending levels would harm the nation's defense. Your budget reduces defense spending as a share of GDP from 3.5% in FY2014 to 2.3% in 2025. Over the past 20 years, the federal government has spent on average 3.8% of GDP on defense, and over the past 30 years, it has spent 4.1% on defense. Does the president believe that our national defense will be adequate if spending is equal to 2.3% of GDP, about 56% of the 30-year historical average?**

The levels proposed in the President's Budget over the next 10 years include increases of $182 billion above the current law caps for national defense discretionary spending between FY 2016 - FY 2021. The FY 2016 Budget will reverse five years of declining national defense spending and maintain real budget authority for national defense discretionary spending at levels comparable to averages over the past thirty years.

Comparing these amounts to historical averages as a percentage of GDP does not adequately measure whether defense spending provides sufficient resources for national defense. A more appropriate measure is whether the activities needed to ensure the safety of the American people and advance our national security interests are sufficiently funded.

By reversing harmful cuts that would occur under sequestration and including critical reforms, the President's FY 2016 Budget appropriately resources the missions needed to execute the defense strategy as laid out in the 2014 *Quadrennial Defense Review* and the *National Security Strategy.* The Budget also continues to balance defense spending increases with commensurate increases in non-defense investments that will sustain America's growing economic strength – a foundation of our national security and a critical source of our influence abroad.

## Sen. Johnson

**Your budget calls for federal revenue that rises to 19.7% of GDP by 2025. Your budget's own historical tables note that federal revenue has reached or exceeded that level in only one of the 70 fiscal years since the end of World War II. You agreed with me at the hearing that economic growth was crucial to producing the additional revenue needed to fund the federal government. Please explain how a federal capture of a portion of the nation's output at the top of historical norms will be consistent with strong economic growth.**

The Budget increases revenues as a share of GDP to their levels of the late 1990s, a period that saw rapid GDP, investment, and job growth and the only balanced budgets of the last 40 years. This revenue is needed to meet our commitments to seniors as the Baby Boom generation retires, while also reducing the debt as a percent of GDP and making critical investments that support economic growth.

Moreover, the Budget raises revenue in pro-growth ways. For example, about a fifth of the revenue raised by the Budget comes from immigration reform, which the Congressional Budget Office and others have estimated would increase economic growth and productivity. The largest new revenue raiser in the Budget not only closes a loophole that lets the wealthiest households avoid capital gains taxes other families have to pay, it would also help unlock capital for more productive investment. Other significant revenue raisers in the Budget include transition revenue from pro-growth business tax reform, curbing inefficient high-income tax expenditures, and imposing a fee on large and heavily-leveraged financial institutions to discourage risky bets that can have costs for the broader economy.

## Sen. Kaine

**As you know, my state of Virginia experiences an especially pronounced impact from the across-the-board cuts known as sequestration. I have witnessed the impact of budget uncertainty firsthand, visiting military installations, private shipyards, research universities, and early childhood education centers across the Commonwealth. In the President's Budget proposal for FY2016, he proposes to replace $74 billion of the $90 billion in discretionary spending cuts scheduled to take effect. Over I 0 years, he proposes to replace about two-thirds of the discretionary sequester cuts scheduled through FY2021, the end of the Budget Control Act austerity measures. However, this means that about one-third of these discretionary cuts are left in place, all in the defense side of the budget.**

*** Is it the President's position that we should continue to strive to replace as much of the discretionary sequestration cuts as we can?**

*** Will you commit to working with me to repeal the full amount of sequester, instead focusing on smart budgeting?**

When the Congress failed to enact the balanced long-term deficit reduction required by the Budget Control Act of 2011, the sequestration cuts that took effect in March 2013 had both harmful economic impacts and severe programmatic impacts, including shortchanging investments that contribute to national security and future growth, reducing economic opportunity, and harming vulnerable populations. Returning to the mindless austerity of sequestration in 2016 would bring discretionary funding to its lowest level since 2006, adjusted for inflation, weakening America's security and our economy at a time of accelerating growth.

As the President has said, sequestration is bad for our national security and bad for growth. While we look forward to working with the Congress on a responsible approach that continues to protect our national security and accelerate our economic growth, he has said he will not accept a budget that locks in sequestration levels going forward. The President's Budget builds on the approach taken in the Bipartisan Budget Act of 2013 (BBA) -- proposing to end sequestration, fully reversing it for domestic priorities in 2016, matched by equal dollar for dollar increases for defense. These increases in the discretionary caps are more than fully paid for with a balanced package of mandatory spending cuts, program integrity measures, and commonsense tax loophole closures.

The President's approach is a responsible and sustainable alternative to current law, making the investments necessary to support economic growth, economic mobility, and national security, while continuing to make progress in meeting the Nation's fiscal goals. It ensures that our military can execute our defense strategy while balancing defense spending with our priorities here at home.

We are committed to working with the Congress to replace the mindless austerity of sequestration with smart investments that strengthen America, and I look forward to working with you to that end.

## Sen. Murray

**Thank you Chairman Enzi and Ranking Member Sanders.**

**And thank you Director Donovan for joining us today to talk about the President's budget proposal and answering some of our questions. As we all know, budgets are about far more than numbers on a page. They represent our values, our priorities, who we are as a nation today-and what we hope to be in the years ahead.**

**They lay out where we should be investing-**

*** to help our families, veterans, and small business owners-**

*** and to lay down a strong foundation for long-term growth.**

**They lay out where we should be cutting-**

*** to keep programs efficient- to eliminate those that are no longer needed or effective-**

*** and to make sure government is truly working for the people it serves.**

**And they lay out how we think government should be financed-**

*** to make sure the wealthiest Americans and the biggest corporations are paying their fair share- while we work to help middle class families keep more of their hard-earned money.**

**So I am very glad the President's budget proposal lays out a vision for a government and an economy that prioritizes jobs, middle class families, and broad-based economic growth.**

**This budget proposal isn't perfect-and I'll get to some issues I plan to work with my colleagues and the Administration on in a bit ...**

**... but I believe it is a strong starting point for Democrats and Republicans to work together to build on the bipartisan budget deal we reached at the end of 2013 that helped the economy**

*** and moved us away from the constant budget crises and job-killing automatic cuts.**

**So Chairman Enzi, Ranking Member Sanders-**

*** I know many of us here on this Committee are ready to work together in a bipartisan way to get this done.**

**We don't need to wait for another crisis before the next bipartisan budget deal-**

*** and I think our constituents would be very disappointed if this Committee and this Congress reverted back to the bad old days of partisanship and crises on the budget.**

**Director Donovan-I have a number of questions and issues I hope to work with you on in the coming months, but I want to take a few minutes today to talk to you about a big one.**

**As a Senator from Washington state, one of my top priorities in the annual budget is providing funding for cleanup work at the Hanford site in Central Washington.**

**As I have said many times before, the Administration and the Department of Energy are responsible for producing a budget that ensures the federal government meets the milestones that have been set at defensive environmental cleanup sites like Hanford and others across the country.**

**So, with that in mind, I applaud the Administration for increasing the FY16 budget request for Environmental Management to $5.8 billion,**

*** which is $200 million more than yonr budget proposed last year.**

**However, I am very concerned that the Administration has once again decided to cut Hanford's Richland Operations by nearly $100 million - just like last year.**

**Given these cuts, I would like to know how the Administration believes it will still be able to meet its commitments to Hanford.**

*** Can you explain the Administration's justifications for this cut? And more importantly can the federal government meet the legally binding commitments it has made to the Tri-Cities community under the Tri-Party Agreement at this reduced funding level?**

The 2016 Budget includes $2,328 million ($109 million above the 2015 enacted level) for the Hanford site, which includes $914 million ($93 million below the 2015 enacted level) for Richland and $1,414 million ($202 million above 2015 enacted) for River Protection. The shift from the Richland Office reflects completed work in the River Corridor, consistent with the site's 2015 Vision to shrink the active footprint from 586 to 75 square miles, and the Administration's commitment to addressing the highest priority cleanup activities in the Environmental Management portfolio.

As you are aware, technical and project management challenges have negatively impacted the Department's ability to meet its commitments in the Tri-Party Agreement and the 2010 Consent Decree. To address these issues and to enhance the probability of project execution success, the Secretary established a special working group in August 2013 to analyze factors that contribute to the success or failure of DOE projects and recommend changes to improve project performance. This group's in-depth analysis culminated in the Improving Project Management report, which provides valuable case studies and recommendations regarding project ownership, independent oversight, funding, front-end planning, and culture from experienced project management leaders. In response to the report, on December 1, 2014, the Secretary directed key actions for improving the Department's management of projects:

- Strengthening the Energy Systems Acquisition Advisory Board
- Establishing a Project Management Risk Committee
- Improving the Lines of Responsibility and the Peer Review Process

Regarding lines of responsibility and peer review, the Secretary directed each Under Secretary to establish its own project assessment office that does not have line responsibility for project execution. Beginning in FY 2016, the Department will transfer the functions of project assessment from EM to the Office of Management and Administration (MA), coincident with the establishment of the new Project Assessment office reporting to the Under Secretary for Management and Performance. In addition to the previous project management functions that occurred within MA, this new office will now also provide independent oversight and assessments of EM construction and capital asset projects greater than $100 million, including all activities involved with cost, schedule, technical and management status review, as well as performance progress of the projects. To the extent milestones are delayed, DOE will follow

the provisions under the Tri-Party Agreement for making notifications and working with regulators regarding schedule adjustments, if necessary.

## Sen. Perdue

**Can you provide this Committee with an explanation of the long-term effects to the Highway Trust Fund in relation to the President's tax plan on repatriating foreign earned profits?**

Under current law, the Highway Trust Fund is authorized to expend more resources than it collects. The Budget uses transition revenue from pro-growth business tax reform to offset the cost of President's six-year surface transportation proposal beyond what existing gas tax receipts can cover. The proposal fills both the gap between baseline receipts and baseline spending for the six-year period of the reauthorization and all of the outlays associated with programmatic increases during the six-year reauthorization.

The Administration has identified a revenue source that will sustain baseline spending levels and programmatic increases in the Budget's proposed six-year reauthorization -- a longer reauthorization than Congress has enacted since 2005. Nonetheless, the offset does not offer a permanent solution. Beyond the reauthorization window (after FY 2021), the Budget assumes that spending returns to baseline levels based on what was enacted in FY 2015. Accordingly the structural gap between baseline trust fund spending and baseline trust fund receipts returns. Policy-makers will need to work together to develop other fiscally responsible solutions beyond the six-year reauthorization period.

## Sen. Perdue

**Middle fifth quintile incomes have shrunk in the last few years from $53,008 to $47,243. How will the President's tuition-free community college plan improve the income for these middle class families and what data do you have to support that?**

The President's proposals would benefit middle-class families and those striving to reach the middle class. These proposals include substantial tax benefits for middle-income parents with children in child care or in college and for dual-earner couples, an increase in the minimum wage, an expansion of the EITC, and new ways for workers to save for retirement. America's College Promise is part of the President's efforts to strengthen the middle class.

Today, more than ever, Americans need new knowledge and skills to meet the demands of a growing global economy without having to take on decades of debt before they even embark on a career. By 2020, an estimated 65 percent of job openings will require postsecondary education or training. America's College Promise will prepare millions of Americans with the skills they need for the jobs of the future by eliminating community college tuition for students willing to work for it. The America's College Promise proposal would create a new partnership with States to help them waive tuition in high-quality programs for responsible students, while promoting key reforms to help more students complete at least two years of college. This proposal will require everyone to do their part: community colleges must strengthen their programs and increase the number of students who graduate, States must invest more in higher education and training, and students must take responsibility for their education, earn good grades, and stay on track to graduate.

## Sen. Perdue

**The President is advocating increasing the Earned Income Tax Credit as part of his "middle class" reform package. Could you provide data on how raising the EITC would raise middleclass incomes, specifically the middle fifth quintile of incomes?**

The President's tax proposals would benefit families at a range of income levels – from a boost for minimum-wage workers from raising the EITC to substantial tax benefits for middle-income parents with children in child care or in college. The Treasury Department has estimated how these proposals would affect families across the income distribution, and those estimates are reproduced below. Overall, the proposed tax policies will benefit over 44 million families, who would receive an average tax cut of nearly $600. This is in addition to the benefits families will receive from tbe President's proposals to partner with States to make community college free for responsible students and to expand access to quality child care.

In particular, the President has proposed to increase the EITC for workers without children and non-custodial parents. The President's proposal would double the maximum EITC available to these workers, increase the income level at which the credit phases out, and make it available to workers age 21 and older (versus 25 and older under current law). The proposal would directly reduce poverty and hardship for 13.2 million working Americans, build on the success of the EITC for families with children in promoting employment, and promote economic mobility, especially by encouraging young adults at the beginning of their working lives to develop a stronger attachment to the labor force.

**Proposals to Improve the Tax System for Families, 2016***

| Adjusted Gross Income | All Families Number (thousands) | Families with a Tax Change | | | | |
|---|---|---|---|---|---|---|
| | | Number (thousands) | Percent of Families | Amount ($ millions) | Percent of Total Tax Change | Average Tax Change ($) |
| 0 <= 15,000 | 51,902 | 11,603 | 22.40% | -7,844 | 31.70% | -676 |
| 15,000 <= 30,000 | 30,570 | 6,128 | 20.00% | -2,819 | 11.40% | -460 |
| 30,000 <= 40,000 | 14,232 | 2,344 | 16.50% | -712 | 2.90% | -304 |
| 40,000 <= 50,000 | 11,503 | 2,521 | 21.90% | -910 | 3.70% | -361 |
| 50,000 <= 60,000 | 9,353 | 2,445 | 26.10% | -1,110 | 4.50% | -454 |
| 60,000 <= 75,000 | 10,806 | 3,578 | 33.10% | -2,042 | 8.30% | -571 |
| 75,000 <= 100,000 | 13,266 | 5,650 | 42.60% | -3,644 | 14.70% | -645 |
| 100,000 <= 200,000 | 19,083 | 10,896 | 57.10% | -5,580 | 22.60% | -512 |
| 200,000 <= 500,000 | 5,888 | 784 | 13.30% | 40 | -0.20% | 51 |
| 500,000 and above | 1,460 | 69 | 4.70% | 21 | -0.10% | 300 |
| Total** | 169,583 | 46,238 | 27.30% | -24,725 | 100.00% | -535 |

Department of the Treasury
Office of Tax Analysis

28-Jan-15

*Includes proposals to reform child care incentives, simplify and better target tax benefits for education, expand the EITC for workers without qualifying children, and provide a second-earner credit.

**Families with negative income are included in the total line only.

## Sen. Portman

**I understand that the Department of Labor may send its ERISA fiduciary rule to OMB this month. Given the considerable controversy and opposition surrounding this rule, will you commit to a full review of the rule by the Office of Information and Regulatory Affairs to ensure that the concerns regarding its economic impacts are evaluated and addressed and that the rule complies with the requirements of Executive Orders 12,866 and 13,563?**

If the Administration decides to move forward with the Department of Labor's Conflict of Interest draft proposed rule, the Office of Information and Regulatory Affairs (OIRA) will review this rule for consistency with Executive Orders 12866 and 13563.

## Sen. Wyden

**The Secure Rural Schools and Community Self-Determination Act, or SRS, is one of my top priorities. I thank the Administration for supporting SRS reauthorization in the Budget, and while the funding level is certainly not as much as SRS counties need, I'm glad to get confirmation that SRS is important to the Administration. I look forward to working with you to ensure that SRS can continue to support counties across the country**

The Administration remains prepared to work with the Congress to fund an appropriately targeted extension of the Secure Rural Schools program, with a realistic phase-out of payments by 2019, and to identify agreeable offsets.

## Sen. Wyden

**The President is asking Congress for a base defense budget of $534 billion, which would exceed the mandatory spending caps by $35 billion. The President is also seeking an additional $51 billion to fund the war in Afghanistan and other so-called "overseas contingency operations." These numbers strike Oregonians as astronomical sums, and they are: military spending represents half the yearly discretionary budget. My constituents are clamoring for a full throated debate on the military budget and priorities. But it's hard to have that debate when it's impossible to follow the money. That's why yesterday I joined Senators Paul, Manchin, and Cruz in introducing the Audit the Pentagon Act, a bill that would require the Defense Department to achieve a clean audit by 2017.**

**Wouldn't it be easier to ensure that our military spending is not being wasted if there was an accounting of where every dollar went?**

The Administration fully supports obtaining a clean opinion for the Department of Defense (DOD) and we are working closely with the Department on this effort. DOD has made significant progress toward achieving auditability in recent years, thanks to senior leadership engagement, clear priorities and guidance, dedicated resources, and appropriate governance mechanisms in place. Drawing on the lessons learned from the U.S. Marine Corps' audit of its Schedule of Budgetary Activity (SBA), the Department has been pursuing a phased approach for the Statement of Budgetary Resources (SBR). The initial phase is to achieve audit readiness on the current year funds on the SBA and work towards audit readiness of the prior year balances of the SBR. The Army, Navy and Air Force are undergoing an audit of their General Fund SBA for Fiscal Year 2015 funds.

An additional key initiative supporting sound financial management is improving the quality, utility, and transparency of Federal financial information through existing initiatives under the President's Open Government Directive and in accordance with statutory requirements, including the Digital Accountability & Transparency Act (DATA Act). DOD has been a crucial partner in the government-wide efforts to improve Federal spending transparency, through its leadership of the Government Accountability and Transparency Board and participation in the DATA Act Interagency Advisory Committee.

## Sen. Wyden

**This year, Oregon small ports were dealt a huge blow, with 9 out of the 13 small ports receiving $0 in the President's FY16 budget. Small ports are the backbone of local economies in coastal states, supporting tourism, commercial fishing, and Coast Guard fleets. With critical maintenance work needed at small ports up and down the Oregon coast to keep the ports healthy and the local economies moving, a lack of funding only pushes this maintenance back further and causes the problems to grow, requiring even costlier repairs and maintenance down the line.**

**In the past the State of Oregon has stepped in to help fund some of the maintenance, but a long-term, reliable solution is needed keep our small ports open for business.**

**What is it going to take to get the necessary funding for small ports now and in the future?**

The 2016 Budget for the Army Corps of Engineers civil works program (Corps) focuses on water resources investments that are likely to produce high economic, environmental, and safety returns to the Nation, within the three main mission areas of the agency (flood and storm damage reduction, commercial navigation, and aquatic ecosystem restoration). It provides $1.95 billion for the Corps commercial navigation program, which is 41 percent of the total Corps request, including $79.2 million that will benefit the users of Oregon's coastal ports, and the ports of the Columbia River in three States (Oregon, Washington, and Idaho). In allocating funding, the Corps generally gives priority to maintaining the coastal ports and inland waterways with the most traffic. It also gives priority to constructing navigation improvements with a high economic return to the Nation, and to studies and design of proposals to deepen, widen, or otherwise improve the Federal channels of our coastal ports.

## Sen. Ayotte

**I wanted to ask you about the solvency we've talked about, the demographic problems that we have with Medicare and Social Security. And the numbers that I've gotten is we've got the demographic problem as the challenge as we look at it is very immediate, not -- it's more than a demographic challenge when it comes to the Social Security Disability Fund because, as I understand it, the trustees have said that the fund will be exhausted in 2016, which is next year.**

**Does the president's budget do anything to address the structural issues or the fact that this disability fund is going to be exhausted next year? And I'm worried because the people who really need this, if we ignore this, obviously, they will only be able to pay 81 percent of disability benefits. Do you do anything about that in the budget?**

The President believes that Social Security is indispensable to workers, retirees, survivors, and people with disabilities. As you note, the Social Security Trustees project that the Disability Insurance (DI) Trust Fund reserves will be depleted in 2016. The FY 2016 President's Budget includes a proposal to address the near-term reserve depletion of the DI Trust Fund.

Specifically, the Budget proposes to temporarily reallocate existing payroll tax collections between the Old-Age and Survivors Insurance (OASI) and DI trust funds. Under the budget proposal, both trust funds would be able to provide full benefits until 2033.

Presidents from both parties have worked to enact legislation to reallocate between the trust funds, both from OASI to DI and the reverse, since the inception of the DI program in the 1950s. Similarly, both parties in Congress have enacted reallocations over the years. It is important that Congress act to make sure DI benefits continue to be paid in full in 2016 and beyond, thus ensuring that workers who have paid into the Social Security system and become disabled get the benefits they need. The Administration and Congress must work together to take action and reallocate the payroll tax rate between the trust funds to avoid deep and abrupt cuts in benefits for individuals with disabilities who paid into the system while they worked and now need help.

The Budget also includes proposals to strengthen the Social Security system and services for people with disabilities. It fully funds Continuing Disability Reviews (CDRs), which ensure only those eligible for benefits continue to receive them, and it establishes a reliable funding stream for CDRs beginning in 2017. The Budget also proposes a $400 million initiative for SSA to test innovative strategies to help people with disabilities remain and succeed in the workforce. The Administration appreciates Congress' $35 million appropriation in FY 2015 to begin this effort and looks forward to quickly making progress on this initiative. Further, the budget also includes several proposals to prevent/recover improper as well as reduce duplicative payments.

# THE COMING CRISIS: SOCIAL SECURITY DISABILITY TRUST FUND INSOLVENCY

**WEDNESDAY, FEBRUARY 11, 2015**

UNITED STATES SENATE,
COMMITTEE ON THE BUDGET,
*Washington, D.C.*

The Committee met, pursuant to notice, at 10:01 a.m., in Room SD–608, Dirksen Senate Office Building, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Grassley, Sessions, Crapo, Graham, Toomey, Ayotte, Wicker, Corker, Perdue, Sanders, Stabenow, Whitehouse, Merkley, Baldwin, Kaine, and King.

Staff Present: Eric Ueland, Republican Staff Director; and Warren Gunnels, Minority Staff Director.

## OPENING STATEMENT OF CHAIRMAN ENZI

Chairman ENZI. Good morning. I will call this hearing to order. I would mention that we had some regular chairs taken out so there would be room for wheelchairs. Both Senator Sanders and I serve on the Health, Education, Labor, and Pensions Committee, and we know that the disability community is very important and needs to be accommodated. And we will try and do that at all the hearings, not just this one.

The intention of this hearing is to have an open, bipartisan discussion on the problems caused once the Disability Insurance Trust Fund becomes exhausted. We also want to talk about ideas for how Congress and the President might work together to address these problems.

I would mention that I try to get as much information in the hearing as possible, and you will note that in the second panel, one of the witnesses was a part of the Obama administration, and the other is an international expert on disability and comes to us with a lot of experience.

I have to say that I was dismayed to learn from press reports and inquiries from off-the-Hill sources and, most importantly, senior citizens who rely on Social Security that the Democrats on this Committee released a paper accusing us of wanting to privatize Social Security. That paper and that accusation was not shared with me by other staff or by Senator Sanders. I am disappointed in that. We share offices that are just across the road from each other, and I hope that we can have a little more conversation on some of those things.

But I want to be clear: No one on this Committee is suggesting that we privatize Social Security. No one on this Committee would

support cutting benefits by 19 percent, which is exactly what is going to happen if we do not fix the Social Security Disability Insurance Trust Fund. No one supports Social Security going bankrupt.

The Federal Government's primary program to assist the disabled will soon be broke, and, regrettably, President Obama is not doing anything to ensure that this never, ever happens again. His effort to paper over the problem is a classic example of Washington ducking a real American need. In this case, disabled Americans and workers deserve a long-term solution so that the program does not once again flirt with disaster and, more importantly, reflect the full ability of the disabled to contribute their talents to our country.

As Budget Chairman, I have the ability to look closely at the operations, the functions, the programs, the Federal budget. How are they working? What is their impact on our budget bottom line? Are there ways to fix what does not work or improve the program and help our budget?

One of the most amazing programs we have which touches so many Americans in very critical ways and impresses the world is what we do to support the disabled. America is a large-hearted country, and in reflection of our caring for some of the neediest among us, for almost 60 years the Federal Government has operated a Disability Insurance program. The program's concept is simple: Employed Americans pay a small tax. In the event that they ever become disabled, the program provides them support if they can no longer work and earn a living.

This year, the disability program will benefit up to 11 million Americans. These beneficiaries are our constituents. They had jobs. They paid a tax into the system. Then in some way at some point they became disabled; they could no longer work or earn a living or support a family. This is where the disability program stepped in. It lent an able hand of support so that potential income that was lost was in some way offset.

But now this program is under threat, a threat that it will run out of money. And that is not a surprise to anyone except maybe the President. The officers of the Government directly responsible for the program have been telling the Government for years that it will run out of money. In fact, I think they started suggesting it in 1994, and they even predicted that it would be 2016 that it would run out of money. So this should not be any big surprise. Outside analysts of the program have been telling the Government for years that it will run out of money. The disabled community has been telling the Government for years that it will run out of money.

Maybe I ought to say that one more time. It has been predicted. Suddenly the President woke up to the fact this year. Perhaps it is because now we know for sure not just that we will run out of money but, based on our own Treasury Department's figures this month, when it will be broke.

Let me put this as clearly as possible. No waffle words, no Washington word games. By December of next year or early January, the program will be broke if we do not fix it. And once broke, the law governing the program means that benefits for the disabled must be cut or delayed. That is just rotten.

But that is not all the bad news. Once that fund becomes insolvent, our congressional budget experts tell us the program will need $352 billion over the next 10 years in order to fully pay disability claims. I have a chart up over there that shows the fund with money, coming down to a crossover point where it does not, and that crossover point, of course, is next December. That is less than a year from that crossover.

For Wyoming alone, this means 13,900 disabled people would lose $3 million in benefits. In Vermont, this means that 24,500 disabled people would have their benefits reduced by $5 million. And, Senator Sanders, we represent two of the smaller States. Looking around the Committee room, millions of additional Americans from all our States could see their benefit cut.

In the face of this crisis facing 11 million Americans, what does the President propose to guarantee a robust and enduring program for them and succeeding generations? He proposes a plan that seems to be something but actually turns out to be nothing. Instead of thinking about how best the disabled—by creating a long-term solution, the best values for them and the program, the President has suggested that all we need to do is shift payroll tax revenue coming in from other programs to cover the shortfall in the disability program. All this does is pass the buck to another Congress and another President after Barack Obama leaves office.

We had a President years ago that said, "The buck stops here." and we need to stop the buck.

President Obama's transfer plan runs up the debt we owe to pay the retirement benefit Social Security recipients rely on. We call it a "trust fund." Do not trust a Federal trust fund. There are not dollars stashed away anywhere. There are no dollars in the Disability Trust Fund, and there are no dollars in the Social Security Trust Fund. We actually more accurately ought to call it "accounts payable" because it is further debt. We spent the money.

Most importantly, it leaves all working Americans and the disabled without certainty about the program and unable to fully live out their ability to live the American dream. Why do I say that? Well, the ability to tap human potential has changed dramatically since the program was first created in 1956. According to a recent article in The Economist, the Disability Insurance program's whole design is antiquated. It presumes that people, once disabled, cannot work. If they do, they usually lose their benefits. Yet lots of people with disabilities can work. Wheelchairs did not stop FDR from becoming President or Gregg Abbott from becoming the Governor of Texas.

On behalf of those who use it, we need to modernize the Disability Insurance program. In the 1950s, when workers were doing manual labor and they experienced a debilitating condition, many times that was it. They could not work anymore. But the work our constituents do has changed as our service and knowledge economy has grown significantly during the past six decades.

Thanks to technology, people are also more likely to work from home. They have flexible hours and even start their own businesses. All of these changes have made it easier for those with disabilities to continue working. And studies have shown that those

with disabilities tend to be happier, healthier, and have higher incomes when they are working.

I have another chart up here, and it shows in 1982 how many people had their own labor income as opposed to now and who have just the SSI and SSDI income. So it dropped from 23 percent down to 12 percent, and the reliance increased from 14 to 25 percent.

Unfortunately, as the chart on the screen shows, the disabled today are less likely to earn income from working than ever before. This is true even after Congress passed the Americans with Disabilities Act of 1990 mandating changes in the workplace intended to facilitate employment for the disabled. Buried deep in the President's budget are a few programs that might be a grudging acknowledgment there is much more to be done to create a disability system that can support the ability of disabled Americans to still contribute to our workforce.

I am encouraged by some of the demonstration ideas proposed in the President's budget to keep those with disabilities in the workforce. However, we need to do more without putting an additional burden on our finances. We should be working in partnership along with Republicans, Democrats, House and Senate, and the President to provide long-term security our disabled deserve and the program finances that fit our balance sheet. Together we can do better. To protect the most vulnerable among us, we should all agree that political gamesmanship must not get in the way of our commitment to help our constituents who need us the most.

Senator SANDERS.

**OPENING STATEMENT OF SENATOR SANDERS**

Senator SANDERS. Thank you very much, Mr. Chairman.

Before I get into my remarks, let me respond briefly to something that you just said about some of us, and I will take that responsibility of suggesting that some of my Republican colleagues are looking forward to either cutting Social Security or moving to the privatization of Social Security. That is exactly what I said. And let me quote to you from the Atlanta Journal Constitution, a major newspaper in Georgia, from Tom Price, who, as you know, is the chairman—not just any Republican; he happens to be chairman of the House Budget Committee—from a January 15, 2015, article. I will just excerpt some of it. But he says:

"On the issue of Social Security, it has indeed been the third rail as Tim Chapman mentioned, and I am hopeful of what the Budget Committee will be able to do is to begin to normalize the discussion and debate about Social Security."

Then he goes on to say: "So all the kinds of things you know about—whether it is means testing, whether it is increasing the age of eligibility. The kind of choices—whether it is providing much greater choices for individuals to voluntarily select the kind of manner in which they believe they ought to be able to invest their working dollars as they go through their lifetime. All those things ought to be on the table and discussed."

So what he is talking about is looking at cutting benefits or moving toward the privatization of Social Security.

Now, Mr. Chairman, the Social Security Disability Insurance program is a life-and-death program for nearly 11 million Ameri-

cans, including more than 1 million veterans and 1.8 million children. This is a program that American workers have paid into. It is an insurance program. This is not charity. When Americans pay 6.2 percent of their income in the payroll tax, almost 1 percent of that amount goes into the Disability Insurance program.

The average Disability Insurance benefit is less than $1,200 a month, and for 30 percent of the beneficiaries, this is their entire income. Nobody is getting rich off of disability benefits.

Sadly, on the very first day of the new Congress, House Republicans passed a rule that would lay the groundwork for a 19-percent cut in Social Security Disability Insurance benefits. This means, if that cut were to go through, that the average benefit of approximately $13,980 a year for a disabled person would be cut by $2,600 to $11,324. Does anybody on this Committee really believe that a person with a severe disability—maybe they are facing a terminal illness, maybe they are paralyzed, maybe they have had their legs amputated. Does anybody in this room really believe that a disabled person in America should be forced to live on $11,324 a year?

Mr. Chairman, in my view, the debate we are having today is nothing more than a manufactured crisis which is part of the long-term Republican agenda of trying to cut Social Security. And in my view, this is a terrible and dangerous idea.

Today Social Security has a $2.8 trillion surplus and can pay out every benefit owed to every eligible American for the next 18 years. That is not the opinion of Bernie Sanders. That report comes from the Social Security Trustees.

Now, because of an aging population, because of more women in the workforce, because of an increase in the retirement age, there has been an increase in the number of Americans who are receiving disability benefits.

Mr. Chairman, this is not a surprise. This is a demographic reality that the Social Security Administration predicted would happen back in 1994. The fact that the Social Security Disability Insurance program is facing a funding shortfall next year is a surprise to absolutely no one. Furthermore, and importantly, shortfalls in the Social Security Disability Insurance program or the Social Security retirement program are nothing new. It has happened 11 times in the past and has always been resolved in a simple, noncontroversial way and a nonpartisan way, and that is by the reallocation of funds between the Social Security Retirement Fund and the Social Security Disability Fund.

As this chart shows, reallocation was done in 1968 under President Johnson, in 1970 under President Nixon, in 1978, 1979, and 1980 under President Carter, in 1982, 1983, and 1984 under President Reagan, in 1994, 1997, and 2000 under President Clinton.

Interestingly—and this is interesting—the 11 times that funds were reallocated from one fund to the other, it turns out that on five occasions it was the Disability Fund that was reallocated to help the Retirement Fund.

Mr. Chairman, every major senior citizen organization in this country, including the AARP—and I, believe their letter is on the desks of everybody in this room—including the National Committee to Preserve Social Security and Medicare, the Alliance for Retired

Americans, and many other organizations representing over 60 million older Americans, all support reallocation and are united in opposition to the rule passed by the House Republicans to make reallocation more difficult.

Here is what, very briefly, the AARP letter says, and it is up there on the chart: "To prevent any imminent reductions in SSDI benefits, we urge you to rebalance the allocation of Social Security payroll taxes between the OASI Trust and the DI Trust, as Congress has done with success in the past. Because of the SSDI, millions of disabled Americans are able to live their lives with dignity and support their families. The highest priority in the near term is to ensure that SSDI beneficiaries, most of whom are older Americans, are not put at risk of a 20-percent benefit cut in the very near future." End of quote from AARP.

I am delighted that President Obama proposed this reallocation plan in his budget request.

Mr. Chairman, the Social Security Trust Fund can pay out every benefit owed to every eligible American for the next 18 years. There is no imminent crisis. But I do agree with many of my colleagues on both sides of the aisle and with many economists that it is terribly important that we do better than 18 years to make sure that Social Security is there for our kids and for our grandchildren. In my view, the best way to extend the solvency of the Social Security Trust Fund over the long term is to eliminate the cap that currently exists on taxable income that goes into the Social Security Trust Fund.

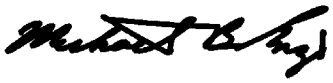
Right now, in the midst of massive wealth and income inequality which we see in our country, a Wall Street CEO who makes $20 million a year pays the same amount into Social Security as someone who makes $118,500. That is wrong. In 2013, I asked the Chief Actuary of the Social Security Administration to estimate how long the solvency of Social Security would be extended based on legislation that I authored which would apply the Social Security payroll tax on income above $250,000, lift the cap on all income above $250,000. His answer was that the Social Security Trust Fund would be made solvent, Mr. Chairman, until 2060—45 years from today.

And, Mr. Chairman, I would ask unanimous consent to inset that letter into the record.

Chairman ENZI. Without objection.

Senator SANDERS. Thank you.

[The letter follows:]



# FOR THE RECORD

**Statement**
**on**
**"The Coming Crisis: Social Security Disability Trust Fund Insolvency"**

**America's Health Insurance Plans**
**601 Pennsylvania Avenue, NW**
**South Building, Suite 500**
**Washington, DC 20004**

**Submitted to the**
**Senate Budget Committee**

**February 11, 2015**

## I. Introduction

AHIP is the national association representing health insurance plans that provide health and supplemental benefits to more than 200 million Americans. Our members offer a broad range of products, including private disability income protection that replaces lost income in the event that a disabling condition forces a covered worker to leave the workforce for an extended period of time.

As Members of this Committee know, the Social Security Board of Trustees has projected that the Disability Insurance (DI) Trust Fund, from which Social Security Disability Insurance (SSDI) benefits are paid, will deplete its assets late next year. Our member insurers that provide disability income protection coverage are doing their best to anticipate and prepare for a potential disruption of scheduled SSDI benefit payments – to minimize the confusion, fear, and financial hardship that a drop in SSDI benefits would bring about in financially vulnerable households because private income protection benefits are typically integrated with SSDI benefits.

We appreciate the Committee's interest in exploring solutions to the financial challenges facing the SSDI program. Our members have demonstrated strong leadership in developing innovative programs to meet the needs of disabled workers, including strategies and services to support them in their efforts to return to work and lead productive lives. This emphasis on return-to-work is a particularly important component of the protection offered by private disability income insurers. By helping people overcome their disabilities and return to the workforce, based on consultation with their health care providers, insurers are enabling working Americans they cover to improve both their financial situation and their quality of life. We believe our members' experience in pioneering these initiatives offers valuable lessons for Congress as you consider legislative options for strengthening the financial stability of SSDI. We also believe that savings to the SSDI program, and other federal programs, arising out of private disability income protection suggest that policies to extend income protection to a greater number of working Americans would serve the public interest.

To contribute to the dialogue at today's hearing, our statement focuses on:

- an overview of private disability income protection coverage;
- examples of successful return-to-work strategies used by our member companies;
- analyses of federal savings arising out of private disability income protection;
- the findings of a survey of disability insurer return-to-work practices; and
- the value this coverage offers to policyholders.

## II. Overview of Disability Income Protection Coverage

Private disability income protection provides tens of millions of Americans with coverage that complements the safety net provided by the SSDI program. Approximately 39 percent of U.S. workers in private industry are covered by employer-sponsored short-term disability coverage, while 32 percent receive long-term disability insurance through their employers.[1] This coverage provides a level of disability income that spares many Americans from financial hardship.

Private short-term disability coverage typically pays benefits for 13 to 26 weeks based on a specified percentage of the employee's pre-disability income – typically 60 percent – after sick leave has been exhausted. Circumstances that may trigger the payment of short-term disability benefits include temporary musculoskeletal or connective tissue conditions, pregnancies, and other illnesses or conditions that are resolved within a relatively short timeframe, often allowing the employee to return to work before benefits are exhausted.

The valuable protection offered by short-term disability coverage can be purchased at a reasonable price – an average of $210 annually when purchased as group coverage by employers.[2] This short-term protection can be purchased in combination with long-term disability coverage as part of a seamless package, with the short-term and long-term benefits coordinated to ensure that disabled workers can meet their daily expenses and avoid financial hardship. Long-term disability benefits continue anywhere from five years to the remainder of an individual's life. Long-term disability insurance allows workers to sustain themselves financially if an illness, injury, or disability takes them out of the workplace for an extended period of time. In 2010, the average annual group premium for long-term disability coverage was $245 per covered employee.[2]

## III. Return-to-Work Strategies by Private Disability Insurers

In addition to replacing lost income for claimants in a timely fashion, private disability income insurers have been very proactive in developing return-to-work programs that help disabled workers move forward when they are prepared to reclaim their financial self-sufficiency. This can be an invaluable tool in helping to maintain the productivity of America's businesses. This

[1] U.S. Department of Labor, Bureau of Labor Statistics, *National Compensation Survey: Employee Benefits in the United States,* March 2013
[2] GenRe, *2010 U.S. Group Disability Market Survey Summary Report*, July 2011

role has become more important with the growing impact of employees with chronic diseases, downsizing by employers during the economic downturn, and baby boomers delaying retirement.

A 2010 AHIP report[3], based on interviews with experts at our member companies, describes trends and innovations in the disability income insurance industry. This report reviews a range of successful return-to-work strategies being used by private disability insurers. Several examples are highlighted below.

**Assisting Cancer Patients and Survivors**

Cancer accounts for a large share of long-term disability claims. Most cancer patients ultimately return to work, and it is becoming increasingly common for cancer patients to continue working while they undergo treatment. Employees who remain at work during cancer treatment or return to work after treatment can face fatigue, difficulties with memory and concentration, pain, and even post-traumatic stress. Strategies for supporting employees facing these challenges include allowing time and space for breaks, planning work schedules to avoid the worst times for pain and fatigue, and creating check lists for job tasks to help deal with temporary memory loss. Insurers work with employers to help them anticipate potential difficulties and work around them.

**Modifying Work Environments to Address Functional Limitations**

Musculoskeletal conditions, such as arthritis, are increasingly a factor in the workplace as the U.S. workforce gets collectively older. Workers with these conditions often have difficulties with strength and range of motion that can make it difficult for them to remain in the same job. Insurers work with employers to find successful ways to modify job responsibilities and workstations to allow workers to overcome physical limits associated with arthritis and other musculoskeletal conditions.

**Facilitating Part-Time Work**

In some cases, an employee may be able to continue carrying out the duties of his or her job, but may have limitations that prevent him or her from working effectively on a full-time basis. Such limitations might be most common for older workers. Disability insurers help employers and employees develop flexible part-time schedules that are suited to the needs and preferences of the affected employee.

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[3] AHIP Center for Policy and Research, *Trends and Innovations in Disability Income Insurance*, January 2010

**Enhancing Support for Workers on Long-Term Disability**
Disability insurers typically seek first to help disabled employees return to their previous job with their current employer. When an employee cannot return to his or her previous job or employer, insurers can help the employee prepare for and find another job, begin a new career, or start a business. Insurers provide vocational counseling and help with resume writing, networking, and interviewing. Counselors also help participants identify job goals and potential employers, identify gaps in skills, and access needed training and education.

**Integrating Health and Disability Support Services**
A number of companies that offer both health care and disability insurance support services are integrating and coordinating these services to ensure that workers receive the most effective care for their chronic conditions and can return to work as soon as possible. This approach recognizes the value of addressing all of an individual's medical, social service, and behavioral health needs in a coordinated way, rather than in separate silos.

One company, for example, has established a program through which enrollees who have both health and disability coverage can work with nurse case managers who act as health advocates. Case managers help workers navigate the health care system and access the health care, disease management, and disability-related services they need. When employees feel ready to return to work, vocational rehabilitation counselors coordinate with employers to develop return-to-work plans suited to the employees' needs and abilities. Such plans often include modified work schedules that help employees transition gradually from part-time to full-time work, use of ergonomic work stations and chairs, and changes to physical requirements (such as eliminating heavy lifting).

Another company with an integrated health and disability program makes it possible, with the consent of employees, for health and disability team members to share information about the employees' health and functional status on a real-time basis so they can return to work as soon as possible. This program also includes a role for case managers in consulting with physicians about including return-to-work considerations in patients' treatment plans.

## IV. Federal Savings Arising Out of Private Income Protection Coverage

Private insurer disability management and return to work (RTW) efforts have also been shown to have a positive impact on the SSDI program by putting ill or injured workers on a path that leads

them away from the SSDI program rolls – or shortens the time that they received SSDI benefits. A 2013 analysis carried out by Charles River Associates estimated that private insurers' disability management and return-to-work interventions save the federal government $25 billion over a ten-year period. Almost half of these savings accrue to the SSDI program. The remaining savings arise when ill or injured workers leave the rolls of public programs such as Medicare, Medicaid, and the Special Nutrition Assistance Program (SNAP) when they return to work.[4]

An earlier Charles River analysis indicated that the receipt of private disability income protection benefits lifts up to 575,000 American families out of poverty each year and saves the nation's taxpayers up to $4.5 billion annually by reducing dependence on the Temporary Assistance for Needy Families (TANF) program and SNAP.[5]

Because of the positive fiscal impact of private income protection on SSDI and other federal programs, AHIP and its disability income protection insurer members believe that we have common ground with stakeholders who favor reductions in federal spending and also those who are working to restore the solvency of the SSDI program. Federal policies that would help expand private income protection – and the return-to-work assistance that private coverage makes available – would benefit taxpayers and SSDI beneficiaries, as well as working Americans and employers. Specifically, we believe that the federal government could play a key role in helping to educate and empower working Americans and employers regarding disability income security issues and best return-to-work practices. We also believe that the automatic-enrollment provisions of the Pension Protection Act of 2006 could serve as a model for parallel provisions to extend disability income protection to many more working Americans.

## V. Survey of Disability Insurer Return-to-Work Practices

Additional information about the return-to-work strategies of private disability insurers is revealed by a survey conducted by Milliman, Inc.

The Milliman survey highlights the investments of private disability insurance carriers in rehabilitation and return-to-work efforts, identifies key industry practices that support these initiatives, and highlights the factors that are most crucial to the success of return-to-work

[4] Charles River Associates, *Private Disability Insurance and Return-to-Work: Cost Savings to SSDI and Other Federal Programs*, September 2013

[5] Charles River Associates, *Financial Security for Working Americans: An Economic Analysis of Insurance Products in Workplace Benefits Programs*, July 2011

strategies.[6] For insurers taking part in the survey, return-to-work closures represented 29 percent of all claim closures and 42 percent of all closures (excluding claims closed due to death or at the end of the maximum benefit period).

The following are several key findings of this survey:

- Private disability insurers make significant investments in returning disabled workers to productivity. On average, participating long-term disability (LTD) insurers spent $3,200 on each disabled employee receiving rehabilitation and return-to-work services. The range of disability insurer investment extended as high as $7,600 per return-to-work client.

- Rehabilitation and return-to-work programs offer a wide range of services to disabled employees, including:
    - Medical case management,
    - Vocational and employment assessment,
    - Worksite modification,
    - Purchasing adaptive equipment,
    - Business and financial planning,
    - Retraining for a new occupation, and
    - Education expenses.

- A number of provisions in disability insurance policies play a role in supporting claimant rehabilitation and return-to-work. These provisions include:
    - Work incentive benefits,
    - Rehabilitation benefits,
    - Workplace accommodation benefits, and
    - Child or dependent care benefits during rehabilitation.

- The employer's willingness to participate in a disabled employee's rehabilitation plan is a crucial factor in achieving a successful return to work.

[6] Milliman, Inc., *Survey of Rehabilitation and Return-to-Work Practices Among U.S. Disability Carriers*, May 2007

## VI. Value for Consumers

Recent surveys clearly show the value of private income protection to working Americans. A survey of group disability insurers comprising approximately 75 percent of the commercial disability insurance marketplace indicates that approximately 653,000 individuals received long-term disability payments in 2013 from private insurers participating in the survey. Participating insurers paid a total of $9.8 billion in long-term disability benefits that year. Twenty-eight percent of these claimants receiving private disability income benefits were not receiving SSDI benefits. Moreover, more than 95 percent of reported disabilities were not work-related and, therefore, not eligible for benefits under workers compensation.[7]

A 2008 Harris Interactive survey, published by AHIP, reveals that a large majority of disability insurance claimants are satisfied with their coverage and their experience filing a claim and receiving benefits. Overall, four out of five claimants (82 percent) said that they were satisfied with their disability income insurance policy. Specifically, claimants were satisfied with the process for filing a claim (81 percent), the promptness of the payments (79 percent), the responsiveness of the insurer (75 percent), and the overall communication from their insurer (71 percent).

Other key findings from the Harris Interactive survey include:

- Most claimants who utilized innovative programs offered by insurers – such as return-to-work, rehabilitation, workplace accommodations, education benefits, and help starting a business – were satisfied with these programs. Eighty percent said they were satisfied with the rehabilitation program they participated in; 78 percent were satisfied with the workplace accommodations provided; 70 percent were satisfied with the education benefits they received; 69 percent were satisfied with the return-to-work program they participated in; and 64 percent were satisfied with the support they received to help start a business.

- Two-thirds of claimants (66 percent) did not encounter any problems with the claims process and for those that did, the vast majority (84 percent) had their problem resolved satisfactorily.

[7] Council for Disability Awareness, *2014 Long-Term Disability Insurance Claims Survey*, September 2013

- The vast majority of claimants (96 percent) say it is at least somewhat likely that they would have suffered financial hardship if they did not have disability income protection. Furthermore, two-thirds (67 percent) say it would have been very or extremely likely that they would have suffered financial hardship.

- Most private disability insurance claimants who also received SSDI benefits (79 percent) said they were satisfied with the process for filing and receiving benefits.

- Ninety-seven (97) percent of SSDI claimants said it was at least somewhat likely that they would have suffered financial hardship if they had received only their SSDI benefits and not private disability insurance benefits.

## VII. Conclusion

We appreciate this opportunity to share our perspectives on the interaction of private disability income protection and the SSDI program. We look forward to working with this Committee and other congressional committees to maintain and strengthen the disability income security of working Americans – and to improve the long-term fiscal strength of the SSDI program.

Senator SANDERS. Mr. Chairman, we all know that the huge increase in wealth and income inequality in America has seen millions of Americans lose a substantial part of their income. The middle class is shrinking. In fact, while the wealthiest people have become much wealthier, real median family income today is almost $5,000 less than it was in 1999.

Now, this is a tragedy unto itself, but it has also had a major impact on Social Security. If income inequality—and this is really an amazing fact. If income inequality remained at the same level today as it was in 1983, Social Security would have $1.1 trillion more than it does today because workers with higher income would have contributed more into the system. If the payroll tax had simply continued to cover 90 percent of all earnings, which it did in 1983, rather than the 83 percent that it covers today, the Social Security Trust Fund would be able to pay every benefit owed to every eligible American, not just for the next 18 years, but for the next 38 years.

So the bottom line is, short term, we have to do what has been done 11 times in the past. Long term, we have to work together to make Social Security solvent for our kids and our grandchildren. In the midst of massive wealth and income inequality in this country, we have got to lift the cap on taxable income.

Thank you.

Chairman ENZI. Thank you, Senator.

I just want to have everybody aware that I am keeping track of what the House does as well—not that we have to do what the House does, but I need to know what they are doing. And I have been following their rules, and their rules do not prohibit a reallocation, nor does it call for benefit cuts. It does include a point of order against reallocation only if the move is not accompanied by policies to improve solvency of the combined Social Security Trust Fund. And there are a number of ways to do that. I mentioned that the President has some in his budget. So it will allow reallocation as long as it includes savings for the OASDI program, however small. Otherwise, the next time that we reach this crisis, we will have about three of these funds coming due at the same time, and we will not be able to shift the money. So I hope everybody understands that, and I want to thank you for your comments.

For our first panel, our witness is Carolyn Colvin, and she has served as the Acting Commissioner of Social Security since February 14, 2013. Prior to this designation, she served in a number of roles at the Social Security Administration under the Clinton administration, including Deputy Commissioner for Policy and External Affairs, Deputy Commissioner for Programs and Policy, and Deputy Commissioner for Operations.

Ms. Colvin has also served in a number of other public positions in the District of Columbia and Maryland, including as Director of Human Services for the District of Columbia. Ms. Colvin has graduate and undergraduate degrees in business administration from Morgan State University.

For the information of colleagues, Acting Commissioner will take about 5 minutes for her opening statement, followed by questions.

Thank you for being here.

**STATEMENT OF CAROLYN W. COLVIN, ACTING COMMISSIONER, SOCIAL SECURITY ADMINISTRATION**

Ms. COLVIN. Good morning. Chairman Enzi, Ranking Member Sanders, members of the Committee, thank you for opportunity to discuss the status of the Social Security Disability Insurance Trust Fund, our efforts to help people with disabilities reenter or stay in the workforce, our Continuing Disability Review process, and the steps we have taken to ensure the integrity of our disability decisions. My name is Carolyn Colvin, and I am Social Security's Acting Commissioner. I have served in this position since February 2013.

The Social Security DI program provides important financial protection for workers who paid into the system and now need help because they have disabilities. Almost 9 million people with disabilities and 2 million of their spouses and children are currently receiving benefits from the DI program.

Realize that these are very modest benefits, $1,165 average per month per worker. Because the program is vital to workers and their families, we must take steps to ensure its stability and avoid deep and abrupt cuts or cessation of benefits for individuals with disabilities.

To this end, the President's fiscal year 2016 budget proposes to address the near-term DI reserve depletion by reallocating a part, 0.9 percentage points of payroll taxes, from OASI to the DI Trust Fund for just 5 years, 2016 through 2020.

The temporary reallocation the President proposes will have no effect on the overall health of the combined OASI and DI Trust Funds, which will remain adequately financed until 2033 on a combined basis. Nor will it result in a change for workers and employers who will continue to pay the same amount of FICA taxes they do now.

The proposal to reallocate existing payroll tax collections between the OASI and DI Trust Funds is consistent with past congressional action where Congress approved legislation as needed for reallocation from DI to OASI or vice versa. These are earned benefits. These two funds provide social insurance for Americans at all stages of life. The same worker who becomes disabled today will become a retiree in the future.

To strengthen the DI program and ensure its integrity, we ask your support for several initiatives. The Social Security Act includes incentives to encourage disability beneficiaries to return to work by allowing continuation of benefits and medical coverage while working or pursuing an employment goal. Although these have produced modest success, we want to explore new ideas. It is essential that we, including Congress, can make evidence-based decisions on innovations to improve the ability of individuals with disabilities to succeed in the workforce. Conducting demonstration projects is the best way to gather the evidence needed to evaluate policy options.

While our previous demonstrations have shown that interventions after individuals qualify for DI benefits can yield positive outcomes, earlier interventions may prove more effective. Thus, the President's fiscal year 2016 budget provides continued support for

a multiyear initiative to test strategies to help people with disabilities remain and succeed in the workforce.

We appreciate Congress's $35 million appropriation in fiscal year 2015 to begin this effort. The budget requests $50 million in fiscal year 2016 and a legislative proposal requesting $350 million over the following 3 fiscal years.

We take very seriously our stewardship of the DI Trust Funds and taxpayers' money. We strive to make the right payment to the right person at the right time. We use cost-effective Continuing Disability Reviews to determine whether an individual continues to be medically qualified. To select cases for these reviews, we use predictive models to target cases where medical improvement is most likely.

The President's fiscal year 2016 budget proposes a dedicated program integrity fund to support 908,000 full medical CDRs, a 15-percent increase over fiscal year 2015. We estimate that CDRs conducted in 2016 will yield a return on investment of about $9 on average in net Federal savings over 10 years per $1 budgeted. We use a strict, single national definition of disability. When evaluating disability claims, every decisionmaker must use the criteria in the act and our regulations.

We have multiple levels of quality reviews to ensure that the rules are applied uniformly and correctly. As required by law, we review at least a half of initial and reconsideration disability allowances before payment is made. These pre-effectuation reviews allow us to correct any errors before we issue a final decision on eligibility. We also extensively train and use tools to enable our adjudicators to follow our policies accurately and consistently such as a Web-based Claims Analysis Tool that helps to ensure policy compliance by requiring examiners to follow all the steps in our disability claims evaluation process as well as comparative tools and data analytics.

In conclusion, thank you for the opportunity to discuss the vitally important DI program and our continued efforts to improve its administration. I will be happy to answer any questions you have.

Thank you.

[The prepared statement of Ms. Colvin follows:]

**COMMITTEE ON THE BUDGET**

**UNITED STATES SENATE**

**FEBRUARY 11, 2015**

**STATEMENT FOR THE RECORD**

**CAROLYN W. COLVIN**
**ACTING COMMISSIONER**
**SOCIAL SECURITY ADMINISTRATION**

Chairman Enzi, Ranking Member Sanders, and Members of the Committee:

Thank you for the opportunity to discuss the status of the Social Security Disability Insurance Trust Fund, the steps we have taken to ensure the integrity of Disability Determination Services (DDS) and Administrative Law Judge (ALJ) decisions, our efforts to help people with disabilities reenter or stay in the workforce, and our Continuing Disability Review process. My name is Carolyn Colvin, and I am the Acting Commissioner of Social Security.

Throughout my career, I have met people from all walks of life who struggle to cope with severe disabilities. Whether their impairments are mental or physical, by birth or circumstance, these individuals face extraordinary challenges. We must never underestimate the very real challenges and the day to day struggles faced by people with disabilities.

**Introduction**

The Social Security Administration (SSA) administers a number of programs, including the Old-Age and Survivors Insurance (OASI) and Disability Insurance (DI) programs, commonly referred to as "Social Security." Social Security is a social insurance program, under which workers earn coverage for retirement, survivors, and disability benefits by working and paying Social Security taxes on their earnings. The DI portion of Social Security helps replace a portion of the lost earnings for workers who, due to their significant health problems, can no longer work to support themselves and their families. DI also ensures that workers who become disabled and their families are protected from the loss of future retirement benefits.

The same people who may be receiving disability today at 55 will be receiving retirement benefits later.

We take our responsibilities in administering Social Security very seriously. In 2014, we paid $698 billion to more than 47 million retirement and survivor beneficiaries, and $141 billion to nearly 11 million DI beneficiaries and their family members. We administer the Social Security program with tremendous efficiency. For example, in Fiscal Year (FY) 2014, our administrative expenses were only around 0.6 percent of the Social Security benefits we paid for the year.

The vitally important DI program, however, will face challenges next year in its ability to provide for those workers who are insured for coverage and have severe

physical or mental impairments. The challenges for the Trust Fund have been well understood and projected for decades. In 1995, right after the last tax-rate reallocation enacted by the Congress, the Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds estimated that the DI fund reserves would become depleted in 2016.[1] This shortfall, the Trustees predicted, was related to demographic changes that could be seen far in advance, such as the entry of more women into the workforce, and the progression of the baby boom generation into its most disability-prone years.

These projections from 20 years ago have proven to be quite accurate. According to the 2014 Annual Trustees Report, the Trustees again project that the DI Trust Fund reserves will reach depletion in the last quarter of 2016. If Congress takes no action before this time, we would only be able to pay about 81 percent of scheduled amounts, resulting in benefit cuts. Cutting these benefits would create hardships for a segment of our society that is ill-equipped to endure them. Therefore, the Administration is committed to working with Congress to prevent the reserve depletion of the DI Trust Fund next year, while continuing to discuss longer-term solutions that would address broader solvency issues that are still many years away.

**DI Trust Fund**

As I mentioned earlier, the Social Security DI Program provides insurance coverage to the families of workers who have paid into the system and subsequently have become disabled. The FY 2016 President's Budget proposes to address the near-term DI reserve depletion by reallocating a portion of payroll taxes from OASI to the DI Trust Fund – as has been done many times in the past – to align the reserve depletion dates for the two trust funds. This temporary reallocation will have no effect on the overall health of the combined OASI and DI trust funds, which will remain adequately financed until 2033 on a combined basis. Note that the 2033 reserve depletion date is the one policymakers and the public most often focus on, because they appropriately focus on the Social Security program as a whole.

We believe that the Congress must take action to reallocate a portion of the payroll tax rate between the trust funds to avoid deep and abrupt cuts or delays in benefits

[1] See http://www.ssa.gov/history/reports/trust/1995/.

for individuals with disabilities who paid into the system while they worked and now need help. The proposal to reallocate payroll tax collections on a temporary basis between the OASI and DI trust funds is consistent with past congressional action, where Congress has approved legislation as needed for reallocation from DI to OASI, and vice versa.[2]

The FY 2016 President's Budget includes a reallocation proposal. In our Budget proposal, the reallocation lasts for five years and the share of the total payroll tax going to the DI trust fund increases by 0.9 percentage points. Under this formulation, the reallocation only needs to last five years for the two trust funds to both be able to provide full benefits until 2033. We look forward to working with Congress on the specifics. Workers and employers would continue to have the same FICA deducted, but a somewhat larger share would go to DI than to OASI on a temporary basis to bring the two trust funds into alignment. We look forward to working with the Congress on proposals that would strengthen Social Security for Americans, including current beneficiaries.

**Factors Affecting the DI Trust Fund**

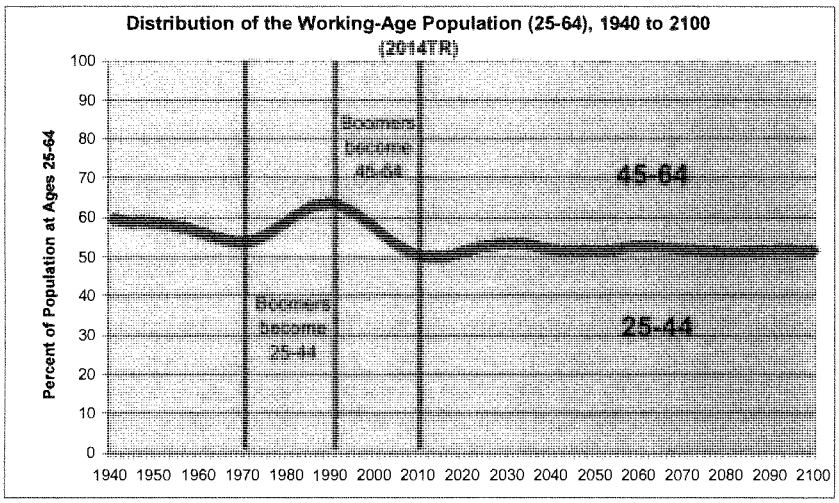
The proposed reallocation of payroll taxes from OASI to DI need only be temporary because – measured over 75 years – the DI trust fund shortfall is actually slightly smaller as a percentage of dedicated payroll taxes. Moreover, DI and OASI are experiencing the same demographic transition, but because individuals qualify for DI at a younger age than eligibility for retirement benefits, that program experiences the full effects first, since the Baby Boom generation has already reached its peak disability years.

As our Chief Actuary, Stephen C. Goss, accompanying me here today, has explained: the growth in the SSDI rolls has long been foreseen and, as expected, has recently slowed. Between 1980 and 2010, the number of disabled worker beneficiaries increased from 2.9 million to 8.2 million. As I noted earlier, nearly all of the growth in the SSDI rolls over this 30-year period can be attributed to a combination of foreseen factors. The first factor is the 41 percent increase from 1980 to 2010 in the total population between the ages of 20 and 64. A second

[2] For example, Congress reallocated payroll taxes from OASI to DI in the *Tax Reform Act of 1969*; from OASI to DI in the *Social Security Amendments of 1973*; from DI to OASI in the *Allocation of Social Security Tax Receipts of 1980*; from DI to OASI in the *Social Security Amendments of 1983*; and from OASI to DI in the *Social Security Domestic Employment Reform Act of 1994*.

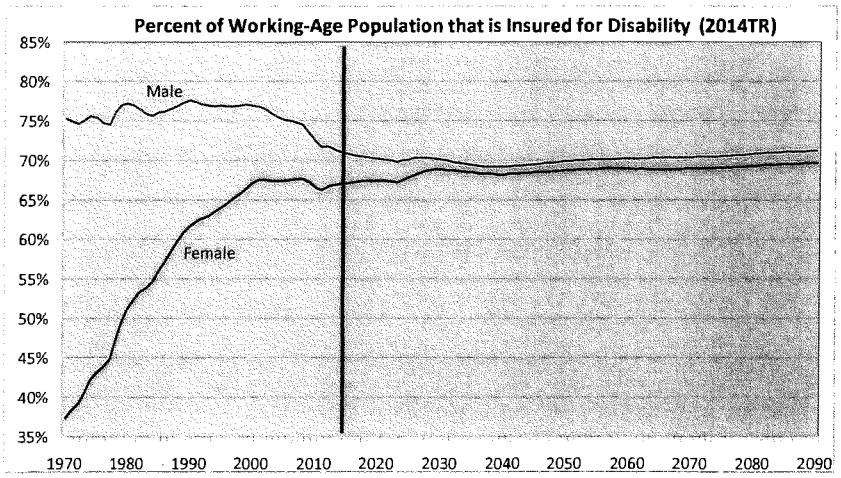
important factor is the changing age distribution of the population, due to the aging of the baby boomers. Specifically, from 1990 to 2010, the baby boomers moved from being young adults, under age 45, to older working adults, ages 45-64, and the ages at which workers become more disability-prone. This anticipated demographic shift has now finished. (See figure 1)

Figure 1.




Another important factor is the increased participation of women in the labor force, which has resulted in many more women being insured for disability (see figure 2). The growth of women in the labor force has contributed positively to economic growth and the fact that these workers have protection against disability is a net positive for their families' economic security.

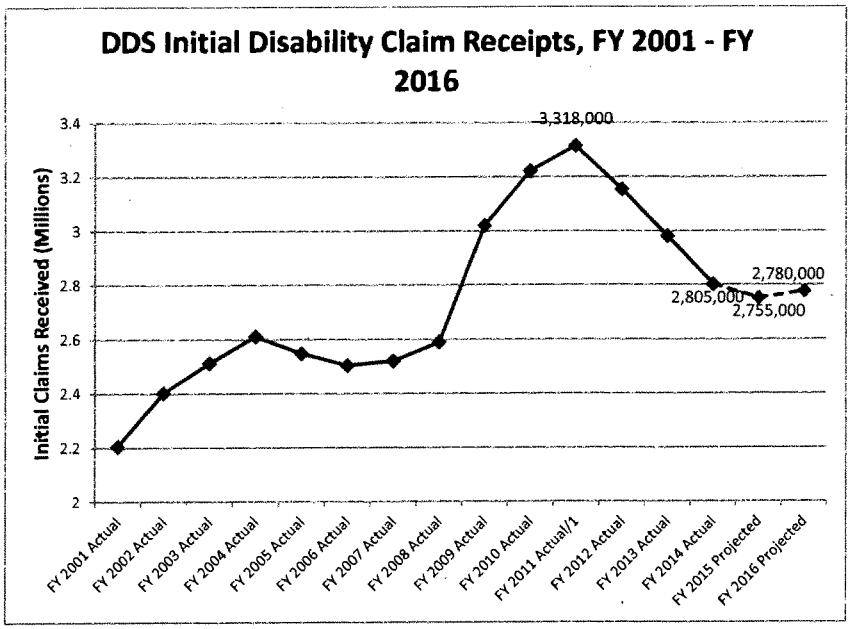
Figure 2.




Between 1980 and 2010, the percent of the working-age population (approximately 20-65) that was insured rose from about 50 to 68 percent for women.

These major factors, in combination with other demographic shifts, are now stabilizing. Indeed, applications for disability benefits have fallen from peak levels of around 3.3 million in FY 2011, to around 2.8 million in FY 2014 (see Figure 3). Mr. Goss is available to explain these foreseen demographic shifts, and the recent slowing of the growth of DI, in greater detail.

Figure 3.




## Overview of the DI Program

In addition to discussing the DI Trust Fund, I would like to share with you information concerning the stringent requirements an applicant must meet to qualify for disability benefits, as well as a general overview of the application process.

### Definition of Disability

The Social Security Act (Act) generally defines disability as the inability to engage in any substantial gainful activity (SGA) due to a physical or mental impairment that has lasted or is expected to last at least one year or to result in death. Under the Act's strict standard, a worker can qualify for DI benefits only if he or she is

insured for Social Security disability protection – meaning they worked substantially in 5 of the past 10 years before becoming disabled[3] – and cannot currently work due to a medically determinable impairment. As the House Committee on Ways and Means noted in its report that accompanied the Social Security Amendments of 1956, even a person with a severe impairment cannot receive disability benefits if he or she can engage in any SGA. The Act does not provide short-term or partial disability benefits.

I would like to stress a salient and often overlooked feature of the DI program. An applicant cannot be found eligible and receive disability benefits simply by alleging pain or other non-exertional limitations. We require objective medical evidence or laboratory findings that show the claimant has a medically determinable impairment(s) that: (1) could reasonably be expected to produce the pain or other symptoms alleged; and (2) when considered with all other evidence, meets our disability requirements.

Because the Act defines disability so strictly, Social Security disability beneficiaries have among the most severe impairments in the country: To give some idea of the standard's stringency, the allowance rate for disability claims in FY 2013 was around 33 percent.[4] While around 30 million Americans ages 21 to 64 self-reported as living with disabilities in the 2010 census,[5] in that same year only about 8 million workers received DI payments. Those who receive DI benefits are more than three times as likely to die in a year as other people the same age. Among those who start receiving disability benefits at the age of 55, one in five men and one in seven women die within five years of the onset of their disabilities.

**The Claims Process**

We take our responsibility to be good stewards of the DI trust funds and taxpayers' money very seriously and strive to provide the highest quality service possible. When we receive a claim for disability benefits, we strive to make the correct

[3] To be insured for Social Security Disability, most individuals must have worked substantially in five out of the prior ten years before the onset of disability. This is in addition to the general 10-year (40 quarters) work requirement needed to gain "fully" insured status.

[4] *See* http://www.ssa.gov/oact/STATS/table6c7.html.

[5] For estimates of the number of Americans living with disabilities, including severe disabilities, see http://www.census.gov/prod/2012pubs/p70-131.pdf.

decision as early in the process as possible so that a person who qualifies for DI benefits receives them in a timely manner. We decide claims for benefits using an administrative review process that consists of four levels: (1) initial determination; (2) reconsideration; (3) hearing before an ALJ; and (4) Appeals Council (AC) review. At each level, the decision-maker bases his or her decisions on the medical and other evidence in the record, the Act, and our regulations and policies.

When evaluating disability claims, every decision-maker must use the strict definition of disability set forth in the Act and our regulations and policies. We have multiple layers of quality review to ensure that our program rules are applied uniformly and correctly. In addition, as required by the Act, we perform a pre-effectuation review of at least 50 percent of all initial and reconsideration disability allowances. These pre-effectuation reviews allow us to correct errors we find before we issue a payment. Estimates show the return on investment of roughly $13 in program savings for every $1 of the total cost of the reviews.[6]

We are continuously developing and improving training and tools to ensure that our adjudicators follow established policies accurately and consistently. For example, at the initial and reconsideration levels, our decision makers use the Electronic Claims Analysis Tool, a web-based application that helps ensure policy compliance by requiring examiners to follow the necessary steps in our disability claims evaluation process. The tool aids in documenting, analyzing, and adjudicating each disability claim according to our regulations.

We now have initiated use of a similar tool – the Electronic Bench Book – at the hearing level. Additionally, for several years we have employed a hearing-level tool that gives adjudicators extensive information about the reasons their favorable and unfavorable decisions were subsequently remanded and allows them to view their performance in relation to the performance of other ALJs in the office, region, and Nation. More recently, we have been incorporating the use of data analytics as another tool to ensure consistent policy compliance and real-time feedback. All of these efforts build on our longstanding commitment and effort to ensure that we provide claimants – who are insured for Social Security coverage – the right decision as quickly as possible.

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[6] For more information about pre-effectuation reviews, see http://www.socialsecurity.gov/legislation/PER%20fy12.pdf

**Return to Work**

As I have discussed, the DI program, together with OASI, provides insured coverage for those Americans who make up a very vulnerable segment of society. While the DI program constitutes a part of our Nation's social insurance, the level of benefits is modest. For example, in January 2015, a worker eligible for DI receives, on average, less than $1,200 in DI benefits per month, or less than $14,000 per year – just above the poverty line. Such DI beneficiary who returns to work may be able to improve upon the modest standard of living provided by DI benefits.

The Social Security Act includes a number of incentives to encourage disability beneficiaries to return to work. Generally, these incentives provide beneficiaries with continued benefits and medical coverage while working or pursuing an employment goal. For example, in the DI program, the incentives include the trial work period, the exclusion of impairment-related work expenses, the extended period of eligibility, and the expedited reinstatement process.[7] In the *Ticket to Work and Work Incentives Improvement Act of 1999*, Congress also created ways for individuals to maintain their Medicare longer or obtain Medicaid coverage even after they have become fully self-supporting and transitioned from the benefit rolls.[8] The Ticket Act also gave beneficiaries more choices to obtain employment services and supports. Beneficiaries could, as before, receive services through State Vocational Rehabilitation agencies or seek assistance from newly formed Employment Networks.

We must not downplay or dismiss the very real difficulties beneficiaries with disabilities face. Because the Act defines disability so stringently, DI beneficiaries have significant disabilities. Realistically, we cannot expect that more than a modest share will return to work or leave the benefit rolls due to substantial earnings. But we must continue to assist those beneficiaries who can retain employment or are able to return to work to do so.

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[7] In the SSI program, work incentives include more beneficial rules for counting income from earnings, the Plan to Achieve Self-Support, special rules about impairment-related work expenses, expedited reinstatement, and continued Medicaid.

[8] A more comprehensive description of our work incentives is available at http://www.socialsecurity.gov/redbook/.

Given the number of individuals who ultimately turn to DI for income security and the cost of the program, it is critical for policymakers to have an evidentiary base from which to consider potential program innovations that would improve the ability of individuals with disabilities to succeed in the workforce. We believe conducting demonstration projects is the best way to gather the evidence needed to evaluate policy options.

We have already tested various initiatives that support DI beneficiaries, so a partial evidence base for policy innovation exists. For instance, the Accelerated Benefits demonstration found that providing health benefits to uninsured DI beneficiaries in the 24-month Medicare waiting period sharply improved their self-reported health status, and providing employment services increased work and earnings. The Mental Health Treatment Study (MHTS) demonstration found that employment supports, along with medical support and coordinated care, were successful in improving health, lowering hospitalizations, and increasing employment for DI beneficiaries with schizophrenia and other affective disorders. Other initiatives, such as the Youth Transition Demonstration, have found that support services can increase employment and earnings for younger beneficiaries.

While our demonstrations have shown that interventions for individuals receiving DI benefits can yield positive outcomes, they also show that not all of these interventions help DI beneficiaries return to full-time employment and leave the DI program. For example, relative to the control group, the beneficiaries who received services in the MHTS were more likely to be employed, but their earnings did not typically rise above SGA and reduce their DI benefits. In other words, comprehensive services to individuals already in the program had positive outcomes, but not at a level that would indicate departure from the disability program was likely.

Earlier interventions, before an individual enters the DI rolls may prove more effective. Consequently, the FY 2016 President's Budget provides continued support for a multi-year initiative for SSA to test innovative strategies to help people with disabilities remain and succeed in the workforce. We appreciate Congress's $35 million appropriation in FY 2015 to begin this effort, and we look forward to quickly making progress on this initiative. This year's Budget includes a request for $50 million in FY 2016, and a legislative proposal requesting $350 million total in mandatory funding for FYs 2017-2020 in conjunction with a reauthorization of the larger DI demonstration authority.

Specifically, we propose to partner with other Federal agencies and the public workforce system to test innovative strategies to help people with disabilities remain in the workforce. Early intervention measures, such as supportive employment services for individuals with mental impairments, targeted incentives for employers to help workers with disabilities remain on the job, and incentives and opportunities for States to coordinate services better, have the potential to achieve long-term gains in employment and improve the quality of life of people with disabilities. These proposed demonstrations will help build the evidentiary base for future program improvements.

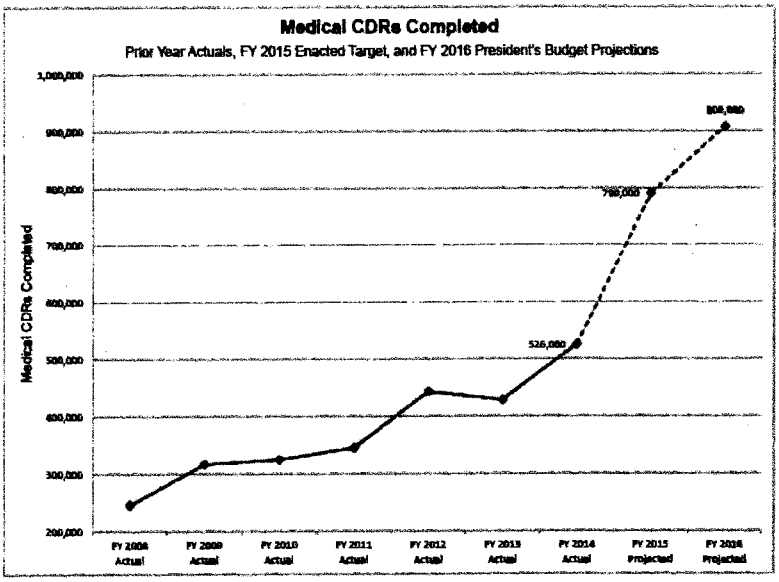
**Program Integrity Initiatives**

The FY 2016 President's Budget contains another important proposal to strengthen the DI program. There is a long-standing adage in our agency – the right check to the right person at the right time. Delivering on this statement preserves the public's trust in our programs. Accordingly, we continually refine and enhance our program integrity tools.

We use Continuing Disability Reviews (CDRs) to determine whether an individual continues to be disabled under the criteria for the DI and Supplemental Security Income Disability programs. We use sophisticated predictive models to ensure that we prioritize reviewing cases where beneficiaries are more likely to have medically improved and are capable of working, which may mean that they are no longer eligible to receive DI or SSI benefits. We estimate that CDRs conducted in FY 2016 will yield a return-on-investment of about $9 on average in net Federal program savings over ten years per $1 budgeted for dedicated program integrity funding, including OASDI, SSI, Medicare, and Medicaid program effects.

In FY 2016, we are using our dedicated program integrity funding for the direct costs of processing CDRs. We will be able to increase the number of full medical CDRs by approximately 15 percent over FY 2015 while continuing to handle a high volume of initial disability claims. We plan to complete 908,000 full medical CDRs in FY 2016 (see Figure 4).

Figure 4.




## Conclusion

Since 1957, Social Security disability benefits have been part of the American fabric, providing insured protection for those Americans who have paid into Social Security through their earnings. We must take the necessary steps in the near term to prevent the depletion of DI trust fund reserves and ensure that disability benefits continue to be paid in full to those Americans who have earned coverage and subsequently acquire a disability.

We thank you for your interest in this important program. We ask for your support for the President's Budget request, which will reallocate payroll tax revenue to the DI trust fund and increase its reserves to a sufficient level until 2033, without risking the financial viability of either the OASI or DI Trust Funds, and without jeopardizing the benefits on which your constituents have come to depend. It

would also invest in learning more about what strategies can help individuals with disabilities remain in the workforce, and would improve program integrity. Moving forward, we stand ready to assist the Congress regarding any Social Security proposals.

Again, thank you for the opportunity to testify today. I am glad to have our Chief Actuary, Stephen C. Goss, with me here today. We will be happy to answer any questions you may have.

Chairman ENZI. Thank you, and thank you very much for your statement, and thank you for meeting separately, of course, with myself and Senator Sanders yesterday. Some of these questions we will have already covered. I was impressed with your answers yesterday.

To start out with questions—and we will have 5-minute rounds of questions—the President's budget has proposed reallocating the payroll tax to delay the DI Trust Fund insolvency. If there were no other changes, does reallocation of the payroll tax worsen the Old-Age and Survivors Insurance Trust Fund for Social Security retirement?

Ms. COLVIN. I am sorry. Say the last part, please?

Chairman ENZI. Does the reallocation worsen the Old-Age and Survivors Insurance Trust Fund for Social Security retirement?

Ms. COLVIN. I think it is very hard to separate the two funds. This is one program. The worker, as you know, pays 6.2 percent, and a portion goes to the DI Trust Fund and a portion to OASI. So I think we really have to think about that in terms of one program, because the person, if they become disabled, would benefit, and then, of course, when they retire they benefit. In fact, many simply transfer from the DI program to the—from the OASI program—from the DI program, I am sorry, to the OASI program.

So I think that it is imperative that we see the reallocation, which would give us adequate time to look at long-term solutions that we need to take.

Chairman ENZI. How much are we reallocating?

Ms. COLVIN. We are reallocating simply 0.9 percent from the OASI Fund to the DI Fund, and that will still allow the program to be solvent through 2033.

Chairman ENZI. Instead of a percent, can you give me dollars that are being reallocated?

Ms. COLVIN. I would need to calculate that. I do not have the exact amount of dollars. I will give it to you in a minute.

Chairman ENZI. Okay. The President's budget proposes several program integrity initiatives that could produce savings. Do you know how much these initiatives would save the Disability Insurance Fund before it is exhausted? And can you mention any of those suggested programs?

Ms. COLVIN. There are a number of proposals in the President's budget. The one that I want to mention first is the funding for the Continuing Disability Reviews. As you know, we should be doing reviews every 3 years. When people come on the rolls, we know that some are likely to improve. And we need to be able to do those reviews to determine if they have, in fact, improved and are no longer disabled.

We have been able to determine that for every $1 that we spend, we bring back $9 into the program. So I think that is a very effective program.

We also are looking at a number of programs or initiatives that we believe would slow down the number of people coming onto the rolls. That would be our early intervention programs where we would be able to test whether or not supportive employment and other types of services would allow people to stay in the job market longer. And, of course, we know that only about 1 percent of our

population go off the rolls now because the definition is so strict and we are serving the most severely disabled.

Chairman ENZI. So you will have some suggestions for how to do that then, I assume?

Ms. COLVIN. We would certainly look forward to working with Congress to come up with solutions that would be bipartisan. I think that there have been many proposals proposed. I think we do have to be cognizant of the impact on the various demographic populations.

I think one of the things that the President has clearly stated is that any proposal really has to strengthen the program. It should not reduce benefits. People should be able to expect a robust disability benefit or a retirement benefit when they need it. But we would be very happy to work with Congress on any initiatives.

Let me mention the figure that you asked for. We would be looking at $330 billion in savings over a 5-year period, through 2016 to 2020. So I think—does that answer your question?

Chairman ENZI. Can you repeat that number for me again?

Ms. COLVIN. $330 billion over a 5-year period from 2016 to 2020.

Chairman ENZI. Thank you. And my next question would take—we will be submitting questions as well, ones that have more detailed numbers than that.

Ms. COLVIN. We would be very happy to provide that.

Chairman ENZI. Okay.

[The questions of Chairman Enzi follow:]

SOCIAL SECURITY
The Commissioner

May 15, 2015

The Honorable Mike Enzi
Chairman, Senate Budget Committee
United States Senate
Washington, DC 20515

Dear Mr. Chairman:

Thank you for your letter requesting additional information to complete the record for the February 11 hearing on the Disability Insurance Trust Fund. Enclosed you will find the answers to your questions, as well as answers to the questions I received from Senators Sessions, Wyden, Warner, Whitehouse, and King. We worked closely with our Chief Actuary, Steve Goss, to respond to the questions related to reallocation. As I indicated in my response, Steve will separately provide additional information related to your first question.

I hope this information is helpful. If I may be of further assistance, please do not hesitate to contact me, or your staff may contact Judy Chesser, our Deputy Commissioner for Legislation and Congressional Affairs, at (202) 358-6030.

Sincerely,

Carolyn W. Colvin

Carolyn W. Colvin
Acting Commissioner

## Questions for the Record

***The Coming Crisis: Social Security Disability Insurance Trust Fund Insolvency***

**Hearing before the Senate Budget Committee**

**February 11, 2015**

**Chairman Mike Enzi**

**1. You mentioned that the President's proposal to reallocate the payroll tax would move $330 billion over five years from dedicated revenues for the Old-Age and Survivors Insurance (OASI) trust fund to the Disability Insurance (DI) trust fund. Please restate this reallocation amount for the first five and the second five years on a per covered worker basis, and separately state the annual interest payments paid to the trust fund by the United States Treasury over this five and ten year period and the period of solvency, or through 2033.**

The reallocation proposal in the President's Fiscal Year (FY) 2016 Budget proposal would result in no net change in interest paid to the combined OASI and DI Trust Funds as the total reserves in the combined funds would be unaffected. I have referred your specific question about average amounts of payroll tax reallocated per covered worker to Steve Goss, our Chief Actuary, who can provide additional information based on assumptions in the 2014 Trustees Report.

The Administration is committed to working with Congress to prevent the reserve depletion of the DI Trust Fund next year, while continuing to discuss longer-term solutions that would address broader solvency issues that are still many years away. The President's Budget includes one possible approach to rebalancing the Trust Funds, but the Social Security Administration (SSA) stands ready to assist the Congress regarding any Social Security proposals, without risking the financial viability of either the OASI or DI Trust Funds and without jeopardizing the benefits on which your constituents have come to depend.

**2. You mentioned in your testimony that reallocations of payroll tax revenues have occurred several times over the life of the Disability Insurance program. Please list the dollar amount of each transfer, the amount expressed as a percent of payroll tax revenue, and the program changes that accompanied each reallocation.**

The table below provides, for the six enacted laws and the President's recent proposal[1], the

[1] These laws and the President's Fiscal Year 2016 Budget proposal include a reallocation of the payroll tax rate between the OASI and DI Trust Funds and, in some cases, change the overall OASDI tax rate.

changes in the total dollar amount of payroll tax over the 75-year projection period from the effective date of each law or proposal. For comparability, we expressed the dollar amounts for each year using the Old Age, Survivors, and Disability Insurance (OASDI) taxable payroll for 2015. These dollar amounts of payroll tax change are not limited to the reallocation years, but include effects for all years for which the payroll tax changed for either fund. Thus, the dollar amounts include all changes specified in the legislation that are due to increasing or decreasing payroll tax rates for either fund.

Attachment A provides the changes in payroll tax rates for each year affected by each law. Subsequent laws overrode some of the payroll tax rates indicated for some laws. Thus, the dollar effects in the table below and the changes in the tax rates for each law indicate the intent of the law at the time.

| **Dollar Changes in Scheduled OASDI Tax Revenue Due to Legislation Involving at Least One Year of Reallocation** | **Total Change: Expressed in Billions of 2015 Dollars*** | |
|---|---|---|
| | OASI | DI |
| (Public Law (P.L.) 90-248)-Social Security Amendments of 1967 | $1,799 | $1,181 |
| (P.L. 91-172)-Tax Reform Act of 1969 | -$709 | $709 |
| (P.L. 95-216)- 1977 Amendments to the Social Security Act | $3,068 | $2,757 |
| (P.L. 96-403)--Allocation of Social Security Tax Receipts of 1980 | $47 | -$47 |
| (P.L. 98-21) Social Security Amendments of 1983 | $4,929 | -$3,760 |
| (P.L. 103-387) The Social Security Domestic Employment Reform Act of 1994 | -$1,934 | $1,934 |
| President's Proposal in FY 2016 Budget | -$293 | $293 |

* OASDI taxable payroll is $6.5 trillion for 2015 (7 percent self employment). Values are derived by applying the annual rate changes as if they each applied in 2015. Annual rate changes are those that applied for any year within the 75-year projection period from the effective date of each law or proposal.

*The calculation of these dollar amounts includes the following steps:
1. For each year in which the payroll tax changed for employees and employers, multiply the change in the payroll tax rate for this group by their taxable payroll in 2015 (93% of $6.5 trillion).
2. For each year in which the payroll tax changed for the self-employed, multiply the change in the payroll tax rate for this group by their taxable payroll in 2015 (7% of $6.5 trillion).
3. Sum amounts in steps 1. and 2. for each year during the 75-year projection period.

Note: For the Social Security Amendments of 1967 and 1977, the increase in payroll tax rates that applied to both the OADI and DI Trust Funds generated positive revenue for both funds over the 75-year period.

Office of the Chief Actuary, SSA
May 12, 2015

Please see Attachment B, which describes some of the program changes that accompanied past laws with tax rate changes that included reallocations.

**3. If the Disability Insurance program relied solely revenue changes to meet all of its obligations and maintain the required minimum trust fund balance between now and 2087, how much additional revenue each between over this time period would be required ("additional" meaning above and beyond currently income from current law payroll taxes)? Also, express this increase as a percent of current law, combined OASI and DI payroll tax rates.**

For years 2016 through 2088, the table below provides one scenario of estimated increases in the DI payroll tax rate that would keep the DI Trust Fund from depleting. This scenario represents the minimum increase needed each year in order to pay full scheduled benefits on a timely basis.

**Percentage-Point Increase in Disability Insurance (DI) Payroll Tax Rate Needed to Keep the Reserves of the DI Trust Fund From Depleting**

| Calendar Year | Increase In DI Payroll Tax Rate Needed | Expressed as a Percent of the Present law Combined OASI and DI Payroll Tax Rate | Calendar Year | Increase In DI Payroll Tax Rate Needed | Expressed as a Percent of the Present law Combined OASI and DI Payroll Tax Rate |
|---|---|---|---|---|---|
| 2016 | 0.013% | 0.001% | 2052 | 0.37 | 3% |
| 2017 | 0.38 | 3% | 2053 | 0.37 | 3% |
| 2018 | 0.33 | 3% | 2054 | 0.38 | 3% |
| 2019 | 0.29 | 2% | 2055 | 0.38 | 3% |
| 2020 | 0.27 | 2% | 2056 | 0.38 | 3% |
| 2021 | 0.26 | 2% | 2057 | 0.38 | 3% |
| 2022 | 0.26 | 2% | 2058 | 0.38 | 3% |
| 2023 | 0.27 | 2% | 2059 | 0.38 | 3% |
| 2024 | 0.27 | 2% | 2060 | 0.37 | 3% |
| 2025 | 0.28 | 2% | 2061 | 0.37 | 3% |
| 2026 | 0.29 | 2% | 2062 | 0.38 | 3% |
| 2027 | 0.29 | 2% | 2063 | 0.38 | 3% |
| 2028 | 0.28 | 2% | 2064 | 0.38 | 3% |
| 2029 | 0.26 | 2% | 2065 | 0.39 | 3% |
| 2030 | 0.25 | 2% | 2066 | 0.39 | 3% |
| 2031 | 0.24 | 2% | 2067 | 0.39 | 3% |
| 2032 | 0.24 | 2% | 2068 | 0.39 | 3% |
| 2033 | 0.24 | 2% | 2069 | 0.39 | 3% |
| 2034 | 0.24 | 2% | 2070 | 0.39 | 3% |
| 2035 | 0.24 | 2% | 2071 | 0.39 | 3% |
| 2036 | 0.24 | 2% | 2072 | 0.39 | 3% |
| 2037 | 0.24 | 2% | 2073 | 0.39 | 3% |
| 2038 | 0.23 | 2% | 2074 | 0.38 | 3% |
| 2039 | 0.24 | 2% | 2075 | 0.38 | 3% |
| 2040 | 0.24 | 2% | 2076 | 0.38 | 3% |
| 2041 | 0.26 | 2% | 2077 | 0.39 | 3% |
| 2042 | 0.27 | 2% | 2078 | 0.40 | 3% |
| 2043 | 0.29 | 2% | 2079 | 0.41 | 3% |
| 2044 | 0.30 | 2% | 2080 | 0.42 | 3% |
| 2045 | 0.31 | 3% | 2081 | 0.43 | 3% |
| 2046 | 0.32 | 3% | 2082 | 0.44 | 4% |
| 2047 | 0.33 | 3% | 2083 | 0.44 | 4% |
| 2048 | 0.34 | 3% | 2084 | 0.45 | 4% |
| 2049 | 0.34 | 3% | 2085 | 0.45 | 4% |
| 2050 | 0.35 | 3% | 2086 | 0.45 | 4% |
| 2051 | 0.36 | 3% | 2087 | 0.45 | 4% |
| | | | 2088 | 0.45 | 4% |

Based on Intermediate Assumptions of the 2014 Trustees Report
Office of the Chief Actuary, Social Security Administration

**4. The Social Security Administration (SSA) reported $744 million in DI overpayments in its most recent Agency Financial Report. What steps does SSA plan to take to reduce overpayments and to better collect the debt owed to the program?**

We provided a consolidated answer to this question in our response to your question #6.

**5. SSA's workload demands are projected to increase over the next decade, yet its workforce faces an ongoing retirement wave and the agency is expected to lose some of its most experienced staff. Please list the steps that the agency is taking to ensure that it will have the appropriate people with the necessary knowledge, skills, and abilities to process disability claims in the coming years.**

On average, four percent of SSA employees retire each year. In FY 2013 (latest information available) 22.2 percent of the SSA workforce was eligible to retire and by FY 2017, 32.7 percent will be eligible. This figure will increase to 44.9 percent by FY 2022. To ensure we have appropriate staff with the necessary knowledge, skills, and abilities to process all agency workloads, including disability workloads, we are undertaking strategies such as modernized recruitment, hiring flexibility, knowledge transfer, succession planning, and leadership development. We have integrated our long-range human capital vision into our agency's business process by creating the Human Capital Operating Plan. The plan serves as our framework for:

- Attracting and retaining a talented and diverse workforce;
- Providing our employees with the proper training and tools; and
- Developing our future leaders.

Our operating plan serves as our commitment to ensuring that all SSA employees have the tools, resources, and skills for today and well into the future, but our plans can only produce results when accompanied by sufficient resources. In FY 2014, we were able to hire new employees, including veterans and individuals with disabilities, to replace half of our staffing losses since FY 2011. With the FY 2015 appropriation, we are continuing to hire claims representatives in our field offices and teleservice centers, and hire more administrative law judges (ALJ) and support staff in our hearing offices. It is important that we maintain our momentum with adequate funding to meet our anticipated workload demands. In addition, we use technology—such as the electronic Case Analysis Tool (eCAT) in our State disability determination services (DDS) offices and the electronic Bench Book (eBB), which we are beginning to use in our hearing offices—to help ensure that our disability decision-makers—including new hires—are making policy-compliant and consistent decisions.

**6. Given the current financial status of the DI Trust Fund, please describe SSA's plans for reducing and recovering benefit overpayments?**

We always take seriously our responsibility to steward our programs prudently—regardless of the status of the trust funds. Our internal quality reviews, which are validated by a third party auditor, indicate that our DI benefit payments are highly accurate; for FY 2013, 99.43 percent of our payments were free of overpayment. However, we are always looking for ways to improve. For the DI program, overpayments most commonly occur when a beneficiary works at or above the substantial gainful activity (SGA) level (in 2015, $1,090 per month for non-blind beneficiaries with disabilities). Under DI program rules, a DI beneficiary may test his or her ability to work during a trial work period (or possibly using other work incentives) and still receive disability payments. However, once the trial work period is exhausted, working at or above SGA generally would result in suspension (or termination) of DI payments.

To reduce overpayments of this type, we developed a statistical model that predicts the likelihood of beneficiaries being at risk of receiving large earnings-related overpayments. In October 2010, we began a pilot in one of our processing centers using a statistical predictive model to prioritize the alerts we receive in our continuing disability review enforcement operation (CDREO), an automated process that matches Internal Revenue Service earnings to our disability rolls to identify unreported earnings for DI beneficiaries. The predictive model allows us to target those cases likely to incur large work-related overpayments first. The predictive model scores cases based on factors such as historical earnings, prior work-related continuing disability reviews (CDR), previous benefit increases due to earnings, overpayments, amount of monthly benefits, time on beneficiary rolls, and type of impairment. In June 2011, we expanded the pilot to include three processing centers, covering over 60 percent of the CDREO workload. In June 2013, we implemented the predictive model nationwide. Since 2011, the average overpayment amount has decreased from $19,500 to $16,200, while the total overpayments due to work have decreased from $1.5 billion to $1 billion.

Based on the success of the predictive model, we are conducting a pilot in our New York region using quarterly earnings data received from the Department of Health and Human Services, Office of Child Support Enforcement (OCSE). The quarterly earnings data we receive from OCSE are more recent than the annual data we currently use in conducting a work-related CDR.

We have a robust debt collection program to recover overpayments in our programs, which enabled us to recover over three billion dollars in benefit overpayments in FY 2014. Please see our report on reducing improper payments that describes our debt collection efforts at http://www.socialsecurity.gov/improperpayments/recoveryEfforts.html.

**7. SSA has been working for several years to update the medical and vocational criteria on which its disability determinations are based. Please list the specific steps the agency will take to ensure that updates to these criteria are completed on-time and remain up to date in the future.**

Since FY 2007, we have published eight Final Rules to update medical listings. In that time, we

have also issued 15 Social Security Rulings; while these rulings do not update the criteria, they clarify existing medical evaluation policy on specific impairments. We are completing the development of seven additional final rules based on the public comments from Notices of Proposed Rulemaking. With the completion of these additional rules, we will have made updates in each medical listing body system. To ensure we stay current with changes in medicine, technology, and health care delivery, we continually interact with advocates, medical experts, Federal partners, and others in all of our efforts. Further, we have previously contracted with the National Academy of Sciences, Institute of Medicine (IOM) to inform our work in areas such as the disability evaluation process, cardiovascular impairments, and HIV. We currently contract with the IOM to provide expertise on areas such as mental disorders in children and psychological testing. After our initial updates, we plan to update each listing on a regular cycle.

We are also researching whether changes to our vocational policies may be warranted. We first worked with the Disability Research Consortium to better understand the use of age, education, and work in other disability programs. We are now working with a group of Federal partners and medical, aging, and employment experts for further discussion.

**8. Please describe the Social Security Administration's plans to use technology, such as mobile wage reporting applications, to reduce monthly benefit overpayments in the Disability Insurance program.**

We may become aware of a DI beneficiary's work activity through several methods, including:

- voluntary beneficiary reporting;
- third party reporting; and
- the CDREO, an automated process that matches Internal Revenue Service earnings to our disability rolls to identify unreported earnings for DI beneficiaries.

We use eWork to process work CDRs. eWork is a web-based application that fully automates the initiation, development, adjudication, and effectuation of DI work CDRs. In addition, eWork issues DI and Supplemental Security Income (SSI) work report and paystub receipts, as required by law. By providing automated case processing support, eWork enhances workload control and customer service while helping to decrease improper payments.

Moreover, the President's FY 2016 Budget contains several, SSA-related legislative proposals to help prevent and improve the recovery of improper payments in the DI program, our other programs, and programs across the Federal government:

- **Allow SSA to Use Commercial Databases to Verify Wages in the SSI Program.** The SSI program is means-tested, and the correct benefit amount can vary monthly based on changes in a beneficiary's income, such as wages. SSI recipients are required to report changes in a timely manner, but some do not, which results in improper payments. This

proposal would reduce improper payments and lessen the recipients' reporting burden by authorizing SSA to conduct data matches with private commercial databases and use that information to automatically increase or decrease benefits accordingly, after proper notification. New beneficiaries would be required to consent to allow SSA to access these databases as a condition of benefit receipt. All other current due process and appeal rights would be preserved.

- **Expand Authority to Require Authorization to Verify Financial Information for Overpayment Waiver Requests.** SSA uses an automated process to verify the financial institution accounts of SSI recipients to improve payment accuracy. SSA has the authority to require applicants and beneficiaries to authorize the agency to get this information in connection with determining SSI eligibility. However, SSA cannot use this process for other determinations that involve consideration of financial institution account information. One such determination occurs when a beneficiary requests a waiver of recovery of an overpayment (whether an OASDI overpayment or an SSI one) or a change in the rate at which SSA withholds funds from a beneficiary's payment to collect a prior overpayment. Determining whether someone qualifies for a waiver or a different rate of recovery can involve determining whether the person has the financial means to repay. This proposal would require OASDI recipients seeking overpayment waivers to grant SSA authority to certify financial information and thereby improve the accuracy of waivers. Currently, there is no automated method for verifying financial assets for overpayment waiver claims.
- **Government-Wide Use of Customs and Border Patrol Entry and Exit Data to Prevent Improper Payments.** U.S. Customs and Border Protection (CBP) maintains data on when individuals enter and exit the United States. This entry and exit information may be useful in preventing improper payments in Federal programs that require U.S. residency in order to receive benefits. This proposal would provide for the use of CBP Entry/Exit data to prevent improper payments for OASI, DI, and SSI.
- **Improve Collection of Pension Information from States and Localities.** Current law requires SSA to reduce OASDI benefits when someone also receives a pension based on work that was not covered by Social Security. SSA currently has a matching agreement with the Office of Personnel Management (OPM) to obtain information on Federal government retirees who receive a pension from work not covered by Social Security. However, SSA generally lacks a way to receive similar information from state and local governments. As a result, many of these pensions go unreported, leading to improper payments. This proposal would require state and local government pension payers to report information on pensions paid for non-covered work to SSA through an automated data exchange.
- **Establish Workers' Compensation Information Reporting.** Current law requires SSA to reduce an individual's DI benefit if he or she receives workers' compensation (WC) or public disability benefits (PDB). SSA currently relies upon beneficiaries to report when

they receive these benefits. This proposal would improve program integrity by requiring states, local governments, and private insurers that administer WC and PDB to provide this information to SSA. Furthermore, this proposal would provide for the development and implementation of a system to collect such information from states, local governments, and insurers.

- **Lower Electronic Wage Reporting Threshold to Five Employees.** SSA processes W-2 forms for Treasury. Currently, Treasury requires businesses that file 250 or more W-2s per calendar year to file electronically. This proposal would modify the Internal Revenue Code so that Treasury can require businesses that employ five or more employees to file electronically. This change would be phased-in over three years and would increase the efficiency and accuracy of this process, because electronic returns are completed more rapidly and are generally more accurate than scanned or keyed returns.
- **Move from Annual to Quarterly Wage Reporting.** Employers report wages annually to SSA. However, from 1939 through 1977, SSA received wage reports on a quarterly basis. Increasing the frequency of wage reporting could enhance tax administration. More frequent reporting may improve program integrity by detecting work on the part of DI and SSI recipients more quickly and providing timelier wage data for use by Federal, income-tested programs. This proposal would revert to quarterly wage reporting. The Administration has pledged to work with the States and employers to minimize any burden as employers already report quarterly to the States.
- **Reconcile Office of Personnel Management and Social Security Retroactive Disability Payments.** OPM must reduce disability payments made to Federal Employee Retirement System (FERS) annuitants who receive DI benefits. In many cases, OPM pays the FERS disability benefit before SSA decides whether the person is eligible for DI benefits. This results in FERS overpayments. This proposal would reduce these improper payments by further automating the coordination between SSA and OPM.
- **Eliminate Concurrent Receipt of Unemployment Insurance (UI) and DI Benefits.** This proposal would reduce DI benefits covering the same period in which a beneficiary is also receiving UI benefits, thereby reducing duplicative spending in government programs.

**9. Like disability determination and adjudication decisions, conducting medical continuing disability reviews (CDRs) are critical for ensuring program integrity. Please list the steps that the Social Security Administration will take to balance the competing demands of processing disability claims accurately and on time with eliminating the existing backlogs of initial and appealed claims and continuing disability reviews.**

The level of service we can deliver to the American public depends strongly on the funding we receive from Congress. Adequate funding, as requested in the President's FY 2016 Budget, helps us meet our challenges and enables us to continue to provide service the public expects and deserves. Our ability to complete our important program integrity work–CDRs and SSI

redeterminations –and the level of work we complete is determined by the funding provided to us in our appropriation. Congress also separately authorized the Budget Control Act of 2011 (BCA) that provides us with a dedicated stream of funding that correspondingly determines the amount of program integrity work we complete, but was not fully funded until FY 2014 and FY 2015.

In FY 2015, we will complete 790,000 CDRs and 2.255 million SSI redeterminations. The FY 2016 President's Budget proposes to continue in FY 2016 the discretionary cap adjustment authorized in the BCA, which will allow us to complete 908,000 CDRs and 2.622 million SSI redeterminations next year.

Beginning in FY 2017, the President's Budget proposes to provide a dedicated, dependable source of mandatory funding for SSA to achieve the savings envisioned by the BCA to conduct CDRs and SSI redeterminations. The proposal includes the creation of a new limitation account entitled Program Integrity Administrative Expenses, which will reflect mandatory funding for SSA's program integrity activities.

The dedicated, dependable source of mandatory funding beginning in FY 2017 should eliminate our backlog of around 900,000 CDRs by the end of 2019 and prevent a new backlog from developing during the budget window.

The FY 2016 President's Budget will allow us to continue balancing service and stewardship. I am dedicated to balancing the demands of completing initial disability claims, hearings, and other workloads, and providing the best possible service to the American public.

We strive to balance the important work we do, and our State DDSs have done an incredible job keeping up with incoming disability claims. In fact, the number of disability claims awaiting a DDS decision has decreased steadily since FY 2010 and average processing times remain stable.

The DDSs make the complex medical decisions for both disability claims and CDRs. With more DDS employees in FY 2014, we were able to better balance service and stewardship by increasing the volume of CDRs we completed while maintaining claims work. In FYs 2015 and 2016, we will also be able to balance claims work while continuing to increase CDRs. In addition, we will continue to pursue initiatives that will help us provide fast and accurate service, such as health information technology.

While we are making strides in completing our work at the initial disability level, we must position ourselves to reduce hearing processing times and to reduce the disability appeals backlog. Several years of budget constraints, high levels of hearing requests, and challenges hiring additional ALJs have limited our ability to keep up with hearings requests. As a result, the average wait time and the number of claimants waiting for a hearing decision increased, with over one million people waiting for a disability appeals decision from an ALJ.

Like the DDS work on disability claims, providing due process on disability appeals is also complex and dependent on having a sufficient number of qualified and well-trained decision makers. With the FY 2016 President's Budget, we would plan to continue to hire ALJs and support staff necessary to provide timely, accurate hearing decisions for the large number of people awaiting a hearing decision. With these resources, we would complete a record 829,000 hearings in FY 2016. These resources would also position us in FY 2017 to begin reducing the number of people waiting for a hearing decision and the length of their wait.

Resources alone will not be enough to address our backlogs. We continue to look for ways to both ensure accuracy and improve efficiency in our hearing process. The FY 2016 President's Budget commits increased resources to hire more ALJs. But resources alone will not be enough. The process for hiring SSA ALJs has not operated efficiently as is needed to fill vacancies even when funding is available. Therefore, the Administration created a workgroup led by the Administrative Conference of the United States and OPM, along with SSA, DOJ, and the Office of Management and Budget (OMB) to review the process of hiring ALJs and recommend ways to eliminate roadblocks, which may include proposing administrative reforms or legislative changes.

**10. SSA's ability to appropriately determine who initially qualifies and continues to qualify for DI benefits has the potential to reduce the growth of DI, improve program integrity, and better use scarce resources. What steps is SSA planning or taking to ensure consistent application of SSA guidelines in making disability determinations and adjudication decisions?**

We take the accuracy of our disability determinations seriously, and continually review policy and make changes, as needed, to improve quality of the determination process. Consequently, we employ numerous measures to ensure that State DDS examiners, our ALJs, and other adjudicators apply our program requirements consistently and accurately. For example, we continually develop and disseminate various tools to assist DDSs in processing medical determinations. We also perform pre-effectuation reviews to ensure that DDS determinations are policy compliant. Finally, we continue to develop communication, training, case review/study, and policy strategies to ensure that DDSs maintain a high level of quality in the disability determination process.

**11. The U.S. Government Accountability Office, SSA's Office of the Inspector General, and others have identified limitations in SSA's ability to use its data to prevent or detect patterns that could indicate fraud. Please list the steps that SSA is planning or taking to improve its capacity to track the involvement of physicians, medical providers, and claimant representatives (attorneys and non-attorneys) in the disability determination process.**

We have zero tolerance for fraud; one case of fraud is one case too many. Attachment C

describes our numerous anti-fraud initiatives, including our data analytics efforts.

Moreover, the President's FY 2016 Budget includes a proposal to hold fraud facilitators liable for overpayments. In a few recent cases of fraud against SSA's disability programs, third parties, such as appointed representatives and doctors, facilitated fraudulent applications for benefits by submitting false statements or evidence purporting to show that the individuals were disabled, when in fact they were not disabled. Under current law, such facilitators may be subject to criminal prosecution and penalties, but they are not required to repay the benefits improperly paid to the person who was not eligible for them. This proposal would hold fraud facilitators liable for overpayments by allowing SSA to recover the overpayment, with interest, from a third party if the third party was responsible for making fraudulent statements or providing false evidence that allowed the beneficiary to receive payments that should not have been paid. Furthermore, a facilitator would be ineligible for a waiver of recovery of such an overpayment.

**12. Would the President's budget proposal to transfer a portion of the payroll tax to delay DI trust fund insolvency require a change in law (i.e. an act of Congress)? (Yes or No).**

Yes, congressional action will be necessary to address DI reserve depletion.

**13. People with disabilities experience relatively low rates of employment, and SSA's efforts to increase employment among the DI population have had little success. Please list the steps that SSA is taking to help people with disabilities overcome barriers to employment**

We have a tiered service structure to help people overcome barriers to employment: State Vocational Rehabilitation (VR) programs, Employment Networks (ENs), Work Incentive Planning and Assistance (WIPA) organizations, and Protection and Advocacy for Beneficiaries on Social Security (PABSS) organizations. State VRs and ENs provide job training, job placement, and other employment support to DI or SSI recipients. We pay these organizations only if beneficiaries achieve certain work-related outcomes. Today, over 300,000 of our beneficiaries are receiving services through VRs or ENs. WIPAs are community organizations throughout the country that help beneficiaries understand work incentives available to them and provide employment counseling, job planning, and job preparation for DI and SSI beneficiaries who are ready to try work. PABSS are protection and advocacy organizations in every state and territory funded by SSA to assist beneficiaries overcome specific barriers, such as employment discrimination based on a disability, or to serve as an advocate for the beneficiary in obtaining employment services in the state.

In addition, the DI and SSI programs include a number of employment support provisions commonly referred to as work incentives. Work incentives are intended to provide our beneficiaries with assistance they need to move from benefit dependency to independence. Work incentives, such as the Trial Work Period or continued Medicare coverage, help our beneficiaries enter, re-enter, or stay in the workforce by protecting their eligibility for cash payments, health care, or both until they achieve an employment goal. In an effort to support

our beneficiaries, we are considering simplifying some of our work incentive policies.

We also support a number of studies and demonstrations intended to address the broad needs of beneficiaries with disabilities. This research can support specific program changes or outreach activities targeted to populations in particular need. Current research efforts include: (1) the Benefit Offset National Demonstration to determine whether eliminating the "cash cliff" (which may discourage beneficiaries currently earning below SGA from working above SGA because they do not want to lose all of their DI benefits) encountered by beneficiaries who work would encourage more people to return to work, and (2) Promoting Readiness of Minors in SSI (PROMISE), a collaboration with the Departments of Education, Labor, and Health and Human Services, which seeks to improve outcomes for children and youths who receive SSI by facilitating positive changes in health status, physical and emotional development, completion of education and training and, eventually, employment opportunities.

Moreover, we continue to strengthen our program and test innovative strategies to help people with disabilities remain in the workforce. We are currently exploring potential early intervention options for people with mental impairments between the ages of 18 and 50 that may be at risk of ending up on disability benefits. By providing medical-vocational services prior to benefit receipt in a demonstration, we can test whether such services help individuals with these impairments remain and succeed in school or in the workforce, and perhaps avoid or delay a need for disability benefits. In FY 2015, Congress provided $35 million for such demonstration projects. On May 7, 2015, SSA published a Request for Information to solicit public feedback to inform our development of this demonstration project moving forward. Building on this bipartisan support for early intervention in FY 2015, the FY 2016 President's Budget includes a request for $50 million in research for early intervention demonstrations, as well as a legislative proposal for an additional $350 million for FYs 2017-2020.

**14. To target scarce resources efficiently and effectively, please describe the efforts that SSA is making to improve the administration of the DI program at the case hearing level.**

We are taking a number of steps to improve the hearing level process. For example:

- To help hearing offices with workload issues, we are moving electronic case workloads from under-staffed offices to offices with greater capacity.
- To increase our adjudicatory capacity, we are hiring ALJs, and working with the OPM to identify ways to streamline the hiring process where possible.
- To improve the quality of decisions, we developed data collection tools to capture a significant amount of structured data concerning the application of agency policy in hearing decisions. Using these data sets, we provide feedback and training on workload and decisional quality, giving adjudicators real-time access to data on decisions.

We also continue to enhance the eBB, which is a policy compliant web-based application used to

document, analyze, and adjudicate disability hearing cases in accordance with our regulations. eBB will help us improve the quality, consistency, and timeliness of our disability decisions.

**15. Last year, the payroll taxes that fund the OASI program were insufficient to cover the benefit outlays. If the OASI program does not have enough income from payroll taxes to cover the cost of benefits, please state where the income will come from to pay disability claims under the reallocation. Please state where the income comes from in order to make interest payments.**

The Social Security Act requires that all revenue to the trust funds be invested in interest bearing securities guaranteed as to interest and principal by the full faith and credit of the United States Government. At the end of calendar year (CY) 2014, the OASI Trust Fund held reserves totaling $2.73 trillion, and the reserves are projected to rise to $2.98 trillion by the end of CY 2021. Over this period, interest credited to the OASI Trust Fund will exceed $90 billion each year. The proposed reallocation would reduce the total income to the OASI Trust Fund in each year 2016 through 2020 by less than the amount of interest credited for the year. Interest paid to the OASI, DI, and Medicare Trust Funds comes from the General Fund of the U.S. Treasury, as is the case for all securities issued by the Treasury to government trust funds and to the public.

Social Security cannot sustain projected long-run program costs in full under currently scheduled financing, and legislative changes are necessary to avoid disruptive consequences for beneficiaries and taxpayers. If lawmakers take action sooner rather than later, more options and more time will be available to phase in changes so that the public has adequate time to prepare. Earlier action will also help minimize adverse impacts on vulnerable populations, including lower-income workers and people already dependent on program benefits

**16. Under the existing taxable payroll tax base, please state how much the DI payroll tax would have to rise starting in 2017 in order to balance the trust fund over the next 75 years.**

The FY 2016 President's Budget proposes to address the DI Trust Fund's projected reserve depletion in 2016 by temporarily increasing the DI payroll tax by 0.9 percentage points with a corresponding decrease in the OASI payroll tax for a five-year period to avoid deep and abrupt cuts in benefits for individuals with disabilities. At various points over the course of Social Security's history, Congress has passed reallocation legislation as the need arose for rebalancing revenue from DI to OASI, and vice versa. This proposed reallocation would have no effect on the overall health of the OASI and DI Trust Funds on a combined basis. This adjustment will allow both the OASI and DI Trust Funds to continue to pay full projected benefits for workers until 2033, thereby providing time for the Administration and Congress to consider proposals to improve long-term fiscal sustainability of the Trust Funds.

The Administration has laid out six principles for strengthening Social Security in the long-term,

that should be the basis for any bipartisan reform: (1) Any reform should strengthen Social Security for future generations and restore long-term solvency, (2) The Administration will oppose any measures that privatize or weaken the Social Security system, (3) while all measures to strengthen solvency should be on the table, the Administration will not accept an approach that slashes benefits for future generations, (4) current beneficiaries should **not** see their basic benefits reduced, (5) reform should strengthen retirement security for the most vulnerable, including low-income seniors, and (6) reform should maintain robust disability and survivors' benefits.

While increases in the payroll tax are one option to achieve balance in the combined OASDI trust Fund over the next 75 years, the President has said in the past that he believes in a balanced approach that achieves long-term sustainability while protecting Social Security beneficiaries.

The table we provided in response to your question #3 provides an annual schedule of the increase in the DI payroll tax rate that would be needed to make full payment of scheduled DI benefits throughout the next 75 years, if DI revenues alone were used to achieve this policy goal. These estimates are based on the intermediate assumptions of the 2014 Trustees Report.

**17. Considering the two trust funds together and under the existing taxable payroll tax base, please state how much the payroll tax would need to rise in order to balance the OASI and DI trust funds over the next 75 years.**

The 2014 Trustees Report shows that, under the intermediate assumption, the combined OASDI program has an actuarial deficit of 2.9 percent of taxable payroll over the period 2014 through 2088. The report indicates on page 23 that "For the combined OASI and DI Trust Funds to remain fully solvent throughout the 75-year projection period: (1) revenues would have to increase by an amount equivalent to an immediate and permanent payroll tax rate increase of 2.8 percentage points (from its current level of 12.4 percent to 15.2 percent)".

**18. In addition to your answer to question 1 above, please state the absolute dollar amount of the reallocation over the next ten-year period, 2016 through 2025.**

The table below indicates the amount (in nominal dollars) of the annual payroll tax revenue that would be reallocated from the OASI Trust Fund to the DI Trust Fund. Payroll taxes contributed on earnings in a calendar year are credited to the trust funds with a short lag, and thus a portion of the amount reallocated for each year 2016 through 2020 is credited on a cash basis in the following year.

**Annual Cash-Flow Effects on Net Payroll Tax Credited for Rate Reallocation of 0.9 Percentage Point from OASI to DI for Earnings in Calendar Years 2016-20**

Billions

**Calendar Year** Change in Net Pavroll Tax Credited

| | OASI | DI | OASDI |
|---|---|---|---|
| 2016 | -$56.99 | $56.99 | $0.00 |
| 2017 | -$62.74 | $62.74 | $0.00 |
| 2018 | -$65.80 | $65.80 | $0.00 |
| 2019 | -$68.81 | $68.81 | $0.00 |
| 2020 | -$72.06 | $72.06 | $0.00 |
| 2021 | -$3.61 | $3.61 | $0.00 |
| 2022 | $0.00 | $0.00 | $0.00 |
| 2023 | $0.00 | $0.00 | $0.00 |
| 2024 | $0.00 | $0.00 | $0.00 |
| 2025 | $0.00 | $0.00 | $0.00 |
| Total | -$330.01 | $330.01 | $0.00 |

Based on the assumptions for the President's FY 2016 Budget
Office of the Chief Actuary, Social Security Administration

The President's proposal to address reserve depletion of the DI Trust Fund is a five-year reallocation of payroll taxes from the OASI trust fund to the DI trust fund. This policy would be in effect from January 1, 2016 through December 31, 2020, and would increase the payroll tax allocated to DI by 0.9 percentage points (with a corresponding decrease in OASI). At various points over the course of Social Security's history, Congress has passed reallocation legislation as the need arose for reallocating revenue from DI to OASI, and vice versa. This proposed reallocation would have no effect on the overall health of the OASI and DI Trust Funds on a combined basis. This proposal would make 2033 the year for trust fund reserve depletion for both the OASI and DI Trust Funds, thereby providing time for the Administration and Congress to consider proposals to improve long-term fiscal sustainability of the Trust Funds.

**Senator Jeff Sessions**

**1. During your testimony, you expressed some doubt about whether the Disability Insurance and the Old-Age and Survivors Insurance programs were self-financing or whether additional funds outside of those provided by the dedicated tax revenues would be required to meet scheduled benefit obligations. Determining whether these programs are self-financing is a matter of examining tables and data in the annual report by the programs' trustees. Please provide me with the current projections over the next 75 years of DI and OASI revenues and costs (or outflows). Also provide this same information on a per beneficiary basis, specifically for the average low- income, average-income, and high-income beneficiary.**

It is correct that under the intermediate assumptions of the 2014 Trustees Report, both the OASI and the DI Trust Funds are projected to have insufficient financing scheduled in current law to permit timely payment of all current-law scheduled benefits over the next 75 years. Please find the link to the 2014 Annual report and extensive supporting documentation for the Report at http://www.ssa.gov/oact/TR/2014/index.html.

Actuarial Note 2014.9 at http://www.ssa.gov/oact/NOTES/ran9/index.html provides projections of the level of benefits scheduled under current law as well as the amount of benefits that will be payable if the Congress does not act to avert depletion of trust fund reserves. Benefit levels are provided for several career earnings levels assuming retirement (start of benefit receipt) at 62, 65, and full retirement age.

**Senator Ron Wyden**

**1. Some policy makers suggest that SSDI should be reformed by adding a "short term" or "temporary" program for disabled workers. This is somewhat odd when considering that SSDI is often the last resort for many who apply, as stated by the National Council on Disability:**

***"Receipt of Social Security disability benefits is merely the last stop on a long journey that many people with disabilities make from the point of disability onset to the moment at which disability is so severe that work is not possible. All along this journey, individuals encounter the policies and practices of the other systems involved in disability and employment issues."***

**This quote makes the point that many people on SSDI have been working with a disability for quite some time. They likely interacted with many other programs and supports. There is probably more we can do to support workers with disabilities before they need to apply for SSDI, such as expanding the EITC and Medicaid-Buy In programs. The statistics bear this out: 30 million working age Americans have a disability, but only 8.9 million workers receive SSDI benefits.**

**I also want to make the point that SSA already categorizes SSDI beneficiaries by whether or not medical improvement is expected. This helps target these beneficiaries for review to improve program integrity and save tax payer dollars- if SSA has the resources to conduct the reviews in a timely manner. Please tell me more about how SSA priorities cases for reviews and what resources would be needed for SSA to be current with all scheduled reviews by 2018?**

The law requires us to conduct disability reviews at regular intervals. When a disability case is first approved, we determine when and how often we will conduct a review. We schedule these reviews to occur once every one, three, five, or seven years, based upon several factors, with the predominant one being the likelihood of medical improvement. We also conduct reviews when individuals return to work or if we receive reports of improvement. Currently—due to a history of a lack of sustained and adequate funding—we have a backlog of these reviews.

As indicated in the question, CDRs and SSI redeterminations are highly effective at detecting improper payments and provide an excellent return on the taxpayers' investment—specifically, current estimates indicate that CDRs conducted in 2016 will yield a return on investment (ROI) of about $9 on average in net Federal program savings over 10 years per $1 budgeted for dedicated program integrity funding, including OASDI, SSI, Medicare and Medicaid program effects. Similarly, SSA estimates indicate that non-medical redeterminations conducted in 2016 will yield a ROI of about $4 on average of net Federal program savings over 10 years per $1 budgeted for dedicated program integrity funding, including SSI and Medicaid program effects.

Assuming the enactment of the legislative proposal for mandatory program integrity funding from FY 2017 through FY 2025, which would ensure a dedicated and dependable source of funding, and assuming we receive the full funding levels proposed in the FY 2016 President's Budget, we expect to eliminate the backlog with these reviews by FY 2019. If Congress were to provide us with the full funding proposed by the President's Budget for FY 2016, we would be able to conduct 908,000 CDRs and 2.6 million SSI redeterminations in FY 2016.

Enclosure—Page 19—The Honorable Mike Enzi

**Senator Mark R. Warner**

**1. Social Security Administration (SSA) field offices are currently experiencing a backlog in claim decisions and a severe lag in constituent responsiveness. One office in Virginia answers the phone only 60 percent of the time, with over 200 phone calls per day. It can take 45-60 days to get an appointment at the office, and if a constituent comes in without an appointment, he or she could wait over an hour. At another Virginia office, initial claim decisions take 250-275 days, and if there is an appeal, a constituent could easily wait three years. There is a 35 minute wait time on SSA's automated telephone service.**

**Social Security has announced that effective March 16, 2015, as a result of Congress' approval of the fiscal year 2015 budget, the agency will expand its hours nationwide and offices will be open to the public for an additional hour on Mondays, Tuesdays, Thursdays and Fridays. The Limitation on Administrative Expenses (LAE) is the discretionary amount of money that the SSA has to spend on all administrative expenses. With an increase in LAE funding, SSA could tackle the long wait times at field offices and the delays for getting responses. What type of reduction of wait times do you perceive as a result of the 201 5 budget?**

We thank Congress for our FY 2015 appropriation. With this funding, we are able to restore some service hours to the public and expect to see an improvement in the service we can provide. Effective March 16, 2015, Social Security offices nationwide are open for an additional hour every weekday except Wednesday. For example, a field office that is usually open to the public Monday, Tuesday, Thursday, and Friday from 9 a.m. to 3 p.m. will remain open until 4 p.m.

Our FY 2015 appropriation will allow us to maintain staffing levels in our field offices. Many of our new employees hired in FY 2014 are currently finishing their training and will help the agency address wait times that had steadily increased in prior years.

We also will be able to improve wait times and reduce busy signals on our National 800 Number. We expect that wait times will decrease from over 22 minutes average at the end of February 2014 to less than 12 minutes average by the end of FY 2015. In addition, busy signals will decrease from 14 percent at the end of FY 2014 to 8 percent by the end of FY 2015.

We are increasing our use of Video Service Delivery to help customers who live in remote locations and want face-to-face assistance from an SSA representative. Video service is also an innovative way to help field offices nationwide balance workloads and reduce customer wait times.

To free-up field office employees' time and better serve people who want personal assistance

from an SSA representative, we have redirected most Internet retirement claims to our 16 "Workload Support Units."

Our State DDSs have done an incredible job keeping up with incoming disability claims. In fact, the number of disability claims awaiting a determination has decreased steadily since FY 2010 and average processing times remain stable.

Our FY 2015 appropriation will help fund hiring more ALJs and support staff to help us handle 46,000 more hearings. Our appropriation, along with the FY 2016 President's Budget, will allow us to continue to hire more ALJs and support staff and position ourselves to start reducing hearings processing times in FY 2017.

We continue to look for ways to both ensure accuracy and improve efficiency in our hearing process. The FY 2016 President's Budget commits increased resources to hire more ALJs. But resources alone will not be enough. The process for hiring SSA ALJs has not operated efficiently as is needed to fill vacancies even when funding is available. Therefore, the Administration created a workgroup led by the Administrative Conference of the United States and OPM, along with SSA, DOJ, and OMB to review the process of hiring ALJs and recommend ways to eliminate roadblocks, which may include proposing administrative reforms or legislative changes.

We also note that a return to sequestration would have *significant* and *long-lasting* negative effects on our ability to perform all of our necessary workloads.

**Will the administrative funding be focused on improved IT and process modernization?**

We employ disciplined investment management processes to determine how to use our limited information technology resources. We will strive for a balanced strategy of investing in new and improving existing business applications and infrastructure as funding permits. We will incrementally modernize our applications based on business needs, technical advancement, and risk management.

**2. The Social Security Administration regularly reviews the workloads to even the distribution of claims amount their hearing offices. Service area realignments are made to address workload imbalances. However, I am concerned that the average wait time for all offices is still at unacceptably high levels. Moving forward, how does the SSA plan to reduce the Virginia/regional average of pending days and wait times?**

To reduce the average pending days and wait times in our Virginia hearing offices, we are providing them with workload assistance. In FY 2014, Virginia hearing offices received assistance with a total of 2,960 cases for pre-hearing workup and 876 cases for decision writing. This fiscal year, the Virginia offices have received assistance with 1,424 cases for pre-hearing workup and 488 cases for decision writing.

To further reduce the Virginia and regional average of pending days and wait times, we are hiring additional ALJs. In FY 2015 so far, nine ALJs have been hired for the Philadelphia Region (which includes the Virginia hearing offices), one of whom will report to the Charlottesville, Virginia hearing office in March.

However, we note that a return to sequestration would have *significant* and *long-lasting* negative effects on our ability to perform all of our necessary workloads.

**3. In your written testimony, you note that you were able to increase the number of full medical Continuing Disability Reviews by approximately 15% over fiscal year 2015 and that you plan to complete 908,000 full medical CDRs in 2016.**

**How many full-medical continuing disability reviews are done annually on average, and what was the numerical increase over the past few years? Can you delineate it out?**

**How would a return to sequestration affect the program integrity of SSDI and your ability to conduct CDRs?**

Below is a table that shows the total volume of CDRs we conducted in each of the past 10 years:

| | FY 05 | FY 06 | FY 07 | FY 08 | FY 09 | FY 10 | FY 11 | FY 12 | FY 13 | FY 14 |
|---|---|---|---|---|---|---|---|---|---|---|
| CDRs (in thousands) | 531 | 317 | 190 | 240 | 317 | 325 | 345 | 443 | 429 | 526 |

The number of CDRs we are able to conduct is directly related to the level of funding provided for program integrity activities. We did not receive dedicated program integrity funding in FYs 2003-2008, which resulted in a decline in the number of full medical CDRs we were able to complete in those years. We then received dedicated program integrity funding beginning in FY 2009 and were able to start to ramp up our CDR processing. Subsequently, the BCA authorized a 10-year funding stream for program integrity work from FY 2012 to FY 2021, although Congress only appropriated the full BCA funding levels in FYs 2014 and 2015.

With access to the dedicated program integrity funding authorized in the BCA in FY 2014, we were able to increase our CDR processing by nearly 25 percent. Our FY 2015 appropriation provided us with funding to plan to complete another large increase in CDR processing this year.

The FY 2016 President's Budget request includes funding to process more CDRs in FY 2016 by proposing to continue the discretionary cap adjustment in FY 2016, and proposing a dedicated,

dependable source of mandatory funding to achieve the savings envisioned by the BCA in FY 2017-2025. Also, the Budget proposes funding only the direct costs of CDRs in FY 2016 and beyond.

A return to sequestration would have *significant* and *long-lasting* negative effects on our ability to perform all of our necessary workloads, including the CDR workload.

**Senator Sheldon Whitehouse**

**1. As you know, the payroll tax that funds the Social Security disability and retirement programs is only assessed on income up to a certain level--$118,500 in 201 5. Part of the solvency issue is the explosion in the incomes of the top 1%, which has eroded the overall portion of wages subject to the payroll tax own from 90% in 1982 to 83% today. In fact, there's been so much income growth at the very top that I calculate you could avoid the impending SSDI shortfall by applying the current payroll tax rate (of 12.4%) to wages and investment income exceeding $10 million and devoting this revenue to the DI trust fund. Would you confirm my calculations are correct? How long would the solvency of the DI trust fund be extended by this revenue proposal?**

The IRS Table 1.1 "All Returns: Selected Income and Tax Items, by Size and Accumulated Size of Adjusted Gross Income, Tax Year 2012" found at http://www.irs.gov/pub/irs-soi/12in11si.xls shows 17,685 returns (of all types) with Adjusted Gross Income (AGI) over $10 million, for a total of $546.67 billion of AGI on these returns. The total AGI for these returns in excess of $10 million each is $369.82 billion. If we enacted a 12.4% tax on all such AGI in excess of $10 million per return that would potentially amount to $45.86 billion for 2012. Note that applying this tax would elicit some behavioral response by tax filing units. With the same threshold applied to both single (and married filing separate) and joint returns we would have an added incentive for filing separate in some cases. Therefore the actual realized additional tax revenue for 2012 would be somewhat less than the direct calculation suggests.

In addition, the IRS data indicate that 17,609 of the returns in 2012 with AGI over $10 million had any taxable income. The total taxable income for these returns was $473.46 billion. The total taxable income for these returns in excess of $10 million each is approximately $370 billion. If we enacted a 12.4% tax on all taxable income in excess of $10 million per return that would potentially amount to roughly $37 billion for 2012. Note again that applying this tax would elicit some behavioral response by tax filing units, reducing the amount taxable somewhat.

**2. In your testimony, you stated that if Congress takes no action by the end of next year "we would only be able to pay about 81 percent of scheduled amounts." If Congress indeed fails to act, would you have any discretion in determining how to impose benefit cuts? Would all beneficiaries receive the same percentage cut? Would the cuts vary from month to month?**

In the event that the DI Trust Fund reserve were to become depleted and unable to pay scheduled benefits in full on a timely basis, the Social Security Act does not provide the Commissioner of Social Security any standards regarding how and when to make payments to DI beneficiaries.

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This is why I support the President's proposal to temporarily reallocate a portion of the payroll tax revenue from the OASI to the DI Trust Fund to address the projected DI Trust Fund reserve depletion in 2016.

The President's proposal to address reserve depletion of the DI Trust Fund suggests one approach for rebalancing the Trust Funds. The President's proposal is a five-year reallocation of payroll taxes from the OASI Trust Fund to the DI Trust Fund. This policy would be in effect from January 1, 2016 through December 31, 2020, and would increase the payroll tax allocated to DI by 0.9 percentage points (with a corresponding decrease in OASI). At various points over the course of Social Security's history, Congress has passed reallocation legislation as the need arose for reallocating revenue from DI to OASI, and vice versa. This proposed reallocation would have no effect on the overall health of the OASI and DI Trust Funds on a combined basis.

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**Senator Angus S. King, Jr.**

**1. Reimagining the DI Program. Can you discuss some of the challenges beneficiaries face in returning to work specific to the construction of the DI program?**

As set forth in the Social Security Act, to qualify for DI an individual must be unable to engage in any SGA because of a medically determinable physical or mental impairment that is expected to result in death, or that has lasted or is expected to last for a continuous period of at least 12 months. By definition, this population faces several barriers to returning to work, the most important of which is poor health. Those who receive DI benefits are more than three times as likely to die in a year as other people the same age. Among those who start receiving disability benefits at the age of 55, one in five men and one in seven women die within five years of the onset of their disabilities.

Additionally, many individuals have spent years out of the labor force prior to receiving DI. Research has shown that earnings begin to drop several years before individuals receive DI and that, for many, DI is a program of last resort. Finally, many DI beneficiaries are unaware of, or confused by, the many program rules that allow them to work and incorrectly fear losing their benefits (including Medicare) should they attempt work.

**Does it remain sensible to require applicants to sever all ties to the work and remain out of the labor force for such an extended period of time prior to receiving benefits?**

It is understandable that many individuals would view any work as potentially jeopardizing their eligibility for benefits. However, it is not true that applicants must sever all ties to the work force or remain out of the labor force prior to receiving benefits. The definition of disability, defined above, limits work efforts to an income limit referred to as "Substantial Gainful Activity." SGA is currently $1,090 per month ($1,820 for blind individuals). For context, SGA is about 150 hours of work per month (251 hours if blind) at the federal minimum wage of $7.25 per hour.

**How does the "cash cliff' influence behavior among DI recipients who would like to work?**

The "cash cliff" represents the loss of all benefits that occurs when a beneficiary performs SGA after a nine-month trial work period and a three-month grace period.

It has been suggested that this eligibility cliff discourages beneficiaries currently earning below SGA from working above SGA because they do not want to lose all of their DI benefits. However, a paper published in 2011 in the Social Security Bulletin[2] found that

[2] See *Longitudinal Statistics on Work Activity and Use of Employment Supports for New Social Security Disability*

"parking," or intentionally keeping earnings at a level below SGA in order to avoid loss of benefits, was very uncommon among DI beneficiaries (around 0.2 to 0.4 percent of all DI beneficiaries). We are conducting a demonstration of a gradual reduction in benefits for beneficiaries working above SGA to determine what impact eliminating this cash cliff would have on the percent of beneficiaries returning to work and the potential savings to the DI Trust Fund.

**What changes to the existing requirements for entry to the program or ability to work while on the program would you propose that could create greater incentives for DI beneficiaries to test their work capacity?**

We currently have over a dozen employment supports for DI that allow individuals to test their work capacity. We also have a number of community partners who provide benefits counseling through our WIPA program. Finally, we have requested funding for demonstrations and authority to test additional work incentives and changes to program rules. For many reasons, including those listed in my answer to the first part of your question, it may be more reasonable to expect greater return to work if we reached individuals prior to receiving DI. Our answer to the second part of your second question provides additional information on our early intervention strategies as well as current and requested funding in the President's Budget to support these activities.

**2. <u>Potential for Innovation and Early Intervention.</u> Could you comment on some of the previous projects that the Social Security Administration pursued with its demonstration authority? Did they yield usable results?**

A successful demonstration project is one that yields results policymakers can use. We recently completed three national demonstrations: the Mental Health Treatment Study (MHTS), the Youth Transition Demonstration (YTD) and the Accelerated Benefits (AB) demonstration. Each yielded clear results that inform future program and policy decisions.

The MHTS evaluated the effect that better access to treatment and employment support services would have on outcomes such as medical recovery, functioning, employment, and benefit receipt for DI beneficiaries with a primary impairment of schizophrenia or affective disorder. The study showed higher employment, more work hours, higher wages, fewer hospitalizations, and better quality of life among those who used the MHTS services. However, we found that the MHTS services had no effect on increasing earnings above SGA or on reducing DI benefit payments among beneficiaries. For further information, please read our study reports, which are available at: www.socialsecurity.gov/disabilityresearch/mentalhealth.htm.

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*Insurance Beneficiaries*, *Social Security Bulletin*, Volume 71, Number 3, 2011 at http://www.ssa.gov/policy/docs/ssb/v71n3/.

The YTD provided benefits counseling, social and health services, and other supports to youths with disabilities, aged 14 to 25, to help them successfully transition from school to economic self-sufficiency. The beneficiaries who participated in this demonstration were youth who were receiving (or who were at risk of receiving) disability payments based on their own disability. YTD showed that substantial doses of well-designed services to youth with disabilities can improve key transition outcomes in the medium term but provided mixed evidence on whether YTD's effects on paid employment and earnings are sustainable. Results from the YTD project informed the development of our Promoting Readiness of Minors in SSI (PROMISE) project.

The AB demonstration tested whether providing medical benefits sooner to DI beneficiaries would improve health outcomes and result in less long-term dependency on cash benefits. This demonstration showed that providing rehabilitation and counseling services to newly awarded DI beneficiaries can lead to an increase in health care use, a reduction in unmet medical needs, and improved health; however, the results do not show any effect on short-term mortality. Additional rehabilitative services provided to these beneficiaries led to increased use of employment services and slight increases in employment and earnings levels. For more information on this demonstration, please read our final report, which is available at: www.socialsecurity.gov/disabilityresearch/factsheets/accelerated.htm.

**What kinds of projects would the SSA like to pursue if granted demonstration authority?**

With the funds Congress appropriated in FY 2015, we are focusing on intervening early with individuals not yet receiving Social Security disability benefits. Early interventions may be warranted, in light of research indicating that health problems begin to materialize in advance of complete disability onset, and data showing that earnings begin to decline well before DI benefits are awarded. Limited evidence suggests that intervening before an individual fully detaches from the labor market may be more effective than providing services after disability benefit receipt. The President's FY 2016 Budget proposes a reauthorization of previously existing DI demonstration authority. We would use this authority to test ways to boost employment and support return to work for disability beneficiaries, including through work incentive simplification. Our FY 2016 budget request included the following examples that could be pursued with broader demonstration authority:

(1) We proposed a demonstration that will provide early intervention for individuals with mental illness. We are currently developing this demonstration. The project will identify individuals, as early as possible after onset of mental illness, who may be at risk of becoming long-term DI and SSI recipients. Potential target populations include individuals whose disability application is denied. The project will follow a model similar to that successfully implemented for our MHTS. We will provide each participant with a team of mental health providers and employment specialists, who would coordinate and provide services that would optimize that individual's ability to obtain and retain employment. In FY 2015, Congress provided $35 million in partial

funding for this project. Building on this bipartisan support, we are requesting an additional $50 million in FY 16 to fully conduct it.

(2) We proposed to improve employer incentives to support retention of workers who are injured or develop a disability. The disability management literature suggests that when employers maintain a relationship with employees who are injured on the job and assist them in returning to work, the employers incur lower workers' compensation costs and the employees have better employment outcomes. This demonstration will provide employers an incentive to retain workers with lost-time workers' compensation injuries and illnesses by allowing a reimbursement of their FICA and Medicare taxes paid to returning workers for a period of time.

(3) We proposed to partner with existing State Medicaid Health Home programs to provide wraparound employment services for workers on a path toward SSA disability benefits. Participants would be individuals age 18-50 who receive Health Home services (administered by state Medicaid programs and the Centers for Medicare & Medicaid Services) but do not receive SSI or DI benefits. Health Home participants are Medicaid-eligible individuals who have at least two chronic health conditions including asthma, diabetes, heart disease, obesity, a mental condition, or a substance abuse disorder. We could fund employment services that focus on long-term employment outcomes for some Health Home participants.

**Does the SSA have the administrative capacity to conduct and monitor demonstration projects with appropriate attention and rigor?**

Yes. We design our demonstration projects with scientific rigor, and they have produced clear results relevant for policy discussions. We consider available resources in our design to ensure that we have the capacity to conduct and monitor demonstration projects to maintain that rigor and yield quality outcomes.

**3. Mental Illness and the DI Program. Your written testimony mentions a demonstration project specific to mentally ill beneficiaries. Could you discuss in greater detail the nature of the project and what kinds of lessons were learned from the study?**

The MHTS evaluated the effect that better access to treatment and employment support services would have on outcomes such as medical recovery, functioning, employment, and benefit receipt for DI beneficiaries with a primary impairment of schizophrenia or affective disorder. We examined the advantages and disadvantages of providing these DI beneficiaries access to high quality services designed to improve their employment outcomes. The services included systematic medication management, the services of a nurse-care coordinator to coordinate participants' physical and mental health therapies, and the services of a specialist trained in the individual placement and support model.

Although their earnings did not typically rise above SGA and reduce their DI benefits, the treatment group showed higher employment, worked more hours, earned higher wages, had fewer hospitalizations, and better quality of life than those in the control group. The MHTS addressed the needs of a severely impaired population with a large measure of success and showed that if a similar set of services were deployed with the larger group of all those with mental disabilities, it is likely that we would see similar successes in work and other outcomes.

**What kinds of demonstration projects with this specific population would the SSA like to pursue in the future?**

As mentioned in our answer to the second part of your second question, we are currently developing a demonstration that will provide early intervention for individuals with mental illness. On May 7, 2015, SSA published a Request for Information to inform our development of this demonstration project moving forward. The project would identify individuals, as early as possible after onset of mental illness, who may be at risk of becoming long-term DI and SSI recipients. The project would follow a model similar to that successfully implemented for our MHTS, except applied to individuals *before* they are already on the rolls. We would provide each participant with a team of mental health providers and employment specialists, who would coordinate and provide services that would optimize that individual's ability to obtain and retain employment.

Enclosure - Attachment A - The Honorable Mike Enzi

***Employers and Employees***

| LAW | Time Frame | Trust Fund | Payroll Tax Before | Payroll Tax After | Change, Percent of Payroll |
|---|---|---|---|---|---|
| (Public Law (P.L.) 90-248)-Social Security Amendments of 1967 | 1966 | OASI | 3.5 | 3.5 | 0 |
| | 1967 | OASI | 3.55 | 3.55 | 0 |
| | 1968 | OASI | 3.35 | 3.425 | -0.125 |
| | 1969-70 | OASI | 4.4 | 4.2 | -0.2 |
| | 1971-72 | OASI | 4.4 | 4.6 | 0.2 |
| | 1973+ | OASI | 4.125 | 4.35 | 0.225 |
| | 1966 | DI | 0.35 | 0.35 | 0 |
| | 1967 | DI | 0.35 | 0.35 | 0 |
| | 1968 | DI | 0.35 | 0.475 | 0.125 |
| | 1969-70 | DI | 0.35 | 0.475 | 0.125 |
| | 1971-72 | DI | 0.35 | 0.475 | 0.125 |
| | 1973+ | DI | 0.35 | 0.475 | 0.125 |
| (P.L. 91-172)-Tax Reform Act of 1969 | 1970+ | OASI | 3.725 | 3.65 | -0.075 |
| | 1970+ | DI | 0.475 | 0.55 | 0.075 |
| (P.L. 95-216)- 1977 Amendments to the Social Security Act | 1977 | OASI | 4.375 | 4.375 | 0 |
| | 1978 | OASI | 4.35 | 4.275 | -0.075 |
| | 1979 | OASI | 4.35 | 4.33 | -0.02 |
| | 1980 | OASI | 4.35 | 4.33 | -0.02 |
| | 1981 | OASI | 4.3 | 4.525 | 0.225 |
| | 1982 | OASI | 4.3 | 4.575 | 0.275 |
| | 1983 | OASI | 4.3 | 4.575 | 0.275 |
| | 1984 | OASI | 4.3 | 4.575 | 0.275 |
| | 1985 | OASI | 4.3 | 4.75 | 0.45 |
| | 1986 | OASI | 4.25 | 4.75 | 0.5 |
| | 1987 | OASI | 4.25 | 4.75 | 0.5 |
| | 1988 | OASI | 4.25 | 4.75 | 0.5 |
| | 1989 | OASI | 4.25 | 4.75 | 0.5 |
| | 1990-2010 | OASI | 4.25 | 5.1 | 0.85 |
| | 2011+ | OASI | 5.1 | 5.1 | 0 |
| | 1977 | DI | 0.575 | 0.575 | 0 |
| | 1978 | DI | 0.6 | 0.775 | 0.175 |
| | 1979 | DI | 0.6 | 0.75 | 0.15 |
| | 1980 | DI | 0.6 | 0.75 | 0.15 |
| | 1981 | DI | 0.65 | 0.825 | 0.175 |
| | 1982 | DI | 0.65 | 0.825 | 0.175 |

| | | | | | |
|---|---|---|---|---|---|
| | 1983 | DI | 0.65 | 0.825 | 0.175 |
| | 1984 | DI | 0.65 | 0.825 | 0.175 |
| | 1985 | DI | 0.65 | 0.95 | 0.3 |
| | 1986 | DI | 0.7 | 0.95 | 0.25 |
| | 1987 | DI | 0.7 | 0.95 | 0.25 |
| | 1988 | DI | 0.7 | 0.95 | 0.25 |
| | 1989 | DI | 0.7 | 0.95 | 0.25 |
| | 1990-2010 | DI | 0.7 | 1.1 | 0.4 |
| | 2011 - | DI | 0.85 | 1.1 | 0.25 |
| (P L. 96-403)--Allocation of Social Security Tax Receipts of 1980 | 1980 | OASI | 4.33 | 4.52 | 0.19 |
| | 1981 | OASI | 4.525 | 4.7 | 0.175 |
| | 1980 | DI | 0.75 | 0.56 | -0.19 |
| | 1981 | DI | 0.825 | 0.65 | -0.175 |
| (P L. 98-21) Social Security Amendments of 1983 | 1983 | OASI | 4.575 | 4.775 | 0.2 |
| | 1984 | OASI | 4.575 | 5.2 | 0.625 |
| | 1985 | OASI | 4.75 | 5.2 | 0.45 |
| | 1986-87 | OASI | 4.75 | 5.2 | 0.45 |
| | 1988-89 | OASI | 4.75 | 5.53 | 0.78 |
| | 1990-99 | OASI | 5.1 | 5.6 | 0.5 |
| | 2000+ | OASI | 5.1 | 5.49 | 0.39 |
| | 1983 | DI | 0.825 | 0.625 | -0.2 |
| | 1984 | DI | 0.825 | 0.5 | -0.325 |
| | 1985 | DI | 0.95 | 0.5 | -0.45 |
| | 1986-87 | DI | 0.95 | 0.5 | -0.45 |
| | 1988-89 | DI | 0.95 | 0.53 | -0.42 |
| | 1990-99 | DI | 1.1 | 0.6 | -0.5 |
| | 2000+ | DI | 1.1 | 0.71 | -0.39 |
| (P L. 103-387) The Social Security Domestic Employment Reform Act of 1994 | 1994 | OASI | 5.6 | 5.26 | -0.34 |
| | 1995 | OASI | 5.6 | 5.26 | -0.34 |
| | 1996 | OASI | 5.6 | 5.26 | -0.34 |
| | 1997 | OASI | 5.6 | 5.35 | -0.25 |
| | 1998 | OASI | 5.6 | 5.35 | -0.25 |
| | 1999 | OASI | 5.6 | 5.35 | -0.25 |
| | 2000+ | OASI | 5.49 | 5.3 | -0.19 |
| | 1994 | DI | 0.6 | 0.94 | 0.34 |
| | 1995 | DI | 0.6 | 0.94 | 0.34 |
| | 1996 | DI | 0.6 | 0.94 | 0.34 |
| | 1997 | DI | 0.6 | 0.85 | 0.25 |
| | 1998 | DI | 0.6 | 0.85 | 0.25 |
| | 1999 | DI | 0.6 | 0.85 | 0.25 |
| | 2000+ | DI | 0.71 | 0.9 | 0.19 |

## ***Self Employment***

| Law | Time Frame | Trust Fund | Payroll Tax Before | Payroll Tax After | Change: Percent of Payroll |
|---|---|---|---|---|---|
| (Public Law (P.L.) 90-248)-Social Security Amendments of 1967 | 1966 | OASI | 5.275 | 5.275 | 0 |
| | 1967 | OASI | 5.375 | 5.375 | 0 |
| | 1968 | OASI | 5.375 | 5.1875 | -0.1875 |
| | 1969-70 | OASI | 6.075 | 5.5875 | -0.4875 |
| | 1971-72 | OASI | 6.075 | 6.1875 | 0.1125 |
| | 1973+ | OASI | 6.475 | 6.2875 | -0.1875 |
| | 1966 | DI | 0.525 | 0.525 | 0 |
| | 1967 | DI | 0.525 | 0.525 | 0 |
| | 1968 | DI | 0.525 | 0.7125 | 0.1875 |
| | 1969-70 | DI | 0.525 | 0.7125 | 0.1875 |
| | 1971-72 | DI | 0.525 | 0.7125 | 0.1875 |
| | 1973+ | DI | 0.525 | 0.7125 | 0.1875 |
| (P.L. 91-172)-Tax Reform Act of 1969 | 1970+ | OASI | 5.5875 | 5.475 | -0.1125 |
| | 1970+ | DI | 0.7125 | 0.825 | 0.1125 |
| (P.L. 95-216)- 1977 Amendments to the Social Security Act | 1977 | OASI | 6.185 | 6.185 | 0 |
| | 1978 | OASI | 6.15 | 6.01 | -0.14 |
| | 1979 | OASI | 6.15 | 6.01 | -0.14 |
| | 1980 | OASI | 6.15 | 6.01 | -0.14 |
| | 1981 | OASI | 6.08 | 6.7625 | 0.6825 |
| | 1982 | OASI | 6.08 | 6.8125 | 0.7325 |
| | 1983 | OASI | 6.08 | 6.8125 | 0.7325 |
| | 1984 | OASI | 6.08 | 6.8125 | 0.7325 |
| | 1985 | OASI | 6.08 | 7.125 | 1.045 |
| | 1986 | OASI | 6.01 | 7.125 | 1.115 |
| | 1987 | OASI | 6.01 | 7.125 | 1.115 |
| | 1988 | OASI | 6.01 | 7.125 | 1.115 |
| | 1989 | OASI | 6.01 | 7.125 | 1.115 |
| | 1990-2010 | OASI | 6.01 | 7.65 | 1.64 |
| | 2011+ | OASI | 6 | 7.65 | 1.65 |
| | 1977 | DI | 0.815 | 0.815 | 0 |
| | 1978 | DI | 0.85 | 1.09 | 0.24 |
| | 1979 | DI | 0.85 | 1.04 | 0.19 |
| | 1980 | DI | 0.85 | 1.04 | 0.19 |

| | | | | | |
|---|---|---|---|---|---|
| | 1981 | DI | 0.92 | 1.2375 | 0.3175 |
| | 1982 | DI | 0.92 | 1.2375 | 0.3175 |
| | 1983 | DI | 0.92 | 1.2375 | 0.3175 |
| | 1984 | DI | 0.92 | 1.2375 | 0.3175 |
| | 1985 | DI | 0.92 | 1.425 | 0.505 |
| | 1986 | DI | 0.99 | 1.425 | 0.435 |
| | 1987 | DI | 0.99 | 1.425 | 0.435 |
| | 1988 | DI | 0.99 | 1.425 | 0.435 |
| | 1989 | DI | 0.99 | 1.425 | 0.435 |
| | 1990-2010 | DI | 0.99 | 1.65 | 0.66 |
| | 2011+ | DI | 1 | 1.65 | 0.65 |
| (P.L. 96-403)--Allocation of Social Security Tax Receipts of 1980 | 1980 | OASI | 6.64 | 6.2725 | 0.2625 |
| | 1981 | OASI | 6.7625 | 7.025 | 0.2625 |
| | 1980 | DI | 1.04 | 0.7775 | -0.2625 |
| | 1981 | DI | 1.2375 | 0.975 | -0.2625 |
| (P.L. 98-21) Social Security Amendments of 1983 | 1983 | OASI | 6.8125 | 7.1125 | 0.3 |
| | 1984 | OASI | 6.8125 | 10.4 | 3.5875 |
| | 1985 | OASI | 7.125 | 10.4 | 3.275 |
| | 1986-87 | OASI | 7.125 | 10.4 | 3.275 |
| | 1988-89 | OASI | 7.125 | 11.06 | 3.935 |
| | 1990-99 | OASI | 7.65 | 11.2 | 3.55 |
| | 2000+ | OASI | 7.65 | 10.98 | 3.33 |
| | 1983 | DI | 1.2375 | 0.9375 | -0.3 |
| | 1984 | DI | 1.2375 | 1 | +0.2375 |
| | 1985 | DI | 1.425 | 1 | -0.425 |
| | 1986-87 | DI | 1.425 | 1 | +0.425 |
| | 1988-89 | DI | 1.425 | 1.06 | -0.365 |
| | 1990-99 | DI | 1.65 | 1.2 | -0.45 |
| | 2000+ | DI | 1.65 | 1.42 | -0.23 |
| (P.L. 103-387) The Social Security Domestic Employment Reform Act of 1994 | 1994 | OASI | 11.2 | 10.52 | -0.68 |
| | 1995 | OASI | 11.2 | 10.52 | -0.68 |
| | 1996 | OASI | 11.2 | 10.52 | -0.68 |
| | 1997 | OASI | 11.2 | 10.7 | -0.5 |
| | 1998 | OASI | 11.2 | 10.7 | -0.5 |
| | 1999 | OASI | 11.2 | 10.7 | -0.5 |
| | 2000+ | OASI | 10.98 | 10.6 | -0.38 |
| | 1994 | DI | 1.2 | 1.88 | 0.68 |
| | 1995 | DI | 1.2 | 1.88 | 0.68 |
| | 1996 | DI | 1.2 | 1.88 | 0.68 |
| | 1997 | DI | 1.2 | 1.7 | 0.5 |
| | 1998 | DI | 1.2 | 1.7 | 0.5 |
| | 1999 | DI | 1.2 | 1.7 | 0.5 |
| | 2000+ | DI | 1.42 | 1.8 | 0.38 |

Enclosure—Attachment B—The Honorable Mike Enzi

| Law | Section | Provision Description |
|---|---|---|
| **Social Security Amendments of 1967 (Public Law 90-248)** | | |
| | 101 | Increased Old-Age, Survivors, and Disability Insurance (OASDI) benefits. |
| | 102 | Increased benefits for certain individuals age 72 and older. |
| | 115 | Changed coverage under the OASDI program for ministers, members of a religious order, and others. |
| **Tax Reform Act of 1969 (Public Law 91-172)** | | |
| | 1001 | Increased OASDI benefits. |
| | 1002 | Increased benefits for certain individuals age 72 and older. |
| | 1004 | Set maximum amount of a wife's or husband's insurance benefit. |
| **Security Amendments of 1977 (Public Law 95-216)** | | |
| | 201 | Changed how the "primary insurance amount" is computed. |
| | 202 | Changed the maximum amount of benefits a family could receive. |
| | 203 | Increased the value of "delayed retirement credits." |
| | 301 | Increased earnings test for individuals age 65 and older. |
| | 317 | Allowed international agreements (totalization) with respect to Social Security benefits. |
| | 335 | Substantial gainful activity in the case of blind individuals--disabled blind person is not considered to have engaged in substantial gainful activity (SGA) that would result in termination of benefits unless the earnings exceeded an amount equal to the monthly earnings measure of retirement for those age 65 or older. |
| **Allocation of Social Security Tax Receipts of 1980 (Public Law 96-403)** | | |
| | [1] | Reallocated payroll tax receipts to the OASI fund for a short period of time (**law contained no program changes**). |
| **Social** | | |

Enclosure—Attachment B—The Honorable Mike Enzi

| Law | Section | Provision Description |
|---|---|---|
| **Security Amendments of 1983 (Public Law 98-21)** | | |
| | 101 | Expanded mandatory coverage to newly hired federal workers. |
| | 114 | Changed the value of delayed retirement credits. |
| | 121 | Permitted the Secretary of Treasury to disclose tax return information to SSA for the purpose of withholding alien tax.<br><br>Appropriated any revenues generated under this title to the TFs. |
| | 131 | Permitted the payment of OASDI benefits to the following:<br>• surviving divorced spouses who remarry after age 60,<br>• disabled widow(er)s who remarry after age 50, and<br>• disabled surviving divorced wives who remarry after age 50. |
| | 132 | Provided benefits to divorced spouses without regard to their ex-spouse's entitlement to benefits. |
| **The Social Security Domestic Employment Reform Act of 1994 (Public Law 103-387)** | | |
| | 5 | Prohibited payment of benefits to certain other types of incarcerated individuals. |
| | 6 | Authorized SSA to use certain procedures to collect delinquent debt. |

Enclosure—Attachment C—The Honorable Mike Enzi

## Social Security Administration's Anti-Fraud Activities (for Fiscal Year 2014)

### 1. Increase Continuing Disability Reviews (CDR)

Background/Objective: While the primary purpose of a CDR is to determine whether a beneficiary is no longer entitled to benefits because his or her condition has medically improved, our ability to perform significantly more CDRs may allow us to detect increased numbers of potentially fraudulent or suspicious activities.

Metrics to Measure: Number of medical CDRs processed and if we meet our processed goal.

### 2. Expand Cooperative Disability Investigations (CDI) Units

Background/Objective: Working with our OIG, we plan to expand the number of CDI units. According to OIG, CDI units have contributed to agency savings of more than $960 million over the last three fiscal years. We provide most of the funding for these units, and in collaboration with OIG, we expanded the CDI program by seven additional units beginning in FY 2014. We anticipate these 7 units will be fully operational in FY 2015, increasing the total number of units from 25 to 32 nationwide.

Metrics to Measure: The number of new CDI units implemented in FY 2015, with five additional units as the goal. Agency savings because of the CDI units.

### 3. Anti-Fraud Training

Background/Objective: We expanded anti-fraud training to all Social Security Administration (SSA) employees during FY 2014, with specific focus on lessons learned from Puerto Rico and New York City. SSA and state disability determination services (DDS) front-line employees remain our best line of defense against those seeking to cheat the system.

Metrics to Measure: Percentage of employees trained.

### 4. Data Analytics

Background/Objective: We undertook a special initiative to use data analytics to enhance our fraud detection efforts. Specifically, we created analytical models based on known cases of fraud and past allegations to identify common characteristics and patterns. We will utilize predictive analytical models to help us uncover potential fraud or other suspicious behavior when we review initial applications or existing data on beneficiaries. We invited OIG to participate in this initiative.

Metric to Measure: To be determined. We continue to work on building predictive analytical models that will be useful in our antifraud efforts.

**5. Fraud Prevention Units (FPU)**

Background/Objective: We are establishing FPUs composed of disability examiners dedicated to reviewing and acting on potential fraud cases. We will compile data from the cases that will help us develop further analytical tools to identify potential fraud.

Metrics to Measure: We established FPUs specifically to target disability fraud through third-party facilitators. This effort utilizes programmatic expertise to provide quality case analysis and support to OIG's Office of Investigations. The units also conduct the disability redeterminations that result from the successful conclusion of the investigation.

We have allotted resources to ensure FPUs maintain peak efficiency while also providing valuable programmatic support to anti-fraud initiatives in the disability program. Our process addresses how cases are directed to the FPUs and how we will leverage the appropriate expertise to perform the work assigned.

**6. National Anti-Fraud Committee (NAFC)**

Background/Objective: On April 3, 2014, our Acting Commissioner approved and signed the charter reinstituting the NAFC, co-chaired by the Inspector General (IG) and our DCBFQM. The NAFC's mission is to support national and regional strategies to combat fraud, waste, and abuse.

The NAFC supports our goal to provide accountable stewardship to taxpayers by ensuring superior financial performance, budget management, and integrity in all payments, records, and processes. In addition, the NAFC will serve as an advisory board for the newly established Office of Anti-Fraud Program Management.

The NAFC is actively monitoring and receiving updates on many of the agency's anti-fraud initiatives.

Metrics to Measure: Meeting frequency and content. The NAFC's mission is to support national and regional strategies to combat fraud, waste, and abuse. At the first full NAFC meeting the NAFC identified component leads for 11 major anti-fraud initiatives to monitor throughout the year. Designated component leads have been providing regular updates on our anti-fraud initiatives to the NAFC; however, the Office of Anti-Fraud Program Management will now lead and track the progress of the anti-fraud initiatives.

Combatting fraud is an ongoing process. It is imperative that we remain on the forefront of technology to prevent and deter fraud, and not just detect fraud that has already occurred. The NAFC will serve as an advisory board for the Office of Anti-Fraud Program Management in re-evaluating best practices, new techniques to detect and prevent fraud, and initiatives to monitor.

**7. Submission of Evidence Regulation**

Background/Objective: Concerns have been raised that some claimants may withhold medical evidence that could be unfavorable to their claims. We propose to revise our regulations to require claimants to inform us about or submit all evidence known to them that relates to their disability claim — both favorable and unfavorable. We also propose to require a representative to help the claimant obtain the information or evidence that the claimant must submit, and we would extend the protections afforded by attorney-client privilege and attorney work product to non-attorney representatives as well.

Metrics to Measure: Issuance of the final regulation. (Rule published March 20, 2015, with an effective date of April 20, 2015.)

**8. Fraud Prosecution Project**

Background/Objective: The Department of Justice (DOJ) is the Federal agency responsible for prosecuting defendants who have violated Federal law. However, due in part to a lack of prosecutorial resources, DOJ declines many cases for prosecution. For more than a decade, our OGC has worked with OIG to develop the SSA Fraud Prosecution Project. The goal of this initiative is to increase the number of prosecutions for crimes involving Social Security matters. To support this project, OGC has provided attorneys to serve as Special Assistant United States Attorneys (fraud prosecutors) in many of the Federal districts where we have regional offices and at headquarters.

Metrics to Measure: Attorneys hired by date.

**9. Representative Payee Criminal Bar**

Background/Objective: We seek only qualified individuals and organizations to serve as representative payees, and we take steps to ensure their continued qualification and the proper use of benefits. We have completed a pilot of a policy change that we believe will help us identify payee applicants who have committed certain serious crimes and bar them from serving as payees. Felony convictions for any of 12 crimes will bar the individuals from serving as a representative payee.

Metrics to Measure: Number of barred payee applicants.

**10. Symptom Evaluation Research Effort**

Background/Objective: Our objective in entering into a contract with the Administrative Conference of the United States (ACUS) was to commission a study of the Social Security Act, our current regulations and sub-regulatory policy, and our development and documentation practices regarding how our adjudicators at all levels evaluate claimants' symptoms, including pain, in adjudication of social security disability claims. We also tasked ACUS with reviewing appropriate Federal court case law involving claimant's symptom evaluation. Upon the

conclusion of its research and review of our data, ACUS will issue a final report with recommendations concerning potential improvements in our sub-regulatory policies and, if necessary, regulatory standards to more clearly articulate the scope of symptom evaluation in the adjudication of disability claims.

Metrics to Measure: The requirements of the interagency agreement between ACUS and SSA serve as the metrics for this initiative.

**11. Psychological Testing Research Effort**

Background/Objective: We have asked the Institute of Medicine (IOM) to perform a comprehensive review of psychological testing, including symptom validity testing. IOM will examine the relevance of psychological testing to disability determinations in claims involving physical or mental disorders. IOM will also provide us guidance to help adjudicators interpret the results of psychological testing.

Metrics to Measure: The IOM report will determine our next steps in this area and the timeline for implementation.

**13. Administrative Sanctions**

Background/Objective: We implemented a new, streamlined process for imposing administrative sanctions that will facilitate national consistency and focus agency resources on the most egregious cases that OIG is unable to pursue for a fraud conviction or civil monetary penalty.

Metrics to Measure: Number of sanctions imposed.

**14. Anti-Fraud Communications Campaign (AFCC)**

Background/Objective: We plan to carry out the AFCC in FY 2015. The end date of the campaign is undecided at this time because it is premature to set an end date until we develop the variables of the AFCC with input from agency stakeholders. As with any good communications plan, the anti-fraud communications plan will be based on our overall agency strategic plan. As the strategic plan evolves, we will adjust the communications strategy.

Metrics to Measure: We will track visits to and use of materials from a dedicated campaign website.

**15. Anti-Fraud Language on Notices**

Background/Objective: To help communicate our anti-fraud message, we are adding new anti-fraud language to our notices.

Metrics to Measure: Number of notices revised.

**16. Case Review - New York and Puerto Rico Fraud**

Background/Objective: We immediately suspended benefits to the indicted beneficiaries and initiated reviews (redeterminations) of thousands of other beneficiaries whose cases included tainted information from the indicted medical providers. Immediately after the arrests, we added staff to our Northeastern Program Center Disability Processing Branch and the New Jersey Disability Determination Service to conduct these reviews. During these reviews, our staff disregards medical evidence received from an indicted or discredited source. If the remaining evidence does not support the original allowance, we provide the beneficiary the opportunity to submit additional medical evidence before making a final determination regarding whether to terminate benefits. Over the past few months, our staff has been reviewing approximately 7,400 cases in which the indicted doctors supplied medical evidence. We are monitoring these cases to ensure accurate and consistent processing.

The objective of this initiative is to terminate benefits if non-tainted medical evidence in the case record does not support the original allowance.

Metrics to Measure: The metrics we are using to measure our objectives include the number of redeterminations pending and completed; the number of reconsiderations filed; and the number of reconsiderations pending and completed.

**17. Impose Civil Monetary Penalties (CMP)**

Background/Objective: After a comprehensive evaluation of the CMP program by OIG in 2011, we instituted several changes to make the program more efficient and effective. We believe this streamlined program deters potential fraudsters.

Metrics to Measure: The CMP program does not have metrics.

**18. Quality Review - Field Office Adjudications**

Background/Objective: We have a review process called the Continuous Quality Area Director (CQ AD) Review Process. This review ensures the accuracy of work completed by field office technicians. One of the primary areas for review is the front-end disability accuracy in field offices, with a concentration on the accuracy of how we determine the applicant's disability onset date. We use the results of these focused reviews to identify systemic issues; recommend training, policy, and systems enhancements; and provide direct feedback to employees regarding their compliance with existing policy.

While the primary purpose of quality reviews is to ensure a high level of decisional accuracy, they can also detect potential fraud.

Metrics to Measure: Number of cases reviewed requiring corrective actions.

**19. eServices Fraud Prevention**

Background/Objective: To improve fraud prevention and detection, we will use automated tools to help identify and track suspicious or potentially fraudulent eService transactions (e.g., direct deposit, claims submittals) and take appropriate preventive and corrective actions.

Our Direct Deposit Fraud Prevention initiative consists of a series of business processes and system releases designed to prevent, detect, track, and recover fraudulently redirected benefit payments.

Metrics to Measure: DCO will use the fraudulent account creation rate as a metric for eServices fraud prevention effectiveness. For the Direct Deposit Fraud Prevention initiative, the specific metrics are as follows:

*Blocking of Problematic RTNs*

Through the monitoring of rejected transactions, tracking the number of attempts made on the blocked RTNs to determine the approximate value of the loss prevented.

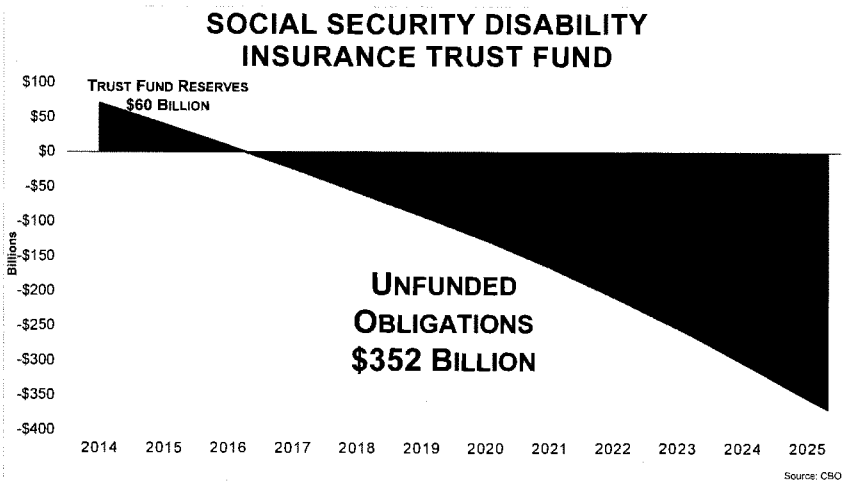
*Development of Potential Fraud Non-Receipt Database*
Comparison of claims of non-receipt due to potential fraud vs. funds recovered from financial institutions reflected as a percent.

*Development of a New Reclamation Process*

Comparison of claims of non-receipt due to potential fraud vs. funds recovered from financial institutions reflected as a percent.

*Recovery of Fraudulent iClaim Payments*

Comparison of fraudulent iClaim value vs. funds recovered from financial institutions reflected as a percent. The iClaim value is equal to the first payment once an internet application for benefits has been approved. Often this payment covers a number of previous months; therefore, it is greater than the normal monthly payment.


SOCIAL SECURITY DISABILITY
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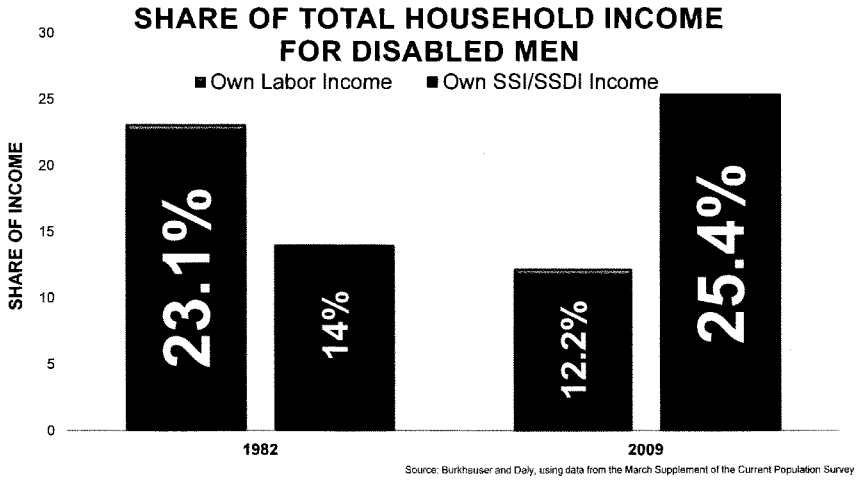
SHARE OF TOTAL HOUSEHOLD INCOME
FOR DISABLED MEN
Own Labor Income
Own SSI/SSDI Income
SHARE OF INCOME
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15
10
5
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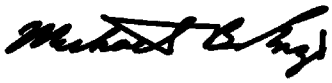
23.1%
14%
12.2%
25.4%
1982
2009
Source: Burkhauser and Daly, using data from the March Supplement of the Current Population Survey



# FOR THE RECORD

**Statement**
**on**
**"The Coming Crisis: Social Security Disability Trust Fund Insolvency"**

**America's Health Insurance Plans**
**601 Pennsylvania Avenue, NW**
**South Building, Suite 500**
**Washington, DC 20004**

**Submitted to the**
**Senate Budget Committee**

**February 11, 2015**

## I. Introduction

AHIP is the national association representing health insurance plans that provide health and supplemental benefits to more than 200 million Americans. Our members offer a broad range of products, including private disability income protection that replaces lost income in the event that a disabling condition forces a covered worker to leave the workforce for an extended period of time.

As Members of this Committee know, the Social Security Board of Trustees has projected that the Disability Insurance (DI) Trust Fund, from which Social Security Disability Insurance (SSDI) benefits are paid, will deplete its assets late next year. Our member insurers that provide disability income protection coverage are doing their best to anticipate and prepare for a potential disruption of scheduled SSDI benefit payments – to minimize the confusion, fear, and financial hardship that a drop in SSDI benefits would bring about in financially vulnerable households because private income protection benefits are typically integrated with SSDI benefits.

We appreciate the Committee's interest in exploring solutions to the financial challenges facing the SSDI program. Our members have demonstrated strong leadership in developing innovative programs to meet the needs of disabled workers, including strategies and services to support them in their efforts to return to work and lead productive lives. This emphasis on return-to-work is a particularly important component of the protection offered by private disability income insurers. By helping people overcome their disabilities and return to the workforce, based on consultation with their health care providers, insurers are enabling working Americans they cover to improve both their financial situation and their quality of life. We believe our members' experience in pioneering these initiatives offers valuable lessons for Congress as you consider legislative options for strengthening the financial stability of SSDI. We also believe that savings to the SSDI program, and other federal programs, arising out of private disability income protection suggest that policies to extend income protection to a greater number of working Americans would serve the public interest.

To contribute to the dialogue at today's hearing, our statement focuses on:

- an overview of private disability income protection coverage;
- examples of successful return-to-work strategies used by our member companies;
- analyses of federal savings arising out of private disability income protection;
- the findings of a survey of disability insurer return-to-work practices; and
- the value this coverage offers to policyholders.

## II. Overview of Disability Income Protection Coverage

Private disability income protection provides tens of millions of Americans with coverage that complements the safety net provided by the SSDI program. Approximately 39 percent of U.S. workers in private industry are covered by employer-sponsored short-term disability coverage, while 32 percent receive long-term disability insurance through their employers.[1] This coverage provides a level of disability income that spares many Americans from financial hardship.

Private short-term disability coverage typically pays benefits for 13 to 26 weeks based on a specified percentage of the employee's pre-disability income – typically 60 percent – after sick leave has been exhausted. Circumstances that may trigger the payment of short-term disability benefits include temporary musculoskeletal or connective tissue conditions, pregnancies, and other illnesses or conditions that are resolved within a relatively short timeframe, often allowing the employee to return to work before benefits are exhausted.

The valuable protection offered by short-term disability coverage can be purchased at a reasonable price – an average of $210 annually when purchased as group coverage by employers.[2] This short-term protection can be purchased in combination with long-term disability coverage as part of a seamless package, with the short-term and long-term benefits coordinated to ensure that disabled workers can meet their daily expenses and avoid financial hardship. Long-term disability benefits continue anywhere from five years to the remainder of an individual's life. Long-term disability insurance allows workers to sustain themselves financially if an illness, injury, or disability takes them out of the workplace for an extended period of time. In 2010, the average annual group premium for long-term disability coverage was $245 per covered employee.[2]

## III. Return-to-Work Strategies by Private Disability Insurers

In addition to replacing lost income for claimants in a timely fashion, private disability income insurers have been very proactive in developing return-to-work programs that help disabled workers move forward when they are prepared to reclaim their financial self-sufficiency. This can be an invaluable tool in helping to maintain the productivity of America's businesses. This

[1] U.S. Department of Labor, Bureau of Labor Statistics, *National Compensation Survey: Employee Benefits in the United States,* March 2013
[2] GenRe, *2010 U.S. Group Disability Market Survey Summary Report*, July 2011

role has become more important with the growing impact of employees with chronic diseases, downsizing by employers during the economic downturn, and baby boomers delaying retirement.

A 2010 AHIP report[3], based on interviews with experts at our member companies, describes trends and innovations in the disability income insurance industry. This report reviews a range of successful return-to-work strategies being used by private disability insurers. Several examples are highlighted below.

**Assisting Cancer Patients and Survivors**

Cancer accounts for a large share of long-term disability claims. Most cancer patients ultimately return to work, and it is becoming increasingly common for cancer patients to continue working while they undergo treatment. Employees who remain at work during cancer treatment or return to work after treatment can face fatigue, difficulties with memory and concentration, pain, and even post-traumatic stress. Strategies for supporting employees facing these challenges include allowing time and space for breaks, planning work schedules to avoid the worst times for pain and fatigue, and creating check lists for job tasks to help deal with temporary memory loss. Insurers work with employers to help them anticipate potential difficulties and work around them.

**Modifying Work Environments to Address Functional Limitations**

Musculoskeletal conditions, such as arthritis, are increasingly a factor in the workplace as the U.S. workforce gets collectively older. Workers with these conditions often have difficulties with strength and range of motion that can make it difficult for them to remain in the same job. Insurers work with employers to find successful ways to modify job responsibilities and workstations to allow workers to overcome physical limits associated with arthritis and other musculoskeletal conditions.

**Facilitating Part-Time Work**

In some cases, an employee may be able to continue carrying out the duties of his or her job, but may have limitations that prevent him or her from working effectively on a full-time basis. Such limitations might be most common for older workers. Disability insurers help employers and employees develop flexible part-time schedules that are suited to the needs and preferences of the affected employee.

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[3] AHIP Center for Policy and Research, *Trends and Innovations in Disability Income Insurance*, January 2010

**Enhancing Support for Workers on Long-Term Disability**
Disability insurers typically seek first to help disabled employees return to their previous job with their current employer. When an employee cannot return to his or her previous job or employer, insurers can help the employee prepare for and find another job, begin a new career, or start a business. Insurers provide vocational counseling and help with resume writing, networking, and interviewing. Counselors also help participants identify job goals and potential employers, identify gaps in skills, and access needed training and education.

**Integrating Health and Disability Support Services**
A number of companies that offer both health care and disability insurance support services are integrating and coordinating these services to ensure that workers receive the most effective care for their chronic conditions and can return to work as soon as possible. This approach recognizes the value of addressing all of an individual's medical, social service, and behavioral health needs in a coordinated way, rather than in separate silos.

One company, for example, has established a program through which enrollees who have both health and disability coverage can work with nurse case managers who act as health advocates. Case managers help workers navigate the health care system and access the health care, disease management, and disability-related services they need. When employees feel ready to return to work, vocational rehabilitation counselors coordinate with employers to develop return-to-work plans suited to the employees' needs and abilities. Such plans often include modified work schedules that help employees transition gradually from part-time to full-time work, use of ergonomic work stations and chairs, and changes to physical requirements (such as eliminating heavy lifting).

Another company with an integrated health and disability program makes it possible, with the consent of employees, for health and disability team members to share information about the employees' health and functional status on a real-time basis so they can return to work as soon as possible. This program also includes a role for case managers in consulting with physicians about including return-to-work considerations in patients' treatment plans.

## IV. Federal Savings Arising Out of Private Income Protection Coverage

Private insurer disability management and return to work (RTW) efforts have also been shown to have a positive impact on the SSDI program by putting ill or injured workers on a path that leads

them away from the SSDI program rolls – or shortens the time that they received SSDI benefits. A 2013 analysis carried out by Charles River Associates estimated that private insurers' disability management and return-to-work interventions save the federal government $25 billion over a ten-year period. Almost half of these savings accrue to the SSDI program. The remaining savings arise when ill or injured workers leave the rolls of public programs such as Medicare, Medicaid, and the Special Nutrition Assistance Program (SNAP) when they return to work.[4]

An earlier Charles River analysis indicated that the receipt of private disability income protection benefits lifts up to 575,000 American families out of poverty each year and saves the nation's taxpayers up to $4.5 billion annually by reducing dependence on the Temporary Assistance for Needy Families (TANF) program and SNAP.[5]

Because of the positive fiscal impact of private income protection on SSDI and other federal programs, AHIP and its disability income protection insurer members believe that we have common ground with stakeholders who favor reductions in federal spending and also those who are working to restore the solvency of the SSDI program. Federal policies that would help expand private income protection – and the return-to-work assistance that private coverage makes available – would benefit taxpayers and SSDI beneficiaries, as well as working Americans and employers. Specifically, we believe that the federal government could play a key role in helping to educate and empower working Americans and employers regarding disability income security issues and best return-to-work practices. We also believe that the automatic-enrollment provisions of the Pension Protection Act of 2006 could serve as a model for parallel provisions to extend disability income protection to many more working Americans.

## V. Survey of Disability Insurer Return-to-Work Practices

Additional information about the return-to-work strategies of private disability insurers is revealed by a survey conducted by Milliman, Inc.

The Milliman survey highlights the investments of private disability insurance carriers in rehabilitation and return-to-work efforts, identifies key industry practices that support these initiatives, and highlights the factors that are most crucial to the success of return-to-work

[4] Charles River Associates, *Private Disability Insurance and Return-to-Work: Cost Savings to SSDI and Other Federal Programs*, September 2013

[5] Charles River Associates, *Financial Security for Working Americans: An Economic Analysis of Insurance Products in Workplace Benefits Programs*, July 2011

strategies.[6] For insurers taking part in the survey, return-to-work closures represented 29 percent of all claim closures and 42 percent of all closures (excluding claims closed due to death or at the end of the maximum benefit period).

The following are several key findings of this survey:

- Private disability insurers make significant investments in returning disabled workers to productivity. On average, participating long-term disability (LTD) insurers spent $3,200 on each disabled employee receiving rehabilitation and return-to-work services. The range of disability insurer investment extended as high as $7,600 per return-to-work client.

- Rehabilitation and return-to-work programs offer a wide range of services to disabled employees, including:
    - Medical case management,
    - Vocational and employment assessment,
    - Worksite modification,
    - Purchasing adaptive equipment,
    - Business and financial planning,
    - Retraining for a new occupation, and
    - Education expenses.

- A number of provisions in disability insurance policies play a role in supporting claimant rehabilitation and return-to-work. These provisions include:
    - Work incentive benefits,
    - Rehabilitation benefits,
    - Workplace accommodation benefits, and
    - Child or dependent care benefits during rehabilitation.

- The employer's willingness to participate in a disabled employee's rehabilitation plan is a crucial factor in achieving a successful return to work.

[6] Milliman, Inc., *Survey of Rehabilitation and Return-to-Work Practices Among U.S. Disability Carriers*, May 2007

## VI. Value for Consumers

Recent surveys clearly show the value of private income protection to working Americans. A survey of group disability insurers comprising approximately 75 percent of the commercial disability insurance marketplace indicates that approximately 653,000 individuals received long-term disability payments in 2013 from private insurers participating in the survey. Participating insurers paid a total of $9.8 billion in long-term disability benefits that year. Twenty-eight percent of these claimants receiving private disability income benefits were not receiving SSDI benefits. Moreover, more than 95 percent of reported disabilities were not work-related and, therefore, not eligible for benefits under workers compensation.[7]

A 2008 Harris Interactive survey, published by AHIP, reveals that a large majority of disability insurance claimants are satisfied with their coverage and their experience filing a claim and receiving benefits. Overall, four out of five claimants (82 percent) said that they were satisfied with their disability income insurance policy. Specifically, claimants were satisfied with the process for filing a claim (81 percent), the promptness of the payments (79 percent), the responsiveness of the insurer (75 percent), and the overall communication from their insurer (71 percent).

Other key findings from the Harris Interactive survey include:

- Most claimants who utilized innovative programs offered by insurers – such as return-to-work, rehabilitation, workplace accommodations, education benefits, and help starting a business – were satisfied with these programs. Eighty percent said they were satisfied with the rehabilitation program they participated in; 78 percent were satisfied with the workplace accommodations provided; 70 percent were satisfied with the education benefits they received; 69 percent were satisfied with the return-to-work program they participated in; and 64 percent were satisfied with the support they received to help start a business.

- Two-thirds of claimants (66 percent) did not encounter any problems with the claims process and for those that did, the vast majority (84 percent) had their problem resolved satisfactorily.

[7] Council for Disability Awareness, *2014 Long-Term Disability Insurance Claims Survey*, September 2013

- The vast majority of claimants (96 percent) say it is at least somewhat likely that they would have suffered financial hardship if they did not have disability income protection. Furthermore, two-thirds (67 percent) say it would have been very or extremely likely that they would have suffered financial hardship.

- Most private disability insurance claimants who also received SSDI benefits (79 percent) said they were satisfied with the process for filing and receiving benefits.

- Ninety-seven (97) percent of SSDI claimants said it was at least somewhat likely that they would have suffered financial hardship if they had received only their SSDI benefits and not private disability insurance benefits.

## VII. Conclusion

We appreciate this opportunity to share our perspectives on the interaction of private disability income protection and the SSDI program. We look forward to working with this Committee and other congressional committees to maintain and strengthen the disability income security of working Americans – and to improve the long-term fiscal strength of the SSDI program.

Chairman ENZI. I will yield the balance of my time.

Senator Sanders?

Senator SANDERS. Thank you very much, Mr. Chairman, and thank you very much, Madam Secretary, for being with us. In fact, you are the Acting Commissioner, are you not?

Ms. COLVIN. Yes. I have been acting for 2 years.

Senator SANDERS. You have been acting for 2 years.

Ms. COLVIN. Yes.

Senator SANDERS. Well, I would hope very much that we in the Senate will move to confirm you and remove the "Acting" from your title.

It is my understanding, Commissioner Colvin, that the average Disability Insurance benefit is around $1,150 a month?

Ms. COLVIN. That is correct; $1,165 to be exact.

Senator SANDERS. If, in fact, a 19-percent reduction took place, that benefit would be reduced, if my arithmetic is correct, to about $11,324. In real human terms, what does this mean to a disabled American, maybe somebody with a terminal illness, somebody paralyzed, an amputee? What in real life does this mean to that person?

Ms. COLVIN. Well, they would really have to think about the inadequacy of the existing benefit. We are talking about 30 percent of the individuals on our rolls for disability who have no other income, this—

Senator SANDERS. No other income.

Ms. COLVIN. No other income.

Senator SANDERS. So they would see a 20-percent or a 19-percent cut in their income.

Ms. COLVIN. Well, certainly 19 percent would take them well below the poverty level. We are talking about most at the poverty level now, and for about 80 percent of the individuals who receive this benefit, about 50 percent would be—they would rely on this benefit. So they are already at the edge financially, struggling to put food on the table, making choices between eating and paying their rent.

I have worked with this population my entire career. This is a population that would like to work. Remember, we are talking about workers who have paid into a system, who experienced a disability, a severe disability, and find that they are no longer able to work.

Senator SANDERS. Commissioner, let me just ask you this: Is where we are today in terms of the Disability Insurance Fund, is that a surprise to anybody? That is number one. Or was this projected many years in the past based on demographic trends? And, number two, I know you are not necessarily a historian, but you do know that time and time again—in fact, 11 times in recent years under Republican and Democratic Presidents—this issue was resolved quietly, non-controversially, I think a number of times under President Reagan, that as you indicated, this is money coming from the worker. Am I correct in saying that this issue was dealt with nonpartisanly 11 times in recent years?

Ms. COLVIN. That is correct. It has been the mechanism to readjust the monies among the trust fund because, in fact, as I said, it is the same worker, some portion of their taxes go into the Dis-

ability Trust Fund and a portion to the retirement, but it is the same worker. And so it has been adjusted both ways, from DI to retirement and from retirement to DI, the last time in 1994.

Senator SANDERS. Right, and as I understand it, with virtually no controversy. Is that correct?

Ms. COLVIN. That is my understanding. And, again, this has not damaged the health of the combined trust funds. The trust funds will still be solvent until 2033.

Senator SANDERS. And, by the way, while we are on that subject, am I correct that the Social Security Trustees have said that Social Security can pay out every benefit owed to every eligible American until 2033? Is that correct?

Ms. COLVIN. That is correct.

Senator SANDERS. All right. Let me ask you this: I have proposed on different—some of my colleagues have approached the problem in a slightly different way, but I asked the Chief Actuary of the Social Security Administration, Mr. Goss, to estimate how long the solvency of Social Security would be extended based on legislation that I authored which would apply the Social Security payroll tax on income above $250,000. Will you confirm with me—and I think he is here—that his answer was that Social Security would be made solvent until 2060, 45 years from today? Is that correct?

Ms. COLVIN. That is correct. He is here, but I did see the letter, and that is a correct statement.

Senator SANDERS. Thank you very much for the hard work that you are doing on behalf of the elderly and the disabled.

With that, Mr. Chairman, I would yield the floor.

Chairman ENZI. Thank you.

Senator Corker?

Senator CORKER. Well, thank you, Mr. Chairman. And I just want to go on the record as saying that I do not think any of us here, at least in my observation, would want to trade places with someone who happens to be on Social Security disability. I think all of us want to make sure that people who are in need have access. I think it is also—I think everyone here knows of the tremendous hardship that people who are living on the minimum benefits, if that is their only income, it is very difficult.

And to the Ranking Member's comments, the 1983 reforms that were put in place were based on 90 percent of income being taxed. Today it is at 83 percent. That is a fact.

And one of the things that Bowles-Simpson, people working in a bipartisan way, had put together was raising it to 90 percent, but in addition to that, over time gradually increasing the age, because people are living longer, using chained CPI, and also adjusting the benefits so that the lower-income benefit more fully from growth and upper-income less.

And so I would just say that it seems to me there is a way, an appropriate way, to deal with this issue and stand ready to work with others to make that happen so that this benefit that is so important to people will be there.

As a matter of fact, I will just—it is your understanding, ma'am—and thank you for your service in this acting position. By the way, have you been put up to be the permanent person?

Ms. COLVIN. My name was submitted in the last session. It will be resubmitted this session.

Senator CORKER. Well, I look forward to that.

Ms. COLVIN. Thank you.

Senator CORKER. It is your understanding that the longer we wait, even though the program is solvent through for 18 years, the longer we wait, it is more difficult to solve the problem, isn't it?

Ms. COLVIN. Absolutely. We do need to act promptly. This is a very complex problem. I think that changes have to be based on scientific evidence, and we certainly have a number of research studies that can be made available to you. And so I think that through the reallocation, which gives us a temporary reprieve, that then gives Congress to find a bipartisan solution to this long-term issue.

Senator CORKER. And I realize that because of the way these budgets operate these days, this would sort of normally be the case. But it is your understanding that the President's proposal does not lengthen the solvency of the program. Is that correct?

Ms. COLVIN. That is correct. It simply buys some time for Congress to come up with a bipartisan solution.

Senator CORKER. And I would hope we would do that.

It is also your understanding, is it not, that the way the President made this proposal regarding disability, it actually shortens the solvency of the program, the other portion of the program for old-age retirement benefits. Is that correct?

Ms. COLVIN. We looked at 2034. We are talking about one year less for the OASDI, yes. But you still have 18 years.

Senator CORKER. That is not very long, is it?

Ms. COLVIN. Well, I would hope it would not take us 18 years to come to a bipartisan solution.

Senator CORKER. But every year we wait it gets more difficult. Is that correct?

Ms. COLVIN. Absolutely.

Senator CORKER. So in many ways, if you think about it, by not addressing this issue for all of those citizens who work hard all of their lives, what this recommendation actually does is lessen those people that are never going to collect disability payments, by the grace of God, anyway, will never be in a position to have to receive those. In many ways, the ones that are working and will only receive their retirement benefits are harmed by this proposal. Is that correct?

Ms. COLVIN. I do not believe that. No, I do not think that is correct. I think that certainly, as we said, we need to take some action now, and I would expect that action would be taken well before 2033. So, in fact, we would be able to come up with proposals that would strengthen this program and take away the need to be concerned about what happens in 2033.

Senator CORKER. But Congress needs to do that pretty quickly.

Ms. COLVIN. Congress needs to do that.

Senator CORKER. And it needs to happen fairly quickly to do it in a way that is not hugely reshaping. Would you agree?

Ms. COLVIN. I agree. The President has set forth six principles that, if you would let me share it with you, I think it is important.

Senator CORKER. If you do not mind, I will read those. Thank you.

Ms. COLVIN. All right. Thank you.

Senator CORKER. I know it is in the budget.

Ms. COLVIN. Okay.

Senator CORKER. Let me ask you this question: What has happened recently is when we have had economic downturns, we have had a significant increase in the use of disability payments, which speaks to something else happening in the program. In other words, all of us want people who deserve disability to get it. But when people get it that do not deserve it, it actually hurts those very people that are in need. So we have seen a change—the economic downturn causes a lot more people somehow to be on the disability program.

We have also seen an appeals process which almost makes it look like there are some attorneys that almost create—are creating mills, if you will, to cause people to be on the program, again, not deserving people in some cases. And my time is up, I know, but do you agree that one of the things we need to also do to make sure those deserving get the benefits they need is to look at some reforms to make sure that those who may be taking advantage of it no longer do that?

Ms. COLVIN. We are always attentive to ensure that the decisions that are made are the right decisions. The definition of disability is that you have to have a severe impairment that prevents you from being able to do any job in the economy and that that disability is going to last at least 12 months and may eventually result in death. I think there is really a misconception about large numbers of people being on our rolls who are not, in fact, disabled. The average person is on the rolls for about 10 years. If you come on the rolls around 55—and a large number of our people come on the rolls around 50—they die within the first 5 years. So it again points to the fact that you have severe disability.

But we focus on quality in the program. We try to make certain that our adjudicators are following the act and following the rules. We have a stringent review process. We are required to do 50 percent reviews of all of the cases at the DDS level before they even go to the point where they are being paid. And we have a 98-percent accuracy rate.

Senator CORKER. My time is up. It sounds like you do not think any reforms are due.

Ms. COLVIN. I definitely think we need reform. I am not going to suggest that. We do need reform.

Chairman ENZI. Senator Stabenow.

Senator STABENOW. Thank you very much, Mr. Chairman and Ranking Member. And, Commissioner Colvin, thank you very much for your service.

Let me just start where my friend left off. I think there is a general sense that during the recession more people apply for disability and, therefore, more people are receiving disability. And the numbers that I have seen do not show that out. Would you agree that more people may apply, but that does not mean they receive it? In fact, we have a number of cases of folks who are seriously disabled in Michigan that we work with all the time that have

challenges even getting through the complexity of the system. And I notice from the Office of Inspector General that of thousands of cases looked at for fraud in 2013, there were only 100 legal cases that were brought, that had enough merit to bring them, and that was the lowest rate I have seen in any Government program, about 10 out of a million people.

But isn't it true—you may have more people applying, but that does not mean you are saying yes. Is that correct?

Ms. COLVIN. That is correct, Senator. We have many workers who are marginal. They have disabilities, and they continue to try to work. And when jobs are there, they work even though they can certainly meet our definition. They are in and out of the job market. They are often not able to do substantial gainful activity, which is a requirement of the disability law. So some of those individuals may go on the rolls. But it is a small number. And if you look at our most recent numbers, you will see that the initial applications are going down.

Senator STABENOW. Thank you. And it is also true—I mean, when we look at the fact that we have more veterans coming home, veterans who are permanently and totally disabled as a result of military service or just as part of the community, they may, in fact, be part of those that you are serving. Is that correct?

Ms. COLVIN. That is correct. And the increase in the disability rolls was predicted by our actuaries. We knew that during this period we would see an increase, but it was not due to people who should not get on the rolls. It was due to the demographics that Senator Sanders talked about earlier.

Senator STABENOW. And we have more women coming into the workforce, and—

Ms. COLVIN. More women.

Senator STABENOW. I know, and I am unfortunately going to be going to the Finance Committee in a moment and not be able to stay for the second panel. But I do notice that we have someone in the second panel, I am sure a distinguished individual, talking about more mental health cases that are being included as somehow a bad thing. I have to say that as somebody who is a mental health advocate, I am glad since the 1980s we recognized that there are diseases above the neck as well as below the neck. And Senator Roy Blunt and I have been leading the effort to make sure that we are doing to more equalize and understand serious mental health issues. And so as that is included, I would actually commend you for that as well.

Mr. Chairman, let me just say that, first of all, Social Security is something that is an insurance program that everyone pays into, and it is probably the best deal in town.

Ms. COLVIN. Yes, it is.

Senator STABENOW. It is a retirement plan; it is a disability plan; it is survivor benefits. We are talking about in the short run the need to adjust it by less than 1 percent. In my judgment, the short term is a phony crisis. We have long-term challenges that we want to make sure to keep it strong and strengthen Social Security, and I think that there is—it may not be in this Committee. I do not know yet, Mr. Chairman, but there certainly is a debate with many on the Republican side of the aisle about wanting to privatize or

fundamentally change the structure, turn it over to Wall Street to manage, which, boy, that would have been great back a few years ago.

You know, I guess I would say I am a supporter of the structure of Social Security, and I think there are a lot of things happening to working people today. They are seeing defined pension plans go away. We do not need to see Social Security go away for people in terms of fundamental financial security for people.

I also want to just recognize for the record that tomorrow is the day when millionaires in America will stop contributing to Social Security. So everybody else, if you earn $50,000, $60,000, $100,000 a year, working hard every day, you are still paying in all year. But there is a certain group of folks that they can still get Social Security but they do not pay in anymore. So I think Senator Corker had a good idea when he talked about how we need to adjust who is certainly paying into that as well.

So the final thing I would just say is that I agree with the idea that we should be focusing on opportunity and job training and creating opportunity for people to work. I think it would be a good test of us in the Budget Committee on how those numbers look in terms of job security—I mean job training funding coming out of the Committee, certainly appreciate that. But in my judgment, Social Security is a great American success story, and I just want to see it strengthened.

Thank you.

Ms. COLVIN. Thank you.

Chairman ENZI. Senator Perdue.

Senator PERDUE. Thank you, Mr. Chairman and Ranking Member.

Administrator Colvin, thank you for your tireless service to our country. You know, this debate, this conversation, is what drives people in my State absolutely crazy. I am not from the political world, so I am going to be very straight with you this morning. You know, the idea that this is a trumped-up, phony crisis is absolutely ridiculous, and it is ridiculous to people back home.

I agree with you on several things. You said this morning that we need to move to ensure that nobody loses their disability benefits. I agree 100 percent. But the irresponsibility since 1974 has created this situation in 2017, and what we are about to do is going to create another crisis in 2033.

I have no problem—let me make sure I understand the real simple details of this.

First, the Social Security retirement fund will go from 2034 being insolvent to 2033 if we move and reallocate funds to the Disability Fund. So the Disability Fund then goes from 2017 to 2033. Frankly, I do not see that as a big deal. What I see as a big deal—and this is where this is not a phony crisis, Mr. Chairman—we have over $120 trillion of future unfunded liabilities coming at us like a freight train.

In 1994, we kicked the can down the road to 2017. Well, here we are. We are about to kick the can down the road to 2033. This should not be a partisan issue. I do not think it is a partisan issue. We get caught up in debating the wrong problem, and the wrong problem right now is what do we do to save this for 2017. That is

easy. In my opinion, I do not have a problem with that, if the administration, along with all the other budget recommendations made, came to us with a well-thought-out, long-term strategy and recommendation to how to solve both of these trust funds for the future of our kids. I have two kids, two sons in their middle career. I have got to look at them, if we do this, and say, "You know what? I am kicking the can down the road. Good luck, pals." In 2033, both of these are insolvent. I think that is correct as well. Is that right? In 2033, both the trust funds are insolvent as of 2033?

Ms. COLVIN. Yes, that is correct.

Senator PERDUE. So what do we do—

Ms. COLVIN. I should say not insolvent. The reserves will be depleted. When you say insolvent, people think that means that you cannot pay anything. It means you would not be able to pay the full amount. For instance, in the DI program you would still be able to pay 80 percent.

Senator PERDUE. Right. And as you said before, that is a mean amount. That is a very small amount. So that is not what any of us want to do.

Ms. COLVIN. Absolutely.

Senator PERDUE. So I think the first goal here, in my opinion, is to make sure that we can live up to the obligations that we have right now. I think everybody in the room so far has said that. And I think you have said that, too, correct?

Ms. COLVIN. Well, I certainly believe we have to satisfy obligations, but I do believe this problem can be fixed, and the administration has clearly indicated its desire to work with Congress to come up with a long-term solution.

Senator PERDUE. And where is that recommendation? That is what I am being asked by the people back home, is, okay, the number one crisis we have right now, in my mind, is our ability to fund our future unfunded liabilities. Right now we have $18 trillion of debt; we have over $100 trillion of future unfunded liabilities coming at us, which is more than $1 million a household. And one of the things creating a problem in both these trust funds is the fact that today we have about 30 percent of our workforce not participating in the workforce. Most of those want to participate in the workforce. Between unemployment, underemployment, and people who have dropped out of the workforce, that is a large number. And if those people, a large number of those people were working, it would not create a solution for this, but it would certainly ameliorate the problem and give us more time to work on it.

You said that we do not need to kick the can down the road. I think your words were this is a temporary reprieve to give us an opportunity until 2033 to solve the problem. I think you said that, and I agree with that. The question I have is: The longer we wait, the harder it is to solve this. How can we move right now—you are the person in charge. How can we move right now to address the long-term solution and enter into an honest and open debate about solving it once and for all?

Ms. COLVIN. Well, Mr. Perdue, I think we have to address the more immediate crisis, which is the 2016 issue right now, and I think the President's proposal on reallocation will do that. And I think we need to do that and do that now.

That does not mean that we cannot then begin to sit down and talk about the more long-term issues, but we should not have persons with disabilities wondering whether or not in 2016 they are going to still receive a full benefit.

Senator PERDUE. I agree with that.

Ms. COLVIN. So I think we need to do that now. We need to address the proposal that is on the table, which will also help to address some of the concerns you have about the program, that we can make sure that there is no one on the roll who should not be on the roll.

Senator PERDUE. And my question is: How can you ask me to do that—I agree with everything you just said. How can you ask me to do that without a bona fide, honest, straight-up proposal to solve this thing past 2033?

Ms. COLVIN. Well, there are various proposals out there. It is going to take a lot of discussion to come to a bipartisan—

Senator PERDUE. What is the President's proposal, what is the administration's proposal to solve this past 2033?

Ms. COLVIN. The President's proposal is to address the immediate problem, which is the—

Senator PERDUE. Which does not solve the problem past 2033. Is that correct?

Ms. COLVIN. The President has an immediate solution for the 2016 problem, which is what we should address, but—

Senator PERDUE. Agreed, but let me—I am sorry to interrupt, but there is no proposal from the administration to solve this crisis past 2033. Is that correct?

Ms. COLVIN. Well, he certainly has set forth the principles that I wanted to mention earlier that gives you the basis—

Senator PERDUE. But there is no—there is no—well, let me just—

Ms. COLVIN. —for what a proposal should—

Senator PERDUE. I understand, but I am really trying to get at this. We have had proposals on everything else in this budget. Is there no proposal to solve the Social Security catastrophe, impending catastrophe, which happens in 2033, coming from this administration?

Ms. COLVIN. I do not think it is reasonable to expect that a 2016 budget is going to have a proposal to solve a problem down the road for 2033. That is going to take a lot of bipartisan discussion and agreement. And there are many proposals out there that Congress can begin to discuss and look at as long as it follows the basic principles. And I will not try to put those forth since I see that you are not interested in them, but I think the thing that I try to convey is we need to make sure that we are going to strengthen this program, that we are not going to slash benefits, that people are going to be able to rely on a robust disability and retirement benefit—

Senator PERDUE. I can assure you that I care very much about each one of those, but I also care about what happens past 2033.

Thank you, Mr. Chairman.

Chairman ENZI. The Senator's time has expired.

Senator Whitehouse?

Senator WHITEHOUSE. Thank you, Mr. Chairman. Welcome, Commissioner. We are delighted that you are here.

The predicament that Social Security is in some say has something to do with income inequality, that because only the first—$108,000, is it?—$118,000 of income is subject to the payroll tax, that as more and more people who earn big incomes get richer and richer while the middle class goes no place, which has been our recent economic story, that more and more of the salary base of the country moves up into that above $118,000 quadrant, and that as a result, there is less money being paid into Social Security. Is that true?

Ms. COLVIN. That is true.

Senator WHITEHOUSE. And how does the aging of the population—we had a very well known baby boom after World War II. Does that play any role in this?

Ms. COLVIN. Absolutely. The people who were sort of at the disability-prone years, who are going no the disability rolls, are now reaching their retirement years. And so they are moving over into the retirement fund. If you are lucky and you are on disability, of course, and you live long enough, then you would automatically go—if would be seamless to you, but your benefit would begin to come out of the OASI retirement fund.

Senator WHITEHOUSE. Now, both Social Security and Social Security disability are funded by the payroll tax, correct?

Ms. COLVIN. By payroll taxes.

Senator WHITEHOUSE. And there is kind of a gate that distributes the payroll tax money between Social Security disability and Social Security retirement?

Ms. COLVIN. That is correct, and it has always been adjusted as needed between the two funds—

Senator WHITEHOUSE. Over and over, correct?

Ms. COLVIN. Eleven times.

Senator WHITEHOUSE. And both ways.

Ms. COLVIN. Both ways.

Senator WHITEHOUSE. And now what our friends in the House have done is they have basically closed that gate in order to precipitate this crisis in—or which will have the effect of precipitating this crisis in Social Security disability, correct? If you move the gate, the crisis goes way off into the future.

Ms. COLVIN. That is correct.

Senator WHITEHOUSE. All right. Now, and the amount in question to make Social Security disability whole right now, if we were to do it, is about how many billion dollars?

Ms. COLVIN. The $330 million that I gave before—billion, I am sorry, $330 billion.

Senator WHITEHOUSE. But that is over 10 years.

Ms. COLVIN. Yes.

Senator WHITEHOUSE. So per year—

Ms. COLVIN. No. Over 5 years.

Senator WHITEHOUSE. Five years, okay. And our information is that if you did something about the cap on the payroll tax—so right now you have got a situation where, if you are a plumber and you make $118,000, you pay the exact same amount to support our national Social Security system as the hedge fund billionaire who

makes $20 million a year. They both pay the exact—not just the same rate. They pay the same amount because of that cap.

Now, if you were to come back in and apply the payroll tax again, our information is that if you started at the 10 million and first dollar of income, so anybody making less than $10 million would pay no additional payroll tax, but if you are making $10,000,001, you would pay payroll tax on the $1; if you made $12 million in a year, you would pay payroll tax on the last $2 million, as well as the $118,000, that if we did that, that would completely cure this problem.

So if we wanted to take care of this problem, we could do it in one fell swoop, and when we are talking about millionaires and billionaires, people making more than $10 million in one year, to ask them to contribute a little bit more of the above $10 million salary to Social Security does not seem like asking a lot. And so I would ask you to take a look at those numbers and see if the numbers work. That could be a question for the record. My information is that those numbers do work and that you can fully resolve this manufactured Social Security disability crisis that the House rule has created by simply going and asking people making more than $10 million a year to pay the same fair share that the $118,000 plumber does, actually net a good deal less because between $118,000 and $10 million, they will be Scot free on payroll tax.

So if you could do that—

Ms. COLVIN. We will provide those numbers for you.

Senator WHITEHOUSE. Will you look at that for me?

Ms. COLVIN. Absolutely.

Senator WHITEHOUSE. Very good. Thank you very much.

Senator WHITEHOUSE. I understand that questions about fraud were asked already, that it is basically very, very small numbers coming out of—

Ms. COLVIN. Well, the question was not asked, but I am glad you raised it because there is a misperception out there. We have had a study done by the Office of Inspector General, and they have identified the very minimal amount of fraud, less than 1 percent. But I want to go on record and say even one case is too many, and we are very aggressive in identifying any type of fraud so that we can prosecute.

We also have programs that detect it in advance—

Senator WHITEHOUSE. Using computer models and so forth.

Ms. COLVIN. Well, also we established a Cooperative Disability Investigative Unit. We have them in 35 States. At least we will have them by the end of 2015. I would like to eventually see them in all States. But this is the one program that we have that allows us to detect or prevent fraud so that we do not pay benefits and then have to chase the money. And there are a number of other very active, aggressive anti-fraud initiatives we have underway, and I would be happy to provide that information if you want it.

Senator WHITEHOUSE. Mr. Chairman, my time has expired. I thank you.

Chairman ENZI. Thank you.

Senator Graham?

Senator GRAHAM. Thank you, Mr. Chairman.

Conceptually, do you think it should be the Congress' goal eventually—not in the 2016 budget but eventually—to come up with a solvency plan for Social Security, the disability, the retirement fund, for 75 years? Would that be a good thing for America?

Ms. COLVIN. Absolutely.

Senator GRAHAM. Okay. Now, as we try to accomplish that goal, I just want to make sure that I understand what we cannot do.

Now, Senator Whitehouse is a smart guy, and I am sure the math works out, or he would not have presented the analogy of taxing people, you know, paying payroll taxes above $10 million to fix this problem that is looming today. I just do not want America to believe that we can tax our way into solvency. Do you believe that to get a 75-year-solvent program we can do it with revenue alone?

Ms. COLVIN. I am not here to advocate for a specific position. I think that we would be very happy to work with you to tell you what is possible.

Senator GRAHAM. Yes, ma'am.

Ms. COLVIN. There are many proposals, and we can help you with the analysis and the—

Senator GRAHAM. Well, when you examine his proposal about closing the gap by using payroll taxes above $10 million, could you come back and answer my question, if you could? What kind of revenue would you have to generate, what would the tax rates be to make Social Security solvent for 75 years with revenue alone?

Ms. COLVIN. I am sure our Actuary can provide that.

Senator GRAHAM. Okay. I appreciate that very much.

Senator WHITEHOUSE. Mr. Chairman, may I get a copy of that as well?

Senator GRAHAM. Absolutely.

Senator WHITEHOUSE. You can make that both. Thank you.

Senator GRAHAM. We are not going to sneak up on you at all.

Ms. COLVIN. And that is what our actuaries do. If you have a proposal, the Actuary will cost it out for you.

Senator GRAHAM. Okay.

Ms. COLVIN. We will let you know what the impact will be for the American public.

Senator GRAHAM. Absolutely. Now, let us talk about why we keep having to do this. In 1956, when the Disability Fund was created, how many workers were there for every retiree in the program? I think it is 16.

Ms. COLVIN. We will get that for you in a minute.

Senator GRAHAM. Yes, ma'am. I was born in 1955, and I believe that for every Social Security retiree, there were 16 workers paying into the system. Check that out.

Ms. COLVIN. I do not have it before me, but I know my staff has it.

Senator GRAHAM. Yes, ma'am. Check that out.

Ms. COLVIN. It is in our Trustee report.

Senator GRAHAM. Thank you. Check that out.

And today I believe there are three workers for every Social Security retiree.

Ms. COLVIN. Today, that is correct.

Senator GRAHAM. Okay. In 20 years, there are supposed to be two. Does that make sense?

Ms. COLVIN. Probably, as we look at the birth rate of the country.

Senator GRAHAM. Right. We are living longer. Life expectancy is at an all-time high. That is good news. Agreed?

Ms. COLVIN. Yes.

Senator GRAHAM. We are having fewer workers born—we are having fewer workers available to the workforce because of demographic changes, and that is a problem.

Ms. COLVIN. That is a problem.

Senator GRAHAM. So the question for the Committee is: How do we fix this basic problem? Eighty million baby boomers are going to retire in the next 20 years or so, and the number of workers to keep this system solvent, Social Security and Medicare, is going to be down to two. How do two people pay for these programs without it putting us on the road to becoming Greece?

Can you solve that problem through revenue alone? I would say no. Would the proposal the President is talking about for long-term solvency include means testing?

Ms. COLVIN. I do not know what the President's long-term solution will include.

Senator GRAHAM. Well, you just told the Senator from Georgia he had a proposal.

Ms. COLVIN. No, I did not. I said that the reallocation proposal which is in the budget. I did not speak—

Senator GRAHAM. I thought you said he had some concepts or—

Ms. COLVIN. Oh, I talked about the concepts, the principles that any reform—

Senator GRAHAM. Principles, I am sorry. It is my bad. Not proposal. Principles. Is one of those principles means testing?

Ms. COLVIN. No, it is not.

Senator GRAHAM. Is one of those principles age adjustment for retirement?

Ms. COLVIN. No.

Senator GRAHAM. Is one of those principles CPI adjustment?

Ms. COLVIN. Would you like me to tell you what the six principles are?

Senator GRAHAM. Yes, ma'am. You have told me what they are not, so tell me what they are.

Ms. COLVIN. All right. The first one is that any reform should strengthen Social Security for the future and restore long-term solvency—

Senator GRAHAM. That is not a principle. That is just a statement.

Ms. COLVIN. Okay.

Senator GRAHAM. Number two?

Ms. COLVIN. The second, the administration will oppose any measures that privatize or weaken the Social Security—

Senator GRAHAM. That is not a principle as much as it is what you will not do. Okay.

Ms. COLVIN. Third, while all measures that strengthen solvency should be on the table, the administration will not accept an approach that slashes benefits for future generations.

Senator GRAHAM. Well, let us—so you have just told me means testing is not on the table. Is that consistent with that statement?

Ms. COLVIN. I can only give you the statements that I have, sir.

Senator GRAHAM. Okay. I am sorry. Keep going.

Ms. COLVIN. Current beneficiaries should not see their basic benefits reduced.

Senator GRAHAM. Okay. These—

Ms. COLVIN. Reforms should strengthen—

Senator GRAHAM. Okay. I am sorry. Keep going.

Ms. COLVIN. —Social Security for the most vulnerable, including our low-income seniors, and reforms should maintain a robust disability and survivor benefit structure.

Senator GRAHAM. That is a set of principles that makes sure we do absolutely nothing meaningful. So I just want to say if that is the President's plan, we will never get there. That is not my plan. I am willing to stretch myself and my party. I am willing to do revenue to get us to entitlement reform.

Ms. COLVIN. I am very happy to talk about the President's plan that is in his budget for reallocation.

Senator GRAHAM. Yes, ma'am, I know you are, and that plan has been used in the past. And I do not know how we will fix this problem, but we will. I just want to let you know that I am really tired of bailing out water when the boat has got a hole in it a mile wide and we are using a very small pail, and somebody someday somehow up here is going to have to do the hard things. And I just want to put myself on the record as being willing to do hard things as long as they work. And we will fix this problem, but apparently we are not going to do much more than that.

Thank you very much.

Chairman ENZI. Senator Kaine.

Senator KAINE. Thank you, Mr. Chairman, and thank you, Commissioner Colvin.

I am going to take my wife out for dinner Saturday for Valentine's Day, and when I am toasting her, I am going to toast you.

Ms. COLVIN. Thank you, Senator.

[Laughter.]

Senator KAINE. I am going to toast you because you were nominated to be Commissioner on Valentine's Day—

Ms. COLVIN. I was.

Senator KAINE. —2 years ago.

Ms. COLVIN. Yes. Thanks for remembering that.

Senator KAINE. And you have been an Acting for 2 years. A mayor or Governor insight: Not having confirmed leadership always is weaker than having confirmed leadership. Always. Always. When the Senate does not exercise the advise-and-consent function to confirm a leader, we create some weaknesses within an organization, despite the best efforts of Actings. But we also send a message. We send a message to the public that we do not think this agency is that important; we do not think this agency that provides Social Security to the most vulnerable people in our country is that important.

And I have noticed something, Mr. Chairman, as I have been here for a couple of years. This happens a lot, and it seems to happen with agencies that are kind of the same. Two years of Acting

at Social Security, 6–1/2 years of Acting, not a confirmed Administrator, for CMS, the Centers for Medicaid & Medicare Services, the single largest line item in the budget of the United States that is specifically designed to serve vulnerable people. This is actually a bipartisan comment. The first 2 years were—the Democratic Senate did not want to approve an Administrator at the end of the Bush administration, and then for 4–1/2 years, the Republican Senators did not want to approve President Obama's nominee. Six and a half years with an Acting in the program that is the largest program—larger than the defense budget.

FHFA, Federal Housing Finance Agency, 4 years of Acting before Mel Watt was finally confirmed, and to do that we had to change the Senate rules.

Consumer Financial Protection Bureau, 1–1/2 years of Acting.

The agencies where we allow Actings and where we do not move to confirm dramatically are all in the human services side. They are all in the human services side. We do not have an Acting Secretary of Defense. Now, in the Department of Defense, there are a lot of questions about contracts and cost overruns and all kinds of things. But we do not have an Acting Secretary of Defense. What we have is Actings in agencies that serve vulnerable people.

I am worried about this because I am worried about an old-timey term that raises a lot of angst in Virginia: legal nullification, trying to nullify the law. If there is an agency that is controversial or unliked, and there is not enough votes to get rid of the agency, and there is not enough votes to defund the agency, what is the next thing that you can do? Not vote to confirm a leader. Not vote to confirm a leader. And I am just fascinated by the fact that most of these long-term Actings where the Senate will not act to confirm a leader cluster in programs that serve the most vulnerable Americans.

So I am going to toast you on Valentine's Day, and I am going to toast you and hope that that Acting title is removed and that the Social Security Administration, which serves vulnerable Americans every day, will be respected enough by the Senate to actually have a confirmed leader.

I want to ask you about anti-fraud efforts. One of our colleagues, not on this Committee—the folks on this Committee are far too savvy to say something like this. But one of our colleagues said recently, and I quote: "Over half the people on disability are either anxious or their back hurts." That was a comment made by one of our Senate colleagues in January. I find that to be a very offensive comment, but it is also quite inaccurate. And I want you to tell the Committee some of the things that you are doing every day, some of the reforms you are putting in place, to take the really low fraud rate—very, very low—and make it even lower.

Ms. COLVIN. Well, first of all, people do not get on our rolls simply because they have a back pain that they allege. That statement has to be corroborated by medical evidence, including lab reports. I really need to say that. The people on our rolls are the most severely disabled. We have 58 million people in this country who have self-identified that they are disabled, and we only have 9 million on the rolls, 7 million who are workers and 2 that are—I mean 9 million workers who are severely disabled.

But we take fraud very seriously, and most of the fraud that has been detected in our program has been detected by our own staff. Our big challenge, of course, is the third-party fraudsters, like doctors and lawyers who facilitate fraud. And in the President's proposal is a proposal—I mean, in the President's budget is a proposal that would allow us to go after overpayments for those individuals, because often they are not—

Senator KAINE. So in the President's budget proposal, there are additional anti-fraud—

Ms. COLVIN. There are additional anti-fraud initiatives to—

Senator KAINE. To help the solvency of this program?

Ms. COLVIN. Absolutely. That is one. The other is the CDRs that I talked about, if we get those fully funded, because we have people on the rolls that are entitled to receive a check until we determine that they are no longer disabled. So they are not being fraudulent, but you would say that you still have that.

The CDR units that I talked about, when I was here in 1998 under President Clinton, I established a unit that was a partnership between the Office of Inspector General and law enforcement at the local level and us here at the Federal level, and these identify people who are pretending that they are disabled, and we are able to then stop them from getting a payment. It has been hugely successful. OIG would say that there is probably about a $17 return for every $1 that is spent. We only have 35 of those. When I came back after being away for 15 years, we only had 24. I increased five in 2014, and I am doing another five in 2015. So that will take that number up. We should have one in every State, but it takes funding to do that.

We also are establishing a centralized fraud unit that is being very aggressive in using data analytics. We are working with the private sector, and we are doing some benchmarking to look at what else we can do to be able to detect the fraud before it occurs.

Senator KAINE. Commissioner Colvin, I have run over time, and I just want to thank you for that answer, and I know that there is more on this score that we can talk about.

Ms. COLVIN. We would be happy to provide more for the record if someone wants it.

Chairman ENZI. Senator Grassley.

Senator GRASSLEY. Commissioner Colvin, I regularly hear from my colleagues on the other side of the aisle contending Republicans are attempting to manufacture a crisis in the Disability Insurance program where none exists. They argue it has been regularly practiced to simply transfer funds from the Old-Age Fund to the Disability Fund to cover any shortfall.

However, that understanding appears to not square with reality. I use this example. Last year, in response to a question from Chairman Hatch at the Finance Committee hearing, Deputy Commissioner La Canfora testified that she was unaware of any past "stand-alone legislation that reallocated payroll tax inflows from the OASI Trust Fund to the DI Trust Fund."

So, Commissioner Colvin, could you confirm previous allocations from the Old-Age Fund to the Disability Fund were not done as stand-alone legislation? And then, in addition, is there any reason

that a stand-alone reallocation should be the only option considered now?

Ms. COLVIN. I am not certain I know what you mean when you say "stand-alone." I do not think that the proposal that the President is making is any different than what has occurred in the past. We have had 11 reallocations in the past from the DI to the OASI and vice versa. So I am not sure that I understand what "stand-alone" means. I would have to go back and research that and give you something for the record.

Senator GRASSLEY. Okay. You can supplement the record if you want to, but the most recent allocation in 1994 included an alteration of eligibility for drug addiction and alcoholism to qualify for disability.

Ms. COLVIN. Okay.

Senator GRASSLEY. It is generally understood that demographic changes have contributed to increased benefits and the projected shortfall. But I am also curious as to the contribution of certain policy changes. According to the Congressional Budget Office, legislation in the early 1980s increased subjectivity in the determination of policy because it "allowed symptoms of mental illness and pain to be considered in assessing whether a person qualified for admission to the DI program, even in the absence of clear-cut medical diagnosis."

CBO goes on to say that these changes "led to a substantial expansion in the share of DI beneficiaries with mental and musculoskeletal disorders."

So, Commissioner Colvin, do you agree with the CBO analysis? Is the increased subjectivity in the determination of disability something Congress should be concerned about?

Ms. COLVIN. I do not think that that statement is fully accurate. Certainly there is an area of subjectivity, but that is complemented by the medical evaluations that I talked about earlier, that no one can come on the rolls simply because they allege pain or some other medical disability that is not substantiated or corroborated by medical records and laboratory results.

Now, in 1984, when Congress acted to make some changes to the law and some would suggest that it was liberalized, you may remember that Congress acted because they felt that the interpretation of the law was very narrow and was not intended to be implemented the way it was implemented. So you had the Medical Improvement Initiative; you had mental health. And coming out of the mental health community, I certainly think it was the right thing to do. Mental health is an illness, but, again, there is very specific criteria that individuals follow in making those decisions. We work with the Institute of Medicine and other such organizations to make sure that we are staying current with medical science. We follow the science. We do not create the medicine, but we interpret it based on what is happening in the medical community at the time.

So I do not think that the 1984 laws liberalized the program. I think that the increase that you saw was the result of the economic and demographic factors that we have talked about: aging of the baby boomers, reaching the disability-prone years, more women coming into the workforce, those kinds of things. And we do a lot

of quality review around those subjective areas that you have talked about. We give ongoing training. As I mentioned before, 50 percent of all decisions at the DDS level are reviewed for accurate before we make a payment. So I think we have control in those areas.

Senator GRASSLEY. Thank you.

Chairman ENZI. Thank you.

Senator King?

Senator KING. Thank you, Mr. Chair.

I want to go back to Senator Perdue's questions and what troubles me about this. I am touched by your faith in bipartisanship to solve difficult problems, but not fully confident. We are much more adept at bipartisan avoidance than we are at bipartisan solutions. And 2033 is not that far off.

Ms. COLVIN. That is correct.

Senator KING. I remember 1998. It was not that long ago. 2033 is going to come, and what I fear is we will have taken a series of steps, such as the one proposed here, and then we will be faced with exactly the same problem, only much larger, on a much more broad scale, involving not only Disability but the Old-Age program, and we will have run out of places to hide.

And let me just state categorically I do not in any way, shape, or form want to see cuts in disability benefits. I do not want to see any diminution of what is already a fairly modest level of support. But what bothers me is the solution, and the solution is avoidance. And inevitably—you have used the phrase "the combined funds actuarially do not change." Well, that is true because one comes down and the other goes up. But the Old-Age does come down by a year, not a lot, but it is the principle of the thing. And we just keep doing this. And I would much rather see some serious discussion about, A, does the program need additional funds because more people are disabled, more p in the workforce, demographics? And are there things that we can do to improve the program and provide the appropriate benefits, but at the same time cut the costs, for example, greater back-to-work programs? I mean, one of the problems, I am sure you are aware, is the so-called cash cliff where there is very little incentive to go back to work. The private sector disability insurance, we have a company based on Maine called Unum that does a great deal of work with this. They have been very successful in getting people back to work. The rate, as I understand it, in this program, in disability, Social Security disability, is 1 to 4 percent ever go back to work.

Ms. COLVIN. That is correct.

Senator KING. It seems to me that dealing with the cash cliff problem, some kind of phasing, greater intervention, working with these folks to get them back into the workforce, which I suspect they would like to do, would do a lot for the actuarial balance of the program. Periodic reviews, demonstration programs to show how we can do this, I would like to see that. Re-fund it. You mentioned the $1 for $9 return. We have got to do things like that, make those kind of programmatic changes. But it just bothers me that we are basically taking from one fund and giving to the other and calling that a solution and saying, well, 2033, I think one of my colleagues said, is way off into the future. It is not. And actu-

arial numbers do not lie, and it is going to come, and this is just another way of making that problem worse when it does come.

So I commend you for the proposal and for the President's stepping forward, but I think it is just too easy to say, "Oh, we are just going to do this for 5 years. It is going to make it okay and, you know, somebody else will deal with it in 2033." We are dealing with problems now because our colleagues 20, 30 years ago did not. And it is just going to get worse. Problems put off rarely get easier to solve with the passage of time. I am sorry to lecture you, but I just had to say I understand the impulse here, but I think it is bipartisan avoidance, not bipartisan solution.

Do you agree that some of these back-to-work and the cash cliff, that those could be effective in dealing with the long-term actuarial problems?

Ms. COLVIN. That is one of the reasons that the President's budget proposes a number of demonstration projects, so we can see just how effective they are. But, clearly, we know that early intervention is the key, Mr. King, because many of the people who come on our rolls are not going to be physically able to go back to work. We certainly want those who are able to go back to work to go back to work, and about 1 percent do. And I think that is terrific considering that the average amount of time on our rolls is about 10 years. So if you get that 1 percent to go back to work, that is about 10 percent.

But I think the key is early intervention to try to get people to be able to remain in the workforce before they come out.

Senator KING. And also the rule that you cannot work at all for, what is it, 2 years before you are eligible or—

Ms. COLVIN. There are some work restrictions, and we are looking at all of those things. I do not want to suggest that within the agency we are not looking to see from, you know, the beginning of the process to the end if there are things that we want to recommend that would require legislative changes. But I just want to reemphasize that anything to fix the program will require congressional action—not administrative action; congressional action.

Senator KING. I understand that, but I would like to see—and I understand that we have got an immediate problem in 2016, and we have got to deal with that, and maybe this rebalancing that you are talking about is the only short-term solution. But I would only support that if I also saw along with that other changes in the program that would increase the actuarial soundness of the overall program and leave us where we are in 2033 instead of aggravating the problem by just pushing it out a few years.

Thank you very much, and thank you for your service under very difficult circumstances. I associate myself with Senator Kaine's remarks. We should get you confirmed so you can fully get to work. I am a former Governor. I think executives should be able to choose the people that they want to work with them, and whatever their party, and stand or fall on the quality of their people.

Ms. COLVIN. Thank you.

Senator KING. Thank you for your service.

Thank you, Mr. Chairman.

Chairman ENZI. Senator Sessions.

Senator SESSIONS. Thank you. Thank you, Mr. Chairman, for what I think is a very important hearing. Commissioner Colvin, it is great to have you here, and we just have to talk about it. Senator King says actuarial numbers do not lie, and we might as well face up to the difficulties.

Commissioner Colvin, is it not fundamentally true that as you consider disability an insurance program, we do not have enough—each individual that pays into Social Security through their payroll taxes for disability actually in effect is paying in less than they are drawing out if they become disabled over time as general numbers?

Ms. COLVIN. I would have to give you those numbers for the record. I am not certain that that is fully accurate, because remember that the average amount of time that someone spends on our rolls is 10 years, and that for anyone coming on who is 55, they die within the first 5 years. So I would like to go back and get the data to make sure that is accurate.

Senator SESSIONS. Well, I think we are running out of money because it is not actuarially sound, is it? I mean, if you are an insurance company, you would have to raise income or cut benefits to keep it on a sound path.

Ms. COLVIN. And those are the things that I hope Congress will look at. What is the path—

Senator SESSIONS. I know. It is our responsibility. It is in law. It is not your—we created this, and we have a shortfall, it seems to me. And with regard to Social Security, the retirement benefit, it is a similar thing. We have created a system that creates a benefit, an increasing benefit when the economy grows, and we do not have enough money coming in both overall and per individual. Is that correct?

Ms. COLVIN. Well, we recognize that you have far fewer workers paying into the system than you did when the program was created.

Senator SESSIONS. Right.

Ms. COLVIN. We celebrated our 80th anniversary this year Social Security will have been in existence, but it is a basic financial security system for the workers of this country. And I think it behooves us to figure out how to make it financially sound.

Senator SESSIONS. I agree we need to make it sound, and it is not your responsibility. It is ours. I acknowledge that. But as I understand it, a worker turning 65 in 2020 who made average wages over their lifetime will pay in $427,000 plus that includes the interest that would be accruing on that into Medicare and Social Security, but they would receive over $100,000 more, $536,000 in benefits. So I am just asking you, this is an actuarially unsound proposition, is it not?

Ms. COLVIN. I would have to look at your numbers. As I said, we recognize that—and we do the Trustee report each year, so we predict what the impact will be each year.

Senator SESSIONS. Well, let me just ask you this: You are in charge of this program. The average person over their lifetime, aren't they going to draw—on average they will draw out more than they pay in, including the interest that might accrue?

Ms. COLVIN. I am not sure of that. I would like to get back with the answer for the record on that. I do not know if that is accurate.

Senator SESSIONS. Okay. Well, thank you. I would like to know that. If that is not so, then we have got less of a problem than I thought we had. It would be nice if that were so.

Ms. COLVIN. I really do not know that number. I need to get back to you for the record with that.

Senator SESSIONS. All right.

Senator SESSIONS. Now, with regard to the disability situation, colleagues—and I know Senator Enzi is going to be wrestling with this, but the administration has said that we would just take the money from the Social Security retirement fund and fix this in the interim. I understand that is the solution. I understand the House has said that they do not want to do that and there has got to be more reforms, which I think should be. Anybody that saw the "60 Minutes" show on disability and lawyers and judges that are too lax and the problems that we have, it is really serious. So I think we need to do that. But I do hope that we can work together on a bipartisan basis to get some reforms in this system instead of just raiding the retirement fund, because it is going kaput, too. It is on an unsustainable path, and the more we take from it to fund the disability portion, the weaker it becomes. So we are not really doing anything but, you know, robbing Peter to pay Paul.

Mr. Chairman, my time is up. Thank you. I look forward to working with you on that, and if you would give me your best estimate on the cash flow of individuals, I would appreciate that.

Chairman ENZI. Senator Merkley.

Senator MERKLEY. Thank you very much for your testimony today, and thank you, Mr. Chairman.

It is my understanding that a lot of veterans are on Social Security disability. Is that correct?

Ms. COLVIN. We have 1 million right now.

Senator MERKLEY. I have a couple letters I thought I would share from veterans back in Oregon.

Kenneth from Medford wrote: "All of my disability came from my service in Vietnam. I am totally dependent on my Social Security disability check. If I do not get paid, I cannot pay the rent. It is impossible for me to work because of my disability, so please stop this game." He is taking it very personally that people are attacking the veterans on disability.

And Roberta from Portland, she wrote: "Dear Senator Merkley, my name is Roberta, and I am a 100 percent service-connected disabled veteran. As such, I collect Social Security disability. I own my home, but I spent a decade homeless after my discharge for disability from the Navy. I am 55 now. I cannot go homeless again. It would be a death sentence."

For folks who are on disability with these significant, major injuries, what happens if we do not sustain the health of this program?

Ms. COLVIN. Well, I do not want to be dramatic, but I have worked with this population my whole career. I think we give them a death sentence. You cannot have people out there who have served this country, you cannot have workers who have helped to build this country strong, that all of a sudden because of inaction we slash their benefits by 20 percent.

If you think about it, if you are getting $1,200 a month, you are barely surviving. And if you then get a cut there, you are not going

to be able to survive. Right now these people are making tough choices between the things that we take for granted—eating, paying their rent, paying for their medicine. I do not think that this country can allow that to happen. These are workers' benefits. People have paid into the system, and they deserve the comfort and certainty that this benefit will continue and it will not be threatened.

Senator MERKLEY. And you have noted in your testimony that just a fraction of those who apply are actually granted disability because it is a very rigorous standard.

Ms. COLVIN. That is correct. At the DDS level right now, there is about a 32-percent approval rate. I do not usually focus on approval or disapproval. What I focus on is making certain that we make the right decision. But these are people who deserve our support and our help. But they have also earned it. It is an earned benefit.

Senator MERKLEY. You have noted that there are these Cooperative Disability Investigative Units around the country in 35 States, and I think I understood you to say that for each dollar invested, we get $15 back.

Ms. COLVIN. I think that the Office of Inspector General says $17.

Senator MERKLEY. $17 back. Is there any reason that we do not just go ahead and put one into another 15 States?

Ms. COLVIN. Money. When I came back, we only had 24. I have already diverted money from customer service, where I should be serving the public, to put these units in, trying to balance. So I put in 10 more, which gives us the 35. But I do not have the resources to do more than that.

Senator MERKLEY. So if we are getting $17 back for every dollar we put in, maybe there would be bipartisan support for that kind of smart investment. There has been a lot of concern expressed. You have noted it is very difficult to be approved for disability and that the fraud rate is minuscule. But certainly having the investigation units is a part of what keeps the solvency, so maybe that is a bipartisan conversation we can have for that type of return on the investment.

And then you have also noted these Continuing Disability Reviews, which are basically another fraud control. You go back and recheck whether somebody is still disabled, because sometime people heal from a disability. But there is a backlog of 1.3 million CDRs, and you are proposing we try to take on some of that backlog. But maybe colleagues on both sides of the aisle could agree that we should accelerate the investment for those reviews.

Do we have a sense of whether those reviews primarily serve a preventive service, that is, people knowing that they will go through these reviews, it reduces even that small fraction of fraud? Or do we find people who have improved and they should be coming off the disability rolls and, therefore, there is a return on these reviews?

Ms. COLVIN. The CDRs are designed to do just that. When people come on the rolls, we know that some are likely to improve and some will not. For those that are likely to improve, we should go back within the time frame to review to see if there is improve-

ment. And when we do not, of course, they continue to get a check even though they may no longer be disabled. So that would be important.

Also, when we do the reviews, we may see some patterns that suggest that things are inappropriate that may allow us to see if there is fraudulent activity. I think that if you support the President's 2016 budget where he is asking for a dedicated program integrity budget, we would be able to do many of the things you are talking about. That 2016 budget will allow us to do 908,000 CDRs versus the 700 that we are doing this year or the 500 we did last year. So I would urge—

Senator MERKLEY. So I will do a summary statement because I am out of time. But I think you are saying if we invest in these two programs—the investigative units and the CDRs—we will even further improve the efficiency and appropriateness of this program. That is a win-win.

Ms. COLVIN. Absolutely.

Senator MERKLEY. Thank you.

Ms. COLVIN. Thank you, sir.

Chairman ENZI. Senator Baldwin?

Senator BALDWIN. Thank you, Mr. Chairman and Ranking Member Sanders. I appreciate the opportunity to be here to discuss an important social safety net that is available to all working Americans: Social Security Disability Insurance.

This program allows workers that have paid in with at least 5 years of work to be insured in the event that they become disabled, by disabling injury or illness or other condition.

Now, if the members of the Committee will indulge me, I would like to take a brief moment to brag about the program's proud origins in the State of Wisconsin. In the State of Wisconsin, we have something called "the Wisconsin Idea," which has actually come under attack in recent days by our Governor. But first articulated in 1904, the Wisconsin Idea states that the mission of the University of Wisconsin system is to solve problems and to improve people's lives beyond the classroom, essentially that academicians and government experts should work together to solve social problems.

It was in the spirit of the Wisconsin Idea that President Franklin Delano Roosevelt asked two Wisconsin professors, Arthur Altmeyer and Edwin Witte, to design the Social Security program and system.

Now, from the beginning, Altmeyer advocated for a disability insurance program, stating that it might eventually be of even greater need than old-age protection. But he was wary at the time of potential political attacks against such a program, so it took a little over two decades for Altmeyer's Disability Insurance program vision and dreams to actually be realized.

The program we have today is really due to that vision. However, I am very concerned by the politics that brings us to this hearing and this moment today, concerned that the Social Security Disability Insurance program has really come under attack by Republicans in the House who are putting up procedural obstacles to the way that we have sustained the viability of this program over many, many years and setting the stage actually for a battle over its future.

Ms. Colvin, the AARP and every major retirement advocacy group opposes this particular House Republican recent action, tactic regarding Social Security Disability Insurance Trust Fund because it puts the whole program at risk.

Can you tell me if it is true that the only two means available other than, of course, transferring money between the Social Security—or into the Social Security Disability Insurance Trust Fund—the only means available to restore solvency would be either drastic benefit cuts or raising revenues with policies like increasing the earnings cap?

Ms. COLVIN. Well, clearly, any change that you make is going to take some time. That is why the President put forth the reallocation proposal. We did not expect the type of reaction because this has been done 11 times in the past on a bipartisan basis. In fact, five of those times we transferred resources from DI to OASI. Clearly, any reform is going to require a combination of the things you have talked about, some changes perhaps to benefits and some changes to revenue. And there are many proposals out there that have been presented by many bipartisan groups as a matter of whether or not the country remains committed to providing this basic benefit for workers of this country.

Senator BALDWIN. But, obviously, if we were able to do the transfers that you describe, having been done 11 times before in both directions, we do not face the immediate issue of drastic cuts.

Ms. COLVIN. And then we can have a thoughtful discussion about what changes will occur and try to minimize the impact on those who receive those benefits. When the President put forth those six principles, it was designed to make certain that people would not be harmed as we looked at reforming the process.

Senator BALDWIN. You know, I appreciate my colleagues who have taken the time to share the stories of their constituents who have applied for and are eligible for and receive Social Security Disability Insurance benefits, because oftentimes we talk about them as a group rather than share their individual stories. But I think that if we find ourselves in the policy choice between either cutting benefits to the very most vulnerable in our society by some reports 20 percent, by your own testimony—

Ms. COLVIN. That is correct.

Senator BALDWIN. —20 percent or asking the wealthiest 6 percent in this country to pay the same in Social Security taxes as poor and middle-class workers pay, I know which side I am on.

Chairman ENZI. Senator Ayotte.

Senator AYOTTE. I want to thank the Chairman, and I want to thank you the witness for being here today. As I hear about 11 years of transfers, whether it is from the Old-Age Fund to the Disability Fund and obviously the immediate issue facing us in 2016, we have been here before since 1994 when we transferred money from Old-Age to Disability with the goal of buying time to fix the program. So we have been doing this for about 20 years with the same problem. We know what the problem is.

And so how do we avoid getting back in the same position next year, and the year, after that where we are kicking the can? How do we avoid that? Because it seems to me we owe the people who really need this fund, and it is important to them that we actually

try to solve the long-term viability of it. And we have got the long-term viability of the Old-Age Fund, as well. It is wonderful to get six principles from the President, but I would also love to know what he would support in terms of concrete reforms so we can work together.

Ms. COLVIN. Well, certainly I think it is going to be incumbent that Congress sit down and look at the various proposals that are out there and determine which ones you can support. This proposal that is before us now is to give you the time to be able to do that.

Senator AYOTTE. See, but here is what I am struggling with: We have had so much time on this. We would love to see concrete proposals from the administration. I know that Senator Baldwin referred to a proposal in the House, but what is it the administration could support that, rather than just a transfer, would actually reform and preserve the programs so that we can work together to figure out on a bipartisan basis how we are preserving this for the long term, and we are not having Groundhog Day again? If we went back to 1994, I bet you there were Senators asking the same question as me here. Can you help me with that? Does the administration have a plan to submit to us that we could look at some concrete proposals that they might support?

Ms. COLVIN. I can only speak today to the proposal that is before you, which is the President's 2016 budget which sets for the reallocation plan as well as numerous legislative proposals and some demonstration proposals, et cetera, and I think you have those. I can certainly walk through those if you wish.

Senator AYOTTE. I do. I understand reallocation, but I think that is just basically robbing Peter to pay Paul. Let us not kid ourselves. And I hope that the administration will actually submit something concrete. If they do not like the House proposal, then let us hear what the proposals are that they would submit. And I hope other people are listening to this and would submit to us some ideas we can work on together.

I got to the hearing a little bit late, and I wanted to understand if you testified about the fact that we have seen, going back to 1994, a significant increase in the number of claims that the Disability Fund has to cover. Could you help me understand what you believe is driving that? And what do we have to look at in terms of a situation where we see an increasing number of claims, that obviously exacerbates the fiscal challenge that we face? All of us want to make sure that the people who really need this fund are able to access it. So, can you give me a sense of what we are facing?

Ms. COLVIN. Absolutely. The increase in the disability rolls during this period of time should not have been a surprise. It has been projected by the actuaries and the trustees of Social Security since 1995, and they were right on target. The primary reasons were the economic and demographic factors, the fact that the baby boomers were reaching the disability-prone years and would be, in fact, coming on to the disability rolls, the fact that more women were working and getting benefit on their own right. In fact, they are now on parity with men.

We knew that this was going to occur. I think the one area that may not have been fully projected was the recession, and so cer-

tainly people who were marginally employed, a number of those individuals came on our rolls.

If you look at data now, you see that those variables are becoming minimal, and so now the number of applications are less. The number has significantly decreased. And the actuaries I believe projected that decrease will continue to go down and level out, because now you have individuals who were in disability-prone years now going into retirement years. Most of your baby boomers will be going into the retirement pool. And, of course, the actuarial challenges are related to the fact that we have less workers paying into the system than when we first started this program.

So I do not think you should be surprised by the spike, and now, of course, we are pleased to see that that spike is decreasing, as was projected.

Senator AYOTTE. I know my time is up but there is one thing I do not understand, and perhaps you could help me with this. I understand the baby-boomer issue because it is, frankly, an issue we are facing in the Old-Age Fund, Medicare and many other programs. I understand the funding problem in terms of the recession, meaning number of people paying in. Maybe I misunderstood your testimony, but is there a relationship between when it is a recession more people go to disability, or were you just speaking to the funding issue? Because if that is a connection, I am curious why that connection would be there.

Ms. COLVIN. No, I think you have people who were marginally employed, they worked part-time, they may have situations where they are in and out of the job market, and they really try to hold on. During a recession you will see more of those people applying for disability, and they, in fact, meet our requirements. People want to work, and they try to work as long as they possibly can. But in some situations, they are just not able to. That is why you have provisions in the statute relative to substantial gainful activity. People who are disability rolls are allowed to earn a certain amount. We want to encourage that.

And so there is a correlation. We would be very happy to meet with you privately and share more information with you.

Senator AYOTTE. I would love more follow-up information for the record.

Ms. COLVIN. We would certainly love to do that.

Chairman ENZI. Thank you, Senator Ayotte.

That concludes the questions for the first panel this morning. Commissioner Colvin, thank you for agreeing to testify this morning. This is an important topic, and we are going to need to work together on a long-term solution to better serve our disabled. That prediction that is so accurate from 20 years ago must have understood every demographic change that was going to happen, and yet we did not take those factors into consideration to come up with a solution. So I am hoping that we do not just kick the can down the road. I am hoping that the President will take an active role in this. And one of the main reasons is, in 2033, we are not going to be able to do any transfer from Old-Age or the Disability Fund or the Medicare HI Fund, Part A. They are all going to be in the same shape come 2033, so a reallocation will not be possible. So I hope we do not kick the can down the road.

Thank you very much for testifying.

Senator SANDERS. Mr. Chairman, if I could, just very briefly, I think at the end of the day there is pretty clear agreement. I would hope that nobody here is going to be supportive of the 19-percent cut for some of the most vulnerable people in this country.

But also I think there is widespread recognition that w have a serious problem that has to be addressed. So my solution or suggestion is let us deal with this, let us do what the President said, let us do what has been done 11 times. Let us sit down and figure out how we do not kick the can down the road.

Chairman ENZI. Thank you.

The next panel, while we are setting up for the panel I will introduce the three witnesses who we are honored to have before the Committee this morning. We have talked about the problem. Now I am hoping we get the solutions.

First we will hear from Dr. Duggan. Dr. Duggan is the Wayne and Jodi Cooperman Professor of Economics at Stanford University and a leading expert on Federal disability programs. Prior to joining Stanford, Dr. Duggan held faculty positions at the University of Pennsylvania, the University of Maryland, and Harvard University. He also was an economist with President Obama's Council of Economic Advisers in 2009 and 2010. Dr. Duggan has written extensively on the causes of the rise in disability insurance over the last 30 years. Along with his co-author David Autor of Harvard University, he proposed reforming the disability system using front-end interventions focused on rehabilitation upon the onset of a disability to keep workers in the labor market.

Second, we will hear from Dr. de Jong, who is a professor of economics at the University of Amsterdam and managing partner at APE, a research firm in the Netherlands. He is an expert on European disability programs and is considered by many to be the father of disability reform in Holland. He has published widely on Social Security and disability insurance. He has also advised the European Union, the OECD, the World Bank, and many countries confronting disability issues.

Finally, we will hear from Ms. Lang. Ms. Lang is a staff attorney at the National Senior Citizens Law Center where she works on issues related to Social Security Disability Insurance and Supplemental Security Income. Prior to joining the National Senior Citizens Law Center, Ms. Lang was an attorney at the Legal Aid Bureau in Maryland and has worked for a variety of other legal services for low-income people. Ms. Lang has an undergraduate degree from Oberlin College, a law degree from Fordham University, and a master's degree in teaching English to speakers of other languages from the University of Pennsylvania.

For the information of colleagues, each witness will take 5 minutes for their opening statements followed by questions.

Dr. Duggan, please begin.

**STATEMENT OF MARK G. DUGGAN, THE WAYNE AND JODI COOPERMAN PROFESSOR OF ECONOMICS, STANFORD UNIVERSITY**

Mr. DUGGAN. Chairman Enzi, Ranking Member Sanders, and members of the Committee, it is truly an honor to be here with you here today.

The Social Security Disability Insurance program currently provides insurance against the risk of disability to more than 151 million American adults. The program represents an extremely important part of our Nation's safety net as it protects workers and their families from the risk of a disability that prevents or greatly inhibits a person's ability to work.

Nearly 9 million adults received SSDI disabled worker benefits in December 2014. SSDI expenditures currently exceed program revenues by 26 percent, and as a result the program's trust fund is rapidly being depleted. Current projections from the OASDI Trustees suggest that the trust fund will reach zero in late 2016.

As shown in Figure 1 of my written testimony, enrollment in the SSDI program has grown steadily since the late 1980s, from 2.3 percent of adults aged 25 to 64 in 1989 to 5.0 percent in 2013. In my testimony today, I will briefly summarize the factors that are responsible for this growth, and in my written testimony, I also outline the implications of this growth for the U.S. labor market and discuss some prospects for reform of the SSDI program.

One contributor, as has been discussed already today, to the growth in SSDI enrollment has been the aging of the baby-boom generation. Individuals in their fifties and early sixties are significantly more likely to receive SSDI benefits than their counterparts in their thirties and forties. However, there has also been a significant increase within age groups during this time period.

Consider individuals in their fifties. In 1989, 4.3 percent of adults in this age group were receiving SSDI benefits. By 2013, this had almost doubled to 8.3 percent. The increase was also substantial for people in their early sixties or for adults from 25 to 49. Because of these age-specific increases, the aging of the population explains only about one-fifth of the increase in SSDI enrollment from 2.3 percent to 5.0 percent. Put another way, if age-specific rates of SSDI enrollment had not changed over this time period, SSDI enrollment would have grown from 2.3 to 2.8 percent, not to 5.0 percent.

Another factor, as has been mentioned, is the increase in the fraction of women who are insured for the program. From 1989 to 2013, the fraction of women 25 to 64 insured for the program increased from 66 to 75 percent. Taking account of this factor can explain another 12 percent of the growth in SSDI enrollment. So about one-third of the growth in SSDI enrollment from 1989 to 2013 as a fraction of the population is attributable to these two factors.

Another important determinant of the growth in SSDI enrollment since the 1980s, based on my own previous research with David Autor and others, is the liberalization of the program's medical eligibility criteria that occurred in the mid-1980s. As shown in Figure 2, there has been a substantial increase in award rates for diseases of the musculoskeletal system and mental disorders, while

award rates for neoplasms and circulatory conditions have remained roughly constant. This shift is important because, as shown in recent research, the employment potential of individuals with these sometimes more subjective conditions is substantial, and it is often somewhat difficult to verify the severity.

A fourth contributor to the rise in SSDI enrollment has been the reduction in the generosity of OASI retired worker benefits. As a result of legislation passed in 1983, the fraction of full benefits that a worker can receive at age 62 if they claim retirement benefits has fallen from 80 to 70 percent, and as a result, the ratio of SSDI benefits to those early benefits is growing from 25 percent higher to 43 percent higher. Some of my own previous research shows that this has resulted in an increase in SSDI enrollment.

Another important driver of the rise in SSDI enrollment is the sensitivity of the program to economic conditions. As shown in Figure 3 of my testimony, applications to the program are highly responsive to the unemployment rate, with applications rising substantially during economic downturns and falling when the economy improves. Previous research has shown that individuals who lose their job or who are unable to find a new job are more likely to exit the labor force and apply for SSDI benefits. This is troubling when one considers the low exit rate from the program back into the labor force.

There have been other factors that have contributed as well to the rise in SSDI enrollment, including changes in replacement rate and other factors that I outline in my written testimony. The steady rise in SSDI enrollment, though, has started to slow down over the last couple of years, and I talk more about that in my written testimony.

While providing valuable insurance to tens of millions of Americans, the SSDI program reduces the incentive to work both for individuals on the program and those applying for SSDI benefits. The growth in the program has coincided with a substantial reduction in employment rates among individuals with disabilities. For example, from 1988 to 2008, the employment rate of men in their forties and fifties who reported a work-limiting disability fell by 12 percentage points.

One way to improve incentives in the SSDI program is to intervene sooner for individuals with work-limiting conditions so that they can continue working, and we have talked a bit—this has already been discussed somewhat here today.

The payoff to keeping a potential SSDI applicant in the workforce is very high given that the average present value of an SSDI award is in the neighborhood of $300,000.

Increasing employment among individuals with disabilities could improve their economic well-being and increase their autonomy while also reducing the fiscal strains on the Social Security program.

Sorry I ran over.

[The prepared statement of Mr. Duggan follows:]

**Testimony before the United States Senate**

**Committee on the Budget**

February 11, 2015

Mark G. Duggan

The Wayne and Jodi Cooperman Professor of Economics

Stanford University

Chairman Enzi, Ranking Member Sanders, and members of the Committee, it is truly an honor to be here with you today. The Social Security Disability Insurance (SSDI) program currently provides insurance against the risk of disability to more than 151 million American adults. This program represents an extremely important part of our nation's safety net as it protects workers and their families from the risk of a disability that prevents or greatly inhibits a person's ability to work.

Nearly 9 million adults received SSDI disabled worker benefits in December 2014 and total program expenditures exceeded $145 billion in the 2014 calendar year. SSDI recipients also receive health insurance through the Medicare program (after two years from onset of disability), with those costs financed by Medicare. SSDI expenditures currently exceed program revenues by 26 percent and as a result the program's trust fund is rapidly being depleted, having fallen from $215 billion at the end of 2007 to $60 billion in December 2014.[1] Current projections from the OASDI Trustees' suggest that the SSDI trust fund will decline to zero in late 2016.

As shown in Figure 1, enrollment in the SSDI program has grown steadily since the late 1980s, from 2.3 percent of adults aged 25-64 in 1989 to 5.0 percent by 2013. This increase has coincided with a reduction in employment rates among individuals with disabilities (Autor and Duggan, 2010). In my testimony today, I will briefly summarize the factors that are responsible for this growth. A large body of recent research demonstrates that changing financial incentives have

[1] The ratio of SSDI trust fund assets to program expenditures fell from 2.2 to 0.4 during that period.

played an important role in the growth of SSDI enrollment. I will then outline the implications of this growth for the U.S. labor market. Finally, I will conclude by discussing the potential for changes to the SSDI program to increase employment and improve economic well-being among individuals with disabilities while also reducing the fiscal burden of the program.

*Why Has SSDI Enrollment Increased?*

One contributor to the growth in SSDI enrollment has been the aging of the baby boom generation. Individuals in their fifties and early sixties are significantly more likely to receive SSDI benefits than their counterparts in their thirties and forties. However, as the following table demonstrates, the percentage of adults receiving SSDI has risen sharply even within age groups.

| Age Group | % of Adults on SSDI | | % of Men on SSDI | | % of Women on SSDI | |
|---|---|---|---|---|---|---|
| | 1989 | 2013 | 1989 | 2013 | 1989 | 2013 |
| 25-39 | 0.8% | 1.4% | 1.1% | 1.5% | 0.5% | 1.3% |
| 40-49 | 1.9% | 3.7% | 2.5% | 3.8% | 1.2% | 3.6% |
| 50-59 | 4.3% | 8.3% | 5.8% | 8.8% | 2.9% | 7.9% |
| 60-64 | 7.8% | 13.0% | 11.0% | 14.4% | 5.0% | 11.8% |
| 25-64 | 2.3% | 5.0% | 3.0% | 5.3% | 1.5% | 4.8% |

Consider individuals between the ages of 50 and 59. In 1989, 1 out of 23 adults in this age group was receiving SSDI benefits. But by 2013, this had almost doubled to 1 in 12. The increase was similarly dramatic for adults in their forties and also substantial for adults in their early sixties and those between the ages of 25 and 39. Because of these age-specific increases, the aging of the population explains less than one-fifth of the increase in SSDI enrollment from 2.3 percent to 5.0 percent during the 1989 to 2013 time period. Put another way, if age-specific rates of SSDI enrollment had remained unchanged from 1989 to 2013, the percentage of adults aged 25 to 64 on SSDI would have increased from 2.3 percent to 2.8 percent.

To be insured for SSDI benefits, a person must have worked in at least five of the ten most recent years. Because employment rates have increased among women since the 1980s, the fraction

of women aged 25 to 64 insured for the program has risen as well, from 66 percent to 75 percent during the 1989 to 2013 period. This has also contributed to enrollment growth in the SSDI program and partially explains why SSDI has grown more rapidly among women than among men during this time period. But this factor explains just 12 percent of the rise in SSDI enrollment. Taken together, the aging of the baby boom population and changes in the fraction of adults insured for SSDI can explain only about one-third of the growth in the program depicted in Figure 1 from 1989 to 2013.

A much more important determinant of the growth in SSDI enrollment since the 1980s is the liberalization of the program's medical eligibility criteria that occurred in the mid-1980s (Duggan and Imberman, 2009). As shown in Figure 2, there has been a dramatic increase in award rates for mental disorders and diseases of the musculoskeletal system (e.g. back pain). In contrast, award rates for neoplasms (cancer) and circulatory conditions (e.g. heart attack, stroke) have remained roughly constant. This shift is important because, as shown in recent research (von Wachter et al, 2011), the employment potential of SSDI applicants with these more subjective conditions is substantial and it is often difficult to verify the severity of these conditions (in contrast to cancer or heart conditions).

A fourth contributor to the rise in SSDI enrollment has been the reduction in the generosity of OASI retired worker benefits. Individuals born in 1937 or earlier could receive 80 percent of their full retirement benefit if they claimed retired worker benefits at the age of 62. But as a result of legislation passed in 1983, this has gradually fallen to 75 percent for individuals born from 1943 to 1954 and will soon fall to 70 percent for individuals born in 1960 or later (with an associated increase in the full retirement age from 65 to 67 as well). No corresponding changes were made to SSDI benefits and thus SSDI has become relatively more attractive financially. More specifically, SSDI benefits were 25 percent more generous than retirement benefits at age 62 for those born in 1937 or earlier but will be 43 percent more generous for those born in 1960 or later. Previous research demonstrates that the falling generosity of retired worker benefits has induced a substantial

number of adults to apply for and ultimately receive SSDI, and that this explains approximately one-fourth of the growth in SSDI enrollment since the late 1980s (Duggan et al, 2007).

Another important driver of the growth in SSDI enrollment is the sensitivity of the program to economic conditions. As shown in Figure 3, applications to the SSDI program are highly responsive to the unemployment rate, with applications rising substantially during economic downturns and falling when the economy improves. Previous research has shown that the SSDI program has become much more sensitive to economic conditions since the early 1980s and that individuals who lose their job or who are unable to find a new job are increasingly likely to exit the labor force and apply for SSDI benefits. Thus the program is to some extent serving as a form of long-term unemployment insurance for some workers, which is troubling when one considers the low exit rate from the program back into the labor force.

A sixth contributor to the growth in SSDI enrollment is the rise in replacement rates for the typical low-skilled worker, which is caused by the interaction of two factors (Autor and Duggan, 2003). First, SSDI (like OASI) uses a progressive 90-32-15 benefit formula with "bend points" that increase each year with average earnings growth. Second, earnings for low-income workers have grown more slowly than the average, and as a result workers replace an increasing fraction of their earnings at a 90 percent rate rather than a 32 percent rate. This has increased the financial incentive to apply for SSDI benefits and subsequently the enrollment in the program.[2]

Other factors have also contributed to the steady rise in SSDI enrollment since the late 1980s. Individuals who are initially rejected when they apply for SSDI have become more likely to appeal those decisions and are increasingly likely to be represented by a lawyer or other professional

[2] Additionally because wages for low-skilled workers have grown more slowly than the average, their average indexed monthly earnings tend to be higher than current earnings. This has further increased the ratio of potential SSDI benefits to potential earnings.

if/when they ultimately appear before an administrative law judge.[3] Meanwhile, the fraction of recipients receiving a continuing disability review and exiting the program for no longer meeting SSDI's medical eligibility criteria has also declined.

The steady rise in SSDI enrollment shown in Figure 1 has started to slow down over the last couple of years. While age-specific enrollment data are not yet available for 2014, total SSDI enrollment increased by just 0.1 percent from December 2013 to December 2014. This is partly because the effect of an aging population has now "run its course", with the oldest members of the baby boom cohort reaching Social Security's full retirement age (and thus converting to retired worker benefits). Additionally, the fraction of applications resulting in an SSDI award has been declining, with the ratio of awards to applications in 2013 at its lowest level since 1982.[4] Third, the fraction of individuals insured for SSDI benefits has been steadily declining (or growing more slowly) in recent years. To be eligible for SSDI, an individual must have worked in at least five of the ten most recent years. For example, the share of men in their forties insured for SSDI fell from 90.3 percent in 2000 to 85.2 percent in 2014, and this will mechanically reduce inflows to the program. And finally, the improving labor market has – as shown in Figure 3 – resulted in fewer SSDI applications and thus a lower flow of new recipients into the program.

*Labor Market Effects of the Rise in SSDI Enrollment*

While providing valuable insurance to tens of millions of Americans, the SSDI program reduces the incentive to work both for individuals on the program and also for those applying for SSDI benefits. In order to receive an SSDI award, a beneficiary must be deemed unable to engage in

[3] In the average year from 2000 to 2008, administrative law judges made awards in 72 percent of their decisions (SSA, 2012). This is striking when one considers that ALJs consider appeals only among those rejected twice previously by SSA. One potential contributor to the high award rate is that SSA is not represented at the hearing – only the applicant and/or his/her representative are typically present with the ALJ (Autor and Duggan, 2006).

[4] This is not a perfect measure because awards in one year may result from applications in previous years. However, because of the lag in the appeals process, it is not yet possible to obtain final data for 2010 or later applications. The most recent data from SSA's Annual Report on the SSDI program suggests that the decline in ALJ award rates is the most important factor in this change.

substantial gainful activity (SGA, currently $1,090 per month). Once on the program, an SSDI recipient has little incentive to return to work, as earnings above the SGA threshold will lead to a termination of benefits. Given that the present value of the average SSDI award is about $300,000 (including Medicare benefits), that is a risk that many SSDI recipients would be reluctant to take (Autor and Duggan, 2006).

The growth in SSDI enrollment has coincided with a substantial reduction in employment rates among individuals with disabilities. For example, from 1988 to 2008, the employment rate of men in their forties and fifties who reported a work-limiting disability fell from 28 percent to 16 percent while the corresponding rate for men without a disability rose slightly from 87 to 88 percent (Autor and Duggan, 2010).

Previous research has shown that workers have become increasingly likely to respond to adverse labor demand shocks by applying for SSDI rather than seeking a new job (Autor and Duggan, 2003). This serves to reduce both the unemployment rate and the labor force participation rate below what it otherwise would be. It also reduces the eventual employment rate as SSDI recipients rarely leave the program to return to the workforce. For example in 2013, only 0.7 percent (7 out of 1,000) of SSDI recipients left the program for improving health and/or to return to work.

This responsiveness of the SSDI program to economic conditions can be seen visually in Figure 3, with increases in the unemployment rate leading to large increases in the SSDI application rate. My analysis of this application data reveals that there have been approximately 2.5 million "extra" SSDI applications since 2008 as a result of the economic downturn, with the application rate declining with the unemployment rate during the past few years. Many of these applicants have withdrawn from the labor force, either because they have been awarded SSDI benefits or are still in the process of applying given the long lags in the process (especially at the appeal stage). Still others have likely withdrawn because their attachment to the labor force has declined during the application process (even if ultimately denied) and thus their potential wages as well.

The steady increase in SSDI enrollment since the late 1980s has contributed to a differential decline in labor force participation among both men and women in the U.S. relative to other industrialized countries. For example, the labor force participation rate declined by 4.7 percentage points (from 93.4% to 88.7%) among men 25-54 in the U.S. during the 1990 to 2011 period while falling just 1.5 percentage points (from 93.6% to 92.1%) among the EU-15 (OECD, 2013).[5] Similarly while the labor force participation rate was almost unchanged among women 25-54 in the U.S. from 1990 to 2011 (rising slightly from 74.0% to 74.7%), it increased by 14.8 percentage points (from 63.7% to 78.5%) among women in the EU-15 during this same period. Thus labor force participation rates for both men and women in the 25-54 age range were in 2011 substantially higher in the EU-15 than in the U.S.[6] While there are of course many factors that influence both the level and the trend in labor force participation, previous research indicates that SSDI program is an important factor (Autor and Duggan, 2003; Maestas et al, 2013; French and Song, 2014).

*Improving Work Incentives in the SSDI Program*

The disability determination process that is currently used by the SSDI program awards benefits to individuals who are deemed unable to engage in substantial gainful activity. This reduces the incentive to work among those who have filed an initial application for SSDI and among those appealing a rejection. Approximately 40 percent of SSDI awards are now made on appeal and the time between the initial application and the ultimate decision is very long for this group. For example, the average lag for an applicant who appeals to an Administrative Law Judge (ALJ) is 27 months (SSA, 2008). This is problematic because those initially rejected are likely to be in better health on average than those receiving an initial award, and thus likely to have higher employment

[5] These differences are even larger when focusing on men between the ages of 25 and 64 and are somewhat smaller when restricting attention to the 1990 to 2008 period. Declines in labor force participation among men aged 25-54 were also much lower in Australia, Canada, and Japan than in the U.S. during this same period.
[6] The labor force participation rate for men in the U.S. aged 25 to 54 declined further to 88.4 percent by 2013 and for women in this same age range fell to 73.9 percent.

potential. And the longer that a person remains out of the workforce, the more their earnings potential declines. Therefore even if an applicant never receives an SSDI award, the program's application process can permanently harm his/her employment prospects (Autor et al, 2015).

One way to improve incentives in the SSDI program is to intervene sooner for individuals with work-limiting conditions so that they can continue working. Many individuals with more subjective disorders – such as back pain – could benefit from such early intervention. In a recent paper, David Autor and I proposed adding a "front end" to the SSDI system that would include early intervention through rehabilitation and related services with the goal of keeping workers with work-limiting disabilities in the labor market (Autor and Duggan, 2010). Employers would contract with private insurers to administer this coverage and would have a financial incentive to keep their workers off the SSDI system (much as the Unemployment Insurance and Workers' Compensation programs provide employers with these types of financial incentives).

The payoff to keeping a potential SSDI applicant in the workforce is very high. The average present value of an SSDI award (including Medicare expenditures) is approximately $300,000. Additionally, to the extent that the program reduces employment, it also reduces tax revenue and GDP. While many awarded SSDI benefits are completely unable to work, previous research makes clear that a large fraction could work (Autor and Duggan, 2003; Burkhauser and Daly, 2011; von Wacther et al, 2011; Maestas, Mullen, and Strand 2013; French and Song, 2014).

Increasing employment among individuals with disabilities could improve their economic well-being and increase their autonomy while also reducing the fiscal strains on Social Security. Past efforts to achieve this goal have unfortunately had little impact. For example, the Ticket to Work program, which was authorized by Congress in 1999, allowed SSDI recipients to have a trial work period of 9 months during which they could retain their benefits. But takeup of the program was close to zero, perhaps because these incentives arrived too late after most SSDI recipients had been out of the labor force for years. Recent efforts to increase work incentives among disability insurance

recipients have had some success in other countries (see Kostol and Mogstad, 2014 for evidence in Norway) and thus modifications to the Ticket-to-Work approach may have a higher payoff.

There are other potential reforms that could improve the functioning of the SSDI program. For example, currently only the applicant and his/her representative are present at appeal hearings before ALJs. Thus SSA does not have someone present explaining why they rejected the application twice and this may partially explain why about 70 percent of those initial decisions that appeal a second time are overturned by ALJs. Additionally, there has been a substantial decline in recent years in the share of SSDI recipients receiving a continuing disability review (CDR) with this partially explaining the lower exit rate from the program (SSAB, 2012). Careful consideration of the appropriateness of the program's medical eligibility criteria also seems warranted given the major shift in the conditions with which individuals qualify for SSDI benefits as shown in Figure 2. And to the extent that economic (rather than only health) factors are considered when making an SSDI award, one could consider a form of time limit or a mandatory CDR for certain awardees.

The lack of progress in improving work incentives in the SSDI program stands in marked contrast to the Temporary Assistance to Needy Families (TANF) program. Reforms introduced in the 1990s (along with expansions in the Earned Income Tax Credit) led to substantial gains in employment among past, current, and potential future TANF recipients and to a steady drop in program enrollment and expenditures. Based on my own research and that of many others, I believe that similar progress is possible within the SSDI program. The timing for such reform may also be better than ever before given the pending expiration of the program's trust fund and the improving employment prospects for U.S. workers.

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**Figure 1: % of Adults 25-64 Receiving SSDI Disabled Worker Benefits: 1957-2013**

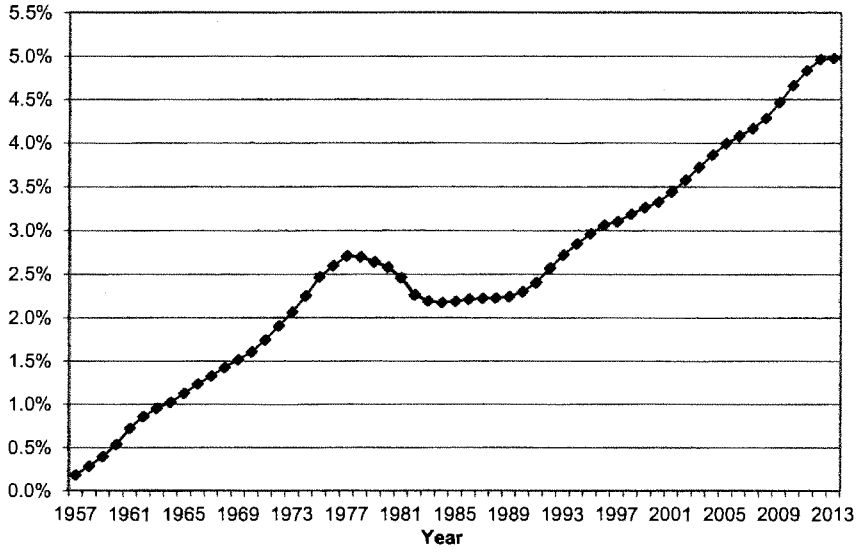


**Figure 2: Awards per 1000 Insured for SSDI by Diagnosis Category in 1983, 1989, 1999, 2009**

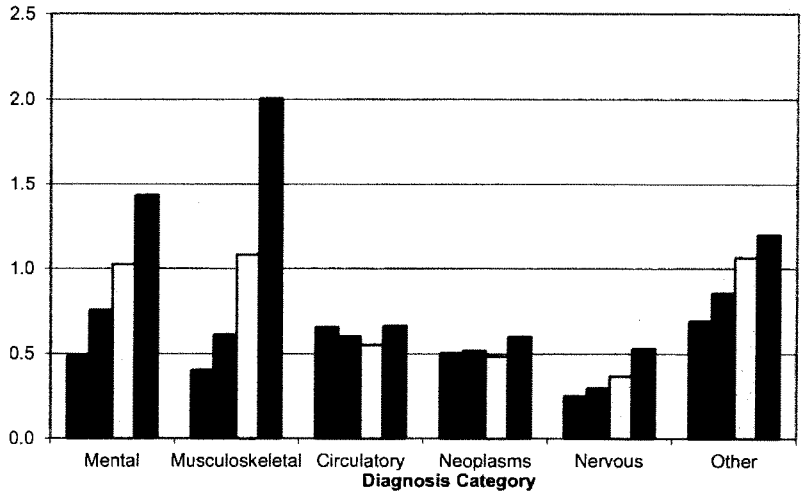
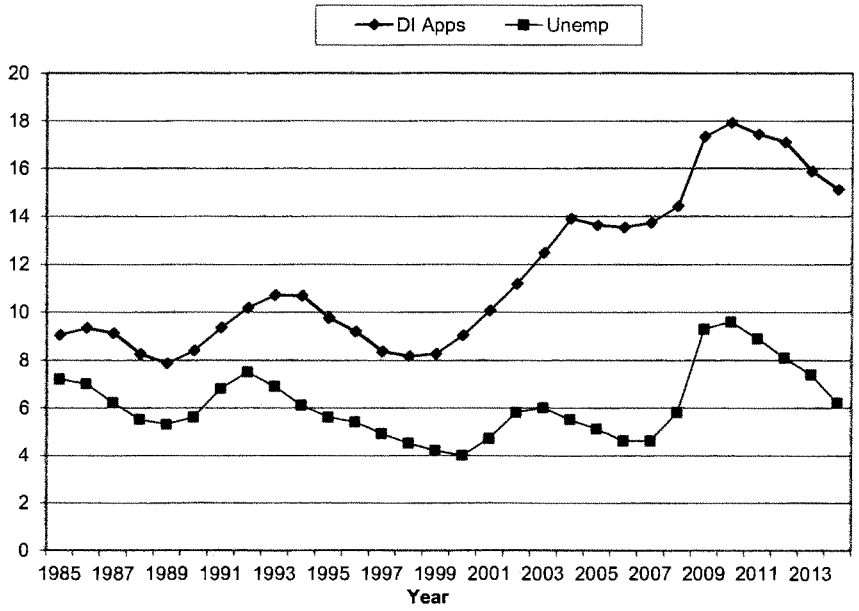


**Figure 3: SSDI Applications per 1000 Insured Workers and Unemployment Rate**



Chairman ENZI. Dr. de Jong?

**STATEMENT OF PHILIP R. DE JONG, PROFESSOR OF ECONOMICS, UNIVERSITY OF AMSTERDAM - AMSTERDAM SCHOOL OF ECONOMICS**

Mr. de Jong. Thank you, Mr. Chairman. It is an honor for me as a Dutchman to address your Committee, but it also restricts myself. I come from a country where the minimum wage, the legal minimum wage is at the level of $1,200 per month, the same as the average benefit, even under the current euro-dollar transfer rates.

Moreover, I come from a country which is not bipartisan, where governments are tripartisan coalitions or even quadripartisan. So what I learned here this morning is a lot about U.S. politics, and I am sorry to say much less about the solutions of the dooming problems with funding disability benefits. A lot of the discussions were about funding and much less, with a few exceptions, about the system. What I present is a system change, and I am sorry to have to use the word which you made use of, privatization, and especially strong incentives for employers, engaging employers. But the principle was focus on capacity, not on incapacity, and that is something which may be changed if you look at the SSDI system. But I feel somewhat awkward to suggest as a foreigner things to your political program.

Anyway, let me start with my testimony. Disability benefit schemes are often used as a provision to accommodate social change and cyclical ups and downs, as Mark just has evidenced. In the Netherlands, the DI scheme supported structural change towards a service-oriented economy, and it mollified the transition of Dutch households from a traditional single breadwinner type to a modern dual-earner family.

Similar uses of disability benefit schemes could be seen in Eastern Europe to soften the pains of transition to a market economy in the 1990s. In the U.S., too, the pronounced positive relationship between the national unemployment rate and the SSDI application rate shows that SSDI works as an alternative, and more generous, unemployment scheme. It is one of the factors that caused secular growth in the U.S. number of disability benefits, as Mark Duggan just explained.

The drawback of using disability benefits as a "soft" unemployment scheme is that it hides the lack of targeted, more cost-effective provisions and postpones their introduction. Meanwhile, huge unfunded financial liabilities are created given the long average duration of disability benefit dependency. The Dutch case is a good illustration both of the size of such liabilities and of the long political road it took to change an entitlement-oriented disability policy into an employment-oriented one.

To give you an example, in 1990 there was no country in the world that had more disability beneficiaries per 100 workers than the Netherlands. Twelve percent of the labor force was on disability, and the entry rate into disability was 2 percent; 2 per 100 went each year on disability.

Under pressure, like which was discussed here, of an aging workforce, the Dutch Government took a series of steps, in fact, from

1994 onwards. Their success fluctuated, but as of 2002 the steps taken were successful in bringing down DI awards, so the entries, by 60 percent. I have a figure in my written testimony to show that.

The major element causing the drop in DI inflow is early intervention, fueled by strong financial incentives for firms. In my introduction by the Chairman, he mentioned that I am a partner in a consultancy, so I am an employer myself, so I know—I am experienced in what it means to pay—to finance sickness benefits oneself, because that is an important part of what the Dutch did. All Dutch firms are obliged to pay for sickness benefits themselves, for rehabilitation, for accommodation, and for job mediation during the first 2 years of disablement. And those 2 years are also the mandatory waiting time before you can be awarded a long-term disability benefit, which is a public program. So that means that the coverage, the income protection of the first 2 years of disablement is fully privatized. Of course, it is based on legal mandates, but firms have to provide for it themselves. And, of course, they can insure against it, and small firms have to insure against such a liability. But they are completely free to do that.

Moreover, disability benefits, so after 2 years when you are assessed, when you put in a claim and you are awarded a disability benefit, these are financed by contributions that are experience rated at the level of the individual firm. That means that Dutch firms pay substantially higher rates if one or more of their employees enter the disability benefit, the Dutch disability benefit scheme.

Dutch workers also face stronger incentives. Although sickness benefits replace about 85 percent of wages, with a cap, but with a very high cap of about 50,000 euros per year, the DI benefits are lower and such that they make work pay if someone has a residual earning capacity that is more than 20 percent of his previous earnings. I have to explain to you that disability under the Dutch law, under the Dutch disability insurance law, is defined in terms of earning capacity, so in terms of money. So you compare what you still can earn with your limitations with what you used to earn before you became disabled. And that earning capacity loss, that is what is insured, what is covered.

DI benefits are lower—if such partially disability benefits—so there is within the disability benefit system in Holland a possibility to get partial benefits, which work, in fact, as a wage subsidy. But if partially disabled workers do not use their residual capacity, they get a much lower benefit. So there is a strong incentive to use as much as you can of your residual capacity.

From 2004 more stringent eligibility standards apply, and these standards are strictly administered, which is also important, by the DI program administrators because you can put stringent things in law but they have to be administrated as well, and that also calls for attention for incentives for administrators. The denial rate is about 45 percent and went up and down with the cyclical conditions. So it turned out to be robust against the business cycle. Of course, applications also in Holland go up under adverse economic conditions. But at the same time, denial rates also went up, so keep entries at a stable level.

Reforming a benefit program creates the issue of what to do with the current beneficiary population, and I think this is unheard of in the U.S. Between October 2004 and December 2007, all 300,000 DI beneficiaries younger than 45 were reassessed under stricter standards, so during the game you change the rules, which is—I think would be here very controversial. Anyway, 39 percent of the benefits were terminated or reduced, and among this group about 60 percent were working 3 years after their benefit status was reviewed and they lost the benefit of part of their benefits. But this is the only thing you can do to do something about this unfunded liability; otherwise, you have inheritance of a lot of people on disability who may be able to work, while your Continuing Disability Reviews may take care of that, that I do not know.

Chairman ENZI. Can I ask you to kind of wrap that up?

Mr. de Jong. Yes, yes.

Chairman ENZI. We will have a lot more questions.

Mr. de Jong. The reformed Dutch disability scheme purports to cover only those that have hardly any productive capacity left and to provide other workers with disabilities with strong incentives to remain active. The results for the first 9 years of the operation of the new scheme show that inflow rates have dropped substantially to levels that are reasonable by international standards and showed to be robust against the deep recession of 2008–13. The incentive structure that steers the behavior of employers and long-term sick workers proves to work.

Thank you.

[The prepared statement of Mr. de Jong follows:]

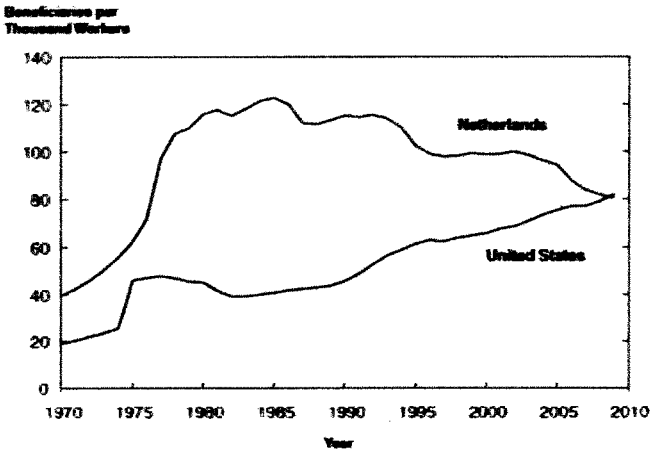
## Testimony before the U.S. Senate Budget Committee

**Philip R. de Jong, University of Amsterdam and APE**
February 11, 2015

Disability benefit schemes are often used as a provision to accommodate social change, and cyclical ups and downs. In the Netherlands, the DI scheme supported structural change towards a service-oriented economy and it mollified the transition of Dutch households from a traditional single breadwinner type to a modern dual earner family. Similar uses of disability benefit schemes could be seen in Eastern Europe to soften the pains of transition to a market economy in the 90s. In the U.S., too, the pronounced positive relationship between the national unemployment rate and the SSDI application rate shows that SSDI works as an alternative, and more generous, unemployment scheme. It is one of the factors that caused secular growth in the U.S. number of disability benefits.

*Figure 1*

**U.S. SSDI and SSI-Disabled Beneficiaries and Dutch Disability Beneficiaries per Thousand Workers Ages Fifteen to Sixty-Four over Time**

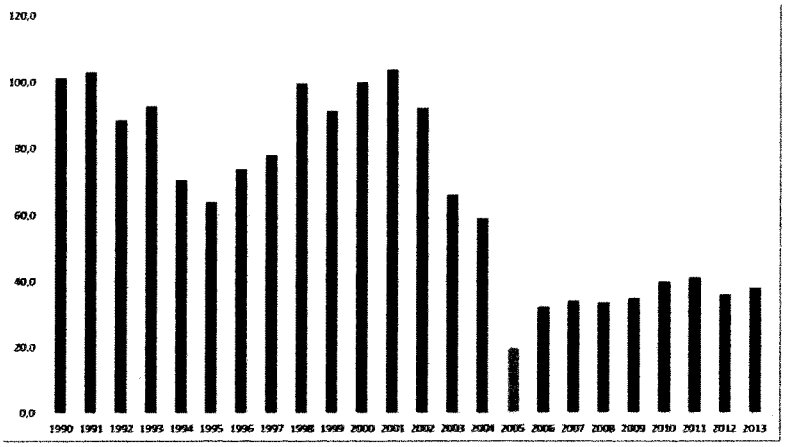



Source: Richard V. Burkhauser and Mary C. Daly, *The Declining Work and Welfare of People with Disabilities*. The AEI Press, 2011.

The drawback of using disability benefits as a 'soft' unemployment scheme is that it hides the lack of targeted, more cost-effective, provisions, and postpones their introduction. Meanwhile, huge unfunded financial liabilities are created given the

long average duration of disability benefit dependency. The Dutch case is a good illustration both of the size of such liabilities and of the long political road it took to change an entitlement oriented disability policy into an employment oriented one.

*Figure 2: Number of Dutch DI awards, 1990-2013*




Under pressure of an ageing workforce the Dutch government took a series of steps from 2002 onwards. These were successful in bringing down DI awards by 60% between 2002 and 2012 (see Figure 2).

***Financial incentives for firms***

The major element causing the drop in DI-inflow is early intervention (before DI application), fuelled by strong financial incentives for firms. All Dutch firms are obliged to pay for sickness benefits, rehabilitation, accommodation, job mediation during the first two years of disablement (before DI application). Moreover, DI benefits are financed by contributions that are experience rated at the level of the firm. This means that Dutch firms pay substantially higher rates if one or more of their employees enter the DI scheme.

***Financial incentives for workers***

Dutch workers also face stronger incentives. Although sickness benefits replace about 85% of wages, the DI benefits are lower and such that they make work pay if someone has a residual earning capacity that is more than 20% of his previous earnings. If such partially disabled workers do not use their residual capacity they get a much lower benefit.

From 2004 more stringent eligibility standards apply, and these standards are strictly administered by the DI program administrators. The denial rate is about 45%, and proves robust against cyclical variations in applications. Denied applicants can rely on UI benefits for a limited period. About 10% of those denied a benefit re-apply later.

Reforming a benefit program creates the issue of what to do with the current beneficiary population. Between October 2004 and December 2007 all (300,000) WAO beneficiaries younger than 45 were re-assessed using the stricter standards. 39% of the benefits were terminated or reduced, and among this group about 60% were working three years after their benefit status was reviewed.

The reformed Dutch DI scheme purports to cover only those that have hardly any productive capacity left, and to provide other workers with disabilities with strong incentives to remain active. The results for the first nine years of the operation of the new scheme show that inflow rates have dropped substantially to levels that are reasonable by international standards, and showed to be robust against the deep recession of 2008-2013. The incentive structure that steers the behaviour of employers and long-term sick workers proves to work.

Chairman ENZI. Thank you very much.

Ms. Lang?

**STATEMENT OF KATE LANG, SENIOR STAFF ATTORNEY, NATIONAL SENIOR CITIZENS LAW CENTER**

Ms. LANG. Thank you, Chairman Enzi, Ranking Member Sanders, and Senator Perdue. My name is Kate Lang, and I am an attorney with the National Senior Citizens Law Center. Our principal mission is to protect the rights of low-income older adults.

I am also a co-chair of the Income Security Committee of the Leadership Council of Aging Organizations, or LCAO, a coalition of 72 national aging advocacy organizations that represent millions of older Americans. Members of the coalition include the AARP, the National Committee to Preserve Social Security and Medicare, and the National Council on Aging, among many others. And together we work to preserve and strengthen the well-being of America's older population.

The LCAO believes that Congress should preserve the disability benefits of millions of older Americans by reallocating the payroll taxes between Social Security's retirement fund and disability fund to equalize the solvency of the two funds and should do so without any cuts to Social Security coverage, eligibility, or benefits.

As we all age, we face an increasing risk of acquiring disabilities that may limit our ability to support ourselves through work and put us at great financial risk. Fortunately, nearly all Americans pay into our Social Security system, a system of earned benefits that protect workers and their families in the event of death, disability, and retirement. More than 9 out of 10 American workers are insured for benefits that can be a lifeline for their families in the event of a qualifying disability.

And I would like to take a moment today to tell you about one of those Americans, who is here with us today, in her green jacket. Darlene B. is a 60-year-old woman who

lives here in Washington, D.C. She worked for many years in a variety of jobs in Pennsylvania and here in the D.C. area, but several years ago, Ms. B.'s children, who are now 28 and 30, noticed that she was struggling with her memory. She thought it might be related to a brain tumor that had been uncovered in her teens, but she was, in fact, diagnosed with early-onset Alzheimer's in her fifties, and she was approved for disability benefits through Social Security's Compassionate Allowances programs.

Ms. B.'s life has changed a lot as a result of her health problems, especially now that her cancer has spread to her spine. She has to plan her activities for each day carefully, and she relies on her son to keep track of her appointments. He is also her representative payee and helps her manage the approximately $900 a month she receives.

Nearly all of her benefits go to pay rent and utilities, and she has had to cut back on her expenses now that her income is so limited. If her benefits were cut, she might not be able to afford to continue living in her apartment. And Ms. B. will face a benefit cut of about 20 percent, or $180 a month, if Congress does not act in the next 2 years.

The LCAO urges Congress to reallocate Social Security's payroll taxes to ensure continuation of benefits for Ms. B. and millions of older Americans with disabilities—and to do so without making any accompanying cuts to Social Security coverage, eligibility, or benefits.

So I would quickly like to wrap up with three points:

First, that most who receive Disability Insurance benefits are older adults, age 50 and older, so helping DI helps seniors. Seven in ten beneficiaries are age 50 and older, and three in ten are 60 and older. When disabled workers receive Disability Insurance benefits as they age into their retirement years, these benefits help to ensure that they will not fall into poverty in later years.

The increase in the full retirement age to 67 delays when disabled workers switch to receiving benefits from the retirement fund. And in December 2013, more than 450,000 people aged 65 and 66 received disability insurance benefits. That is over 5 percent of the disabled workers receiving disability benefits. Under the rules in place until 2003, they would have been receiving retirement benefits instead. This is just one example of how closely the retirement and disability components of Social Security are interwoven and how changes to one part impact the other.

Second, the need for reallocation has been expected for many years. When Congress last acted to reallocate payroll taxes in 1994, it was predicted that this action would need to be taken again in 2016. And this is primarily due to a rapid, but temporary, increase in the number of disabled beneficiaries as baby boomers passed through their fifties and early sixties, when the risk of disability is greatest.

Third, this present situation is nothing new. Congress has rebalanced payroll tax revenues between the two trust funds 11 times over the past 50 years, about equally in both directions. This is a traditional and usually noncontroversial step, and there should be nothing unusual or contentious in taking such a step now.

In closing, reallocation does not require any increase in tax rates and will maintain the solvency of the combined trust funds until 2033. One of the strengths of our Social Security system is its universality. Most Americans who rely on Social Security Disability Insurance are, in fact, older adults, and we reject any attempts to manufacture a crisis that pits older adults against people with disabilities.

Thank you. I welcome any questions.

[The prepared statement of Ms. Lang follows:]

NSCLC
National Senior Citizens Law Center
PROTECTING THE RIGHTS OF LOW-INCOME OLDER ADULTS

**Testimony Before the U.S. Senate Budget Committee**

**"The Coming Crisis: Social Security Disability Trust Fund Insolvency"**

Kate Lang, Esq.
Senior Staff Attorney
National Senior Citizens Law Center

February 11, 2015

Thank you, Chairman Enzi, Ranking Member Sanders, and Members of the Committee, for the invitation to appear before you today. My name is Kate Lang, and I am an attorney with the National Senior Citizens Law Center.[1] Our principal mission is to protect the rights of low-income older adults.

I am also a co-chair of the Income Security committee of the Leadership Council of Aging Organizations (LCAO).[2] The LCAO is a coalition of 72 national aging advocacy organizations that represent millions of older Americans. Members include the AARP, the National Committee to Preserve Social Security and Medicare, and the National Council on Aging, among many others.[3] Coalition members work together to preserve and strengthen the well-being of America's older population.

The LCAO believes that Congress should preserve the disability benefits of millions of older Americans by reallocating payroll taxes between Social Security's retirement trust fund and disability trust fund, to equalize the solvency of the two funds, and should do so without any cuts to Social Security coverage, eligbility or benefits.[4]

As we age, we all face an increasing risk of acquiring disabilities that may limit our ability to support ourselves through work and put us at great financial risk. Fortunately, nearly all Americans pay into Social Security, a system of earned benefits that protect workers and their families in the event of death, disability, and retirement. More than 9 out of 10 American workers are insured for benefits that can be a lifeline for their families in the event of a qualifying disability.[5] Insurance under Social Security is particularly important because the alternatives for many families are often extremely limited. Seven in 10 civilian workers have no access to long-term private disability insurance through their employer,[6] and many families have little to no savings to fall back on if a breadwinner experiences a significant disability.[7]

National Senior Citizen Law Center
www.nsclc.org
nsclc@nsclc.org
1444 Eye Street, NW Suite 1100
Washington, DC 20005
202-289-6976 - Fax 202-289-2274
3660 Wilshire Blvd, Suite 718
Los Angeles, CA 90010
213-639-0930 - Fax 213-550-0501
1330 Broadway, Suite 525
Oakland, CA 94612
510-663-1055 - Fax 510-663-1051

I'd like to tell you about one American receiving disability benefits.

Darlene B. is a 60 year old woman living in Washington, DC. She worked for many years; in fact, her first employer was the Social Security Administration, where her roles included assisting people applying for benefits. She also worked in the private sector in jobs as diverse as chauffeur and caseworker at an organization for survivors of domestic violence. Several years ago, Ms. B's children, who are now 28 and 30, noticed she was struggling with her memory. She thought it might be related to the brain cancer she had survived in the past, but she was in fact diagnosed with early-onset Alzheimer's. She was approved for disability insurance benefits through SSA's Compassionate Allowances program.[8]

Ms. B's life has changed a lot as a result of her health problems, especially now that her cancer has returned and spread to her spine. She has to plan her activities for each day carefully, and relies on her son to keep track of her appointments. He is also her representative payee and helps her manage the approximately $900 a month she receives in disability benefits.

Nearly all of Ms. B's disability insurance benefits go to rent and utilities, and she has had to cut back on expenses now that her income is so limited. If her disability benefits were cut, she might not be able to continue living in her apartment.

Unfortunately, Ms. B's benefits would be cut, by 20 percent or almost $180 per month, if Congress does not reallocate the payroll taxes between Social Security's retirement trust fund and disability trust fund, to equalize the solvency of the two funds.

The LCAO urges Congress to act expeditiously to reallocate Social Security's payroll taxes to ensure continuation of benefits for Ms. B and millions of older Americans with disabilities – and to do so without making any accompanying cuts to Social Security coverage, eligibility or benefits.

I would like to make three points about the Social Security disability program and the need for reallocation:

**First, a significant majority of those receiving Disability Insurance benefits are, in fact, older adults, age 50 and older – so helping DI helps seniors.**

The risk of disability rises with age. People are twice as likely to collect disability benefits at age 50 as at 40, and twice as likely at age 60 as at age 50.[9] Seven in ten beneficiaries are age 50 and older, and three in ten are age 60 and older.[10]

Although the population of those receiving disability insurance benefits is extremely varied, Ms. B's story above is in many ways illustrative of a "typical" beneficiary - in his

or her late 50s or early 60s and in poor health, living with one or more severe impairments, such as advanced cancers, end stage renal disease, multiple sclerosis, and serious mental illnesses.[11] Beneficiaries' death rates are at least three times higher than that of other people their age.[12] One in five male and one in six female beneficiaries die within five years of being found eligible for benefits.[13]

As Ms. B's story also illustrates, these benefits are a modest but vital source of income. When disabled workers receive Disability Insurance benefits as they age into their retirement years, Social Security helps to ensure that they don't fall into poverty in their later years.

Disability Insurance benefits averaged $1,165 per month in December 2014.[14] Benefits are so modest that many beneficiaries struggle to make ends meet; nearly one in five, or about 1.6 million, disabled-worker beneficiaries live in poverty. But without Disability Insurance, this figure would more than double, and more than 4 million beneficiaries would be poor.[15] Eight in ten beneficiaries count on disability insurance as their main source of income, and one in three as their only source of income.[16]

When Disability Insurance beneficiaries reach Social Security's full retirement age, they begin receiving retirement benefits from the Old Age and Survivors Insurance trust fund rather than the Disability Insurance trust fund. The increase in the full retirement age to 66 delays that conversion. In December 2013, more than 450,000 people aged 65 and 66 received disability insurance benefits – over 5 percent of the disabled workers receiving benefits. Under the rules in place until 2003, they would have been receiving retirement benefits instead. This is just one example of how closely the retirement and disability components of Social Security are interwoven, and how changes to one part of the system impact the other.

**Second, the need for reallocation has been expected for many years.**

When Congress last acted to reallocate the two funds in 1994, it was predicted that this action would need to be taken again in 2016.[17] The 1995 Social Security Trustees Report showed that the disability trust fund reserves would be depleted in 2016, primarily due to a rapid, but temporary, increase in the number of disabled beneficiaries as Baby Boomers passed through their 50s and early 60s, when the risk of disability is greatest. As noted by Social Security's Chief Actuary,[18] the recent growth in the disability program stems mostly from this and other well-understood demographic factors, including growth of the U.S. population in general, increase in women's participation in the labor market, and the rise in Social Security's full retirement age from 65 to 66, as mentioned above.

Congress reallocated a substantial percentage of payroll taxes from the Disability Insurance (DI) program to the Old Age and Survivors Insurance (OASI) program in 1983. The Social Security Amendments of 1983 were needed to address the shortfall in

the retirement trust fund at that time, as the reduction in the DI share of payroll taxes allowed for a parallel increase in the OASI share to address its financial problems as the major reforms enacted at that time were phased in. Those who drafted the 1983 amendments did not deliberately set out to underfund the Disability Insurance program. They used the best information available to them at the time when they decided to reduce DI's share of the payroll tax.[19] After the amendments, both funds were projected to be solvent through about 2060, based on the economic and technical assumptions of the time.

The 1994 reallocation boosted DI's share of payroll taxes, but still held it below the rate that had been scheduled before the 1983 amendments. If the Disability Insurance program's share of the tax rate had remained at its pre-1983 level, there would be no need for reallocation now.[20]

The projections made at the time of the last reallocation in 1994 have proven to be remarkably accurate. The current shortfall in the Disability Insurance trust fund is thus not a surprise or a reflection of a program that has somehow grown "out of control" in recent years or is "going bankrupt." Rather the growth in the program between 1972 and 2008 is due almost entirely (90 percent) to the Baby Boomers aging into the high-disability years of their 50s and 60s, the rise in women's labor-force participation, and population growth.[21]

**Third, the present situation is nothing new.**

Congress has reallocated payroll tax revenues between the two trust funds 11 times over the six decades since Social Security Disability Insurance was established — about equally in both directions.[22] Reallocation has historically been a traditional and noncontroversial step.

The reallocation plan in the Administration's FY 2016 budget would ensure that both the Old Age and Survivors Insurance trust fund and the Disability Insurance trust fund remain fully solvent until 2033.[23] Importantly, reallocation can be done without increasing taxes or cutting benefits, and would keep the combined trust funds on their current course; under current law as well as under reallocation, the combined trust funds will be able to pay all scheduled benefits until 2033.[24]

U.S. Secretary of the Treasury Jacob Lew testified in March 2014 at a U.S. Senate Budget Committee hearing that "there's only one solution the technical experts believe can work in the timeframe between now and 2016. And that's a reallocation of the tax rate, as we've done in the past."[25]

There should be nothing unusual or contentious in taking such a step now. We urge Congress to do so expeditiously and without any accompanying cuts to Social Security coverage, eligibility or benefits.

In closing, reallocation does not require any increase in tax rates and will maintain the solvency of the combined Social Security trust funds until 2033, as currently projected. We recognize that one of the strengths of our Social Security system is its universality. Disability Insurance is a core component of our Social Security system. Most of the Americans who rely on Social Security Disability Insurance are, in fact, older adults, and we reject any attempts to manufacture a crisis that pits older adults against people with disabilities.

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[1] http://www.nsclc.org/

[2] http://www.lcao.org/

[3] http://www.lcao.org/about-lcao/membership/

[4] LCAO Letter to White House on Disability Insurance (DI) Fund Reallocation, October 9, 2014, http://www.lcao.org/files/2014/10/LCAO-DI-Reallocation.pdf; LCAO Chair's Letter on House Rules and DI, January 20, 2015, http://www.lcao.org/files/2015/01/LCAO-Chair-Letter-on-House-Rules-and-DI.pdf.

[5] SSA Fact Sheet on the Old-Age, Survivors and Disability Insurance Program; Section D. Measures of Protection. http://www.ssa.gov/OACT/FACTS/

[6] Department of Labor, Bureau of Labor Statistics, National Compensation Survey, 2012, http://www.bls.gov/ncs/ebs/benefits/2012/ownership/civilian/table12a.htm.

[7] Survey of Consumer Finances, 2013 SCF Chartbook, http://www.federalreserve.gov/econresdata/scf/files/BulletinCharts.pdf.

[8] "The Compassionate Allowances (CAL) initiative is a way to expedite the processing of SSDI and SSI disability claims for applicants whose medical conditions are so severe that their conditions obviously meet Social Security's definition of disability. It is not a separate program from SSA's two disability programs, SSDI and SSI." http://www.ssa.gov/compassionateallowances/cal_faqs.htm

[9] Kathy Ruffing, "Social Security Disability Insurance Benefits are Vital to Workers with Severe Impairments," August 9, 2012, http://www.cbpp.org/cms/?fa=view&id=3818.

[10] http://ssa.gov/OACT/ProgData/benefits/da_age201312.html

[11] Rebecca Vallas and Shawn Fremstad, "Social Security Disability Insurance: A Bedrock of Security for American Workers," Center for American Progress, July 8, 2014, https://www.americanprogress.org/issues/poverty/report/2014/07/08/93386/social-security-disability-insurance/

[12] Kathy Ruffing, "No Surprise: Disability Beneficiaries Experience High Death Rates," Center on Budget and Policy Priorities, April 4, 2013, http://www.offthechartsblog.org/no-surprise-disability-beneficiaries--experience-high-death-rates

[13] Ibid.

[14] Social Security Administration, Monthly Statistical Snapshot, December 2014, available at http://www.ssa.gov/policy/docs/quickfacts/stat_snapshot/ (last accessed February 8, 2015).

[15] Vallas and Fremstad, "Social Security Disability Insurance: A Bedrock of Security for American Workers."

[16] Michelle Stegman Bailey and Jeffrey Hemmeter, "Characteristics of Noninstitutionalized DI and SSI Program Participants, 2010 Update," SSA Research and Statistics Note No. 2014-02 (released February 2014), http://www.ssa.gov/policy/docs/rsnotes/rsn2014-02.html.

[17] The Board of Trustees, Federal OASI and Federal DI Trust Funds, *The 1995 Annual Report of Trustees of the Federal Old--Age and Survivors Insurance and Federal Disability Insurance Trust Fund* (1995), http://www.ssa.gov/history/reports/trust/1995/trif.html.

[18] "The Financing Challenges Facing the Social Security Disability Insurance Program," Testimony by Stephen C. Goss, Chief Actuary, Social Security Administration, House Committee on Ways and Means, Subcommittee on Social Security, March 14, 2013, http://waysandmeans.house.gov/uploadedfiles/goss_testimony.pdf.

[19] The 1983 amendments also raised DI's costs by increasing the full retirement age from 65 to 66 between 2000 and 2005 and increasing it again from 66 to 67 between 2017 and 2022.

[20] Kathy Ruffing and Paul N. Van de Water, "Congress Needs to Boost Disability Insurance Share of Payroll Tax By 2016," July 2014, http://www.cbpp.org/cms/index.cfm?fa=view&id=4168#_ftn3

[21] David Pattison and Hilary Waldron, "Growth in New Disabled Worker Entitlements, 1970-2008," Social Security Bulletin 73 (4) (2013): 25–48, http://www.ssa.gov/policy/docs/ssb/v73n4/v73n4p25.pdf.

[22] Geoffrey Kollmann, "Social Security: Summary of the Major Changes in the Cash Benefits Program," May 18, 2000, http://www.socialsecurity.gov/history/reports/crsleghist2.html.

[23] White House Office of Management and Budget, *Fiscal Year 2016 Budget of the United States,* http://www.whitehouse.gov/sites/default/files/omb/budget/fy2016/assets/budget.pdf

[24] The Board of Trustees, Federal OASI and Federal DI Trust Funds, *The 2014 Annual Report of Trustees of the Federal Old--Age and Survivors Insurance and Federal Disability Insurance Trust Fund.*

[25] Jacob Lew, Testimony before the U.S. Senate Budget Committee, March 6, 2014. Video of Secretary Lew's testimony available at http://www.bloomberg.com/video/lew--testifies--before--senate--on--obama--budget--plan-- s0Nj4eyFT5mkoX19pfkdoA.html

Chairman ENZI. Thank you, Ms. Lang. I want to thank all the panelists for their information and ideas and hope you will be open to written questions submitted by people as well. We can go into more detail, and you are the three that we are relying on for the solutions. We in the earlier panel covered the problem pretty well.

Let me begin my questions with Dr. de Jong. I want to thank you for coming all the way over here, and one of the reasons that we wanted you to testify is that when I was in the State legislature, I always tried to find some kind of a State that had already done what we were talking about doing and seeing what the pitfalls were and how they accomplished it. And so you are that on an international scale, and I appreciate it.

You talked about privatization of Disability Insurance as a major instrument in helping the disabled people remain in the workforce, and you have probably already sense that that is a nasty word around here. But what it sounds like you did was get private insurance to pick up the first 2 years. Can you explain how you developed the market for that Disability Insurance for that first 2 years?

Mr. de Jong. Well, it was not really developed. What you have now is that a Dutch employer has to contract—whether he wants to insure his financial liabilities towards paying sickness benefits for 2 years is something he can decide himself. There is no mandate. But he has to—he is legally mandated to contract occupational health services, because, I mean, normally employers—I can speak for myself—are not managers of absenteeism, of sickness absenteeism, so they have to contract company doctors, they have to contract people who—so that is all legally mandated, and what you normally see is that especially for small firms—and most firms are small—is a package that—an insurer offers a package including all these occupational health services so that the management of sickness absenteeism is in the hand of professionals that are contracted by the firm.

But the point is that in the end the employer and the sick employee together have their responsibilities, and what their responsibilities are is when sickness lasts longer than 6 weeks, it is laid down in law also by what is called a "gatekeeper protocol," by a protocol, where the steps that you have to take and that you have to follow promoting work resumption as soon as possible are laid down in law. And that sounds like a lot of red tape. I mean, of course, you can follow those rules. But in the end, you are judged, if it all fails and within those 2 years an employee is not able to return to work or to return to the labor market, then he or she has to—can claim a disability benefit. But then the public disability benefit administrators will test whether or not enough effort has been put in that work resumption plan, the "reintegration plan," as it is called.

So that is how it works. It is not really a market. Of course, there are private insurance, some of them you may know, ING, for instance, in Holland, and they provide those policies.

Chairman ENZI. Thank you.

Dr. Duggan, your research has shown that the Social Security Administration's projections of the growth has consistently been too optimistic. Do you believe the SSA's predictions of the future program growth are too low? And can you explain why?

Mr. DUGGAN. I served on a technical panel to evaluate the assumptions and methods used by the Office of the Actuary, and I want to praise—I think they have—it is an incredibly complicated program to examine. There is the Old-Age program, the disabled program, and so forth. And I have not studied the most recent Trustees report, but from my service on the panel, then my recollection is that in certain respects my projections were—my analysis suggested that projections were somewhat optimistic, looking ahead to the future, about—optimistic in terms of the program flattening out somewhat more in the future.

And it is true that—I mean, there are Trustees reports each year, and they are—there is an incredible amount of work that go into them, and I have gotten to know a lot of the people who work in the staff, and they are outstanding. I do think there are years in which they were on target with their projections, but more often than not, the projections were below in terms of the size of the SSDI program, let us say as of today.

But that is not to say—it is a complicated thing to measure. I mean, as you can see from my testimony, the growth in SSDI enrollment has been larger than one would expect based purely on the aging of the baby-boom population and the increase in the fraction of women insured for the program.

So there have been really big changes in the composition of conditions with which people are qualifying for the program. So, for example, conditions like stroke and cancer have been relatively flat since, let us say, 1989; whereas, conditions like musculoskeletal conditions and mental disorders have grown a lot.

That is not to say that people with—all disability recipients with musculoskeletal or mental disorders, that those are not very deserving recipients, but there has been a big change in the composition of the recipient population that is much greater than one would have expected based purely on aging and the insured status.

So I do not envy their task because there are a lot of variables that go into it. There is the economy. There is—and many—the age distribution and so forth. But I do—you know, so—but I cannot say because I have not studied the most recent report how that one looks. My preliminary look at it suggests that there have been some adjustments since the panel recommendations that I was a part of that have gone in certain dimensions in the dimension that we as a panel recommended, but I just cannot—I do not remember them right now. Sorry.

Chairman ENZI. Thank you. I will ask some of those in writing, and I appreciate all of your expertise, and we will draw on that significantly for all three of you.

Senator Sanders?

Senator SANDERS. Thank you, Mr. Chairman, and I thank all of you for coming here, especially you, Mr. de Jong, coming across the ocean to testify, and we appreciate that.

Let me start off with Ms. Lang. Ms. Lang, you are here testifying on behalf of the Leadership Council of Aging Organizations.

Ms. LANG. Yes, I am.

Senator SANDERS. Which represents more than 70, as I understand it, senior citizen groups.

Ms. LANG. That is right.

Senator SANDERS. And all of those groups, including the AARP and the National Committee to Preserve Social Security and Medicare, I think all told they represent some 60 million Americans. Is that about right?

Ms. LANG. About right, yes.

Senator SANDERS. And you are here very clearly to tell us that you believe we should go forward with the allocation process that has taken place 11 times previously. Is that correct?

Ms. LANG. Yes, it is.

Senator SANDERS. Why? Why do groups representing 60 million Americans think that we should make sure there are not major cuts in the disability programs?

Ms. LANG. Well, as I mentioned in my testimony, 70 percent of the current disability beneficiaries are, in fact, older adults, so any reduction in the program would harm them.

I am sorry to see that Senator Sessions and Senator Ayotte have left, because they made the comment about robbing Peter to pay Paul, and the money is not actually taken out of the Old-Age or retirement fund. It is reallocating the payroll taxes that go into each fund. So I do not think it is accurate to characterize the situation as stealing from retirees to pay benefits to people with disabilities. It is merely reallocating the percentage of the payroll taxes that go to each fund, and it is very important to make sure that those older Americans who meet the very strict disability standard for receiving these benefits are able to continue receiving the income that they need as they age into their retirement years.

Senator SANDERS. Ms. Lang, I happen to believe that at the end of the day, despite what the Republicans did in the House, we are going to reach an agreement, and I do not think anybody here really wants to see a 19-percent cut in disability benefits. That is what I think.

But you also worked as an attorney representing low-income people with disabilities. Just very briefly, what would a 19-percent cut in benefits mean to people who are barely making it today?

Ms. LANG. I would say for my clients, I represented dozens of people applying for disability benefits over several years, and for those who did meet the very strict standard and were able to get on benefits, it was a fairly low amount of money. So any sort of cut for them would really, I think, mean homelessness for many of—

Senator SANDERS. How does a person with a disability survive out on the street when the weather gets, in my State, 10 below zero?

Ms. LANG. I do not know. And, quite frankly, many shelters for homeless people are not equipped to accommodate people with disabilities and serve them. So it really can be a death sentence for many individuals with disabilities to face homelessness.

Senator SANDERS. Mr. Chairman, I love the idea that we brought somebody from Europe to be with us today. I think that is a great idea, and I think we should do more of it. It is called best practices. You know, Vermont can learn from Wyoming, and Wyoming can learn from California, and we can learn from Europe and so forth and so on.

But what is interesting to me is that when we talk about the United States and Europe, I think what we should begin with is

appreciating that the social safety net that we have here is quite minimal compared to Europe. I would just for a moment, if I could ask Dr. de Jong, in this country we have 40 million people who have no health insurance. We have many more who are underinsured, large co-payments. How many people in Holland do not have any health insurance?

Mr. de Jong. Well, only those that refuse to—well, no, everybody has health—

Senator SANDERS. Everybody has health insurance, so maybe we should have a hearing here as to how that works, and my guess is you end up spending far less per capita on health care than we do in the United States.

In this country, we have large numbers of people who cannot afford to go to university or college. Others graduate deeply in debt. What is the cost of a college education in Holland?

Mr. de Jong. Well, you mean the tuition fees?

Senator SANDERS. Yes.

Mr. de Jong. That would be around 2,000 euros per year.

Senator SANDERS. But it is my understanding also for many it is free. Is that correct? For lower-income people it might be free?

Mr. de Jong. Yeah, they get grants. They get grants.

Senator SANDERS. Okay. Now, let me ask you this about the reason that you are here, which is disability benefits. Let us hypothesize that you have two people who have suffered the same exact accident on the job—one is in the United States, and one is in Holland—and they needed disability benefits. Correct me if I am wrong, but my understanding is that for someone who is fully disabled in Holland, they would receive benefits equivalent to about 85 percent of what their previous income was. Is that correct?

Mr. de Jong. Yeah, during the first 2 years, on average, and that is including collectively bargained supplements, so that is—

Senator SANDERS. Yes, they have a strong union.

Mr. de Jong. So there is 70 percent legal base, you could say, and all workers have supplements that are from collectively bargained arrangements. But that is only for the first 2 years.

Senator SANDERS. Okay, right. My understanding—and, Ms. Lang, you correct me if I am wrong, or anybody up there, correct me if I am wrong—is that while for the first 2 years 85 percent of a worker's benefits goes to disability. In this country, Ms. Lang, do you know what the number is?

Ms. LANG. It is less than 50 percent replacement rate, and probably 40, 45 percent replacment rate.

Senator SANDERS. So I think, Mr. Chairman, another point we may want to continue this discussion and see if we in the United States can move toward where Holland is in their very generous benefits for some of the most vulnerable people in their country. I think it would be an interesting discussion.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Senator Perdue?

Senator PERDUE. Thank you, Mr. Chairman.

Along with yourself and the Ranking Member and Senator Whitehouse, I have sat here this morning and listened to every question and every ounce of testimony because I think this is at

the core of our financial crisis—not the disability and what we are about to do to solve that problem for 18 years. To me, that is the wrong thing we should be debating. I think we have agreed on two things today, or at least I have. The Ranking Member earlier this morning accused a friend of mine in the House—or misinterpreted, I think, comments made there. But there are two things that I agree with the Ranking Member on. One is that we have got to move to ensure that benefits are not reduced, period. Two, we have got to solve the long-term crisis.

I have been saying this for quite a while. I believe this is not a debate over what we do between now and 2017 relative to 2033 with the Disability versus the Old-Age Fund. But I disagree on that this is a manufactured crisis. I have heard several people this morning mention that, and I take offense about that. I think this is our irresponsibility over the last really 30 years, but certainly since 1994, across three Presidents, 11 different Congresses, we have kicked this ball down the court.

I think the only hesitancy I have personally about doing this is that I would like to see some long-term—or a debate about a long-term solution. That is really what my concern is, Mr. Chairman: What do we do for the beneficiaries past 2033?

Ms. Lang, you talk about stealing from Peter to pay Paul. I disagree with your characterization of it. The one thing I am sure of is that by doing this, all we are doing is stealing from the future to make sure we do not have a problem for the next 18 years. That I will not be comfortable with. We have got to debate that. If we are going to move toward a responsible budget in this country, we have got to solve the long-term Social Security, and then eventually the Medicare program as well, which is an even bigger problem.

I have a question for Dr. Duggan. You mentioned that about a third, I think you said—and correct me if I am wrong—about 15—I am sorry, about a fifth, about 20 percent of the increase—and I think the number of people participating in the DI program has almost tripled since 1984, in the last 30 years. About a fifth of that was age-related, and I think you said about 12 percent was due to spouses coming into the workforce. Help me understand with some granularity what the other two-thirds represent.

Mr. DUGGAN. So there has been a large increase in the likelihood that—so, yeah, about a third combined between those two factors, the aging of the baby-boom generation and the increase in the fraction of women who are insured for the SSDI program. And the numbers differ a bit depending on what exact base year you use, but it is in the neighborhood of one-third from, let us say, 1989. And the increase, the rest of the increase is attributable to a greater likelihood that a person with certain characteristics will be on the program. So I gave one example, and the increase has been larger for women than for men because of this growth in the share insured, partly because of that. But take men, for example, 50 to 59, so men in their fifties, 25 years ago, 5.8 percent of them were receiving SSDI benefits, and now 8.8 percent of them are receiving, so basically an increase from almost 6 percent to almost 9 percent during that time period. And that is, you know, that sort of increase has been—has existed at other ages as well.

And so if we look at—so where is that coming from? So if one looks at the composition of conditions with which people are qualifying—and this comes from Figure 2 of my testimony, and I tried to distill the complexity into just a few figures. There is a lot more—you can drill down at a much finer level. But there has been a change in the composition of conditions with which people are qualifying. Musculoskeletal conditions, for example, the award rate for those has increased by a factor of about 6 since just prior to the liberalization that we have talked about in 1984; whereas, during that same time, the award rate—and when I say the "award rate," I mean here number of awards divided by number of people insured for the program. So you can see that in Figure 2.

And if you look at the corresponding change for people, let us say, cancer or with circulatory conditions like stroke, those have been pretty flat. So there has been a big change in the characteristics of the people flowing onto the program. And so that is where it has come from.

Senator PERDUE. Thank you. I just have one last comment. Dr. de Jong, your indictment of our partisanship is well deserved this morning, and I appreciate your comments, and Ms. Lang as well. Thank you for being here.

Thank you, Mr. Chairman.

Chairman ENZI. Senator Whitehouse.

Senator WHITEHOUSE. Thank you, Chairman.

Let me first ask each of the witnesses, starting with Dr. Duggan, would you recommend an across-the-board benefit cut in Social Security Disability Insurance in the neighborhood of 20 percent under any circumstances?

Mr. DUGGAN. I would not recommend that, no.

Senator WHITEHOUSE. Because?

Mr. DUGGAN. Well, I have not evaluated the facts of that specific proposal, but it would clearly—as has been talked about earlier today, SSDI provides benefits to many of the Nation's most vulnerable citizens, and that would inflict significant hardship on a very large number of people. So I certainly would not—

Senator WHITEHOUSE. Dr. de Jong, how about you?

Mr. de Jong. My answer would be—thank you for asking this question. My answer would be more bold. I would be very strongly against it, but maybe the—what I know of the SSDI system is that it focuses much more in incapacity than on capacity.

Senator WHITEHOUSE. But irrespective of that, with respect to my exact question, which was: Would you recommend a near 20-percent cut?

Mr. de Jong. No, I would—

Senator WHITEHOUSE. You would not.

Mr. de Jong. I would be more selective.

Senator WHITEHOUSE. Okay. Ms. Lang?

Ms. LANG. No, I would not.

Senator WHITEHOUSE. Okay. Dr. Duggan, you have looked—you appear to have looked pretty closely at this question. You appear also to have focused pretty much on the expenditure side. Do you have a view as to how the recent changes in income inequality, the extent to which higher incomes have exploded in this country, has changed the percentage of income that is above the $118,000 pay-

roll cap and has, therefore, been a factor in the current Social Security imbalance?

Mr. DUGGAN. So I personally have not evaluated that specific thing, but I recall from reading reports by the actuaries and by CBO and others that the fraction of income that is within that cap has declined over time.

It is also true that the rise in inequality has affected benefits for people at the lower end of the income distribution because the bend points—we have this benefit formula, essentially the same benefit formula used for Social Security retired worker benefits. It is a 90–32–15 benefit formula, and the points where that formula bends from 90 to 32 and from 32 to 15, those are indexed to average wage growth in the economy. And so some of the first research that I did on this program showed that because of slower wage growth at the lower end of the distribution, lower-income workers were replacing more of their income at that 90 percent rate than at the 32 percent rate, basically because the bend point was moving faster than their incomes were. So at some level, the formula has helped cushion somewhat that change.

Senator WHITEHOUSE. That might cushion it for individual workers, but as a program, the effect has been to forgo what otherwise would have been revenue and has added to the deficit. Correct? I.e., if income inequality had not changed from, let us say, 1990 to now, if that were a constant, there would have been more income subject to payroll tax and there would be more revenue coming into Social Security, and we would have less of a deficit. That is kind of mathematics, isn't it?

Mr. DUGGAN. It just depends a little bit on the assumptions that you—like at what rate will those things grow. But, in general, the spirit of what you are describing seems plausible to me. It just depends on—I do not mean to—it depends a bit—the devil is in the details a little bit on what you assume would have happened to those—

Senator WHITEHOUSE. Let me try it this way: You have got a chunk of American salary that is under $118,000.

Mr. DUGGAN. Right.

Senator WHITEHOUSE. And it contributes revenue to Social Security. You have got a chunk of American salary that is over $118,000, and it does not contribute to Social Security.

Mr. DUGGAN. Right.

Senator WHITEHOUSE. If the second chunk gets bigger relative to the first chunk instead of staying even, that means less money for Social Security. Isn't that pretty simple?

Mr. DUGGAN. Like I said, it just depends on the assumption. Are you going to bring it into balance by raising the—

Senator WHITEHOUSE. No, no. I am not asking out-year assumptions. I am just asking if what I have said is accurate.

Mr. DUGGAN. It is the case that—I do not know if it 90 to 83 percent. I think someone here earlier said that. But that—

Senator WHITEHOUSE. It is the case that if less of America's income is subject to taxation than otherwise would be, the revenues for the program are less than they otherwise would be. Right?

Mr. DUGGAN. It seems plausible, once again, but there are behavioral responses that one needs to take into account. So if you change the—

Senator WHITEHOUSE. Oh, all right. Well—

Mr. DUGGAN. I am not—

Senator WHITEHOUSE. Thank you, Dr. Duggan.

Chairman ENZI. The Senator's time has expired, and I want to thank everyone for their participation today. That concludes the questions for the second panel this morning, but—

Senator WHITEHOUSE. Oh, Mr. Chairman?

Chairman ENZI. —I would hope that they would—

Senator WHITEHOUSE. May I offer an exhibit for the record?

Chairman ENZI. Without objection, sure.

Senator WHITEHOUSE. Thank you.

Chairman ENZI. And people can submit statements, too, if they wish.

We appreciate the time here for all of our witnesses and hope that they will be open to answering questions. Sometimes the questions can be more specific in writing, but mostly because ones with numbers kind of put the people in the back to sleep, and that is not very exciting.

I want to remind my colleagues that questions for the record are due no later than 6:00 p.m. today, filed in writing with the Committee clerk in Dirksen 624, and we hope the witnesses will respond within 7 days.

With no further business to come before the Committee, we stand adjourned.

[Whereupon, at 12:46 p.m., the Committee was adjourned.]

**Submission for the Record**
**From: Ranking Member Bernard Sanders**

**Hearing on "The Coming Crisis:**
**Social Security Disability Trust Fund Insolvency"**
**February 11, 2015**
**Senate Budget Committee**

**CONSORTIUM FOR CITIZENS WITH DISABILITIES**

**Statement for the Record**
**U.S. Senate Committee on the Budget**
**Hearing on "The Coming Crisis: Social Security Disability Trust Fund Insolvency"**
**Wednesday, February 11, 2015**

The undersigned members of the Consortium for Citizens with Disabilities (CCD) submit the following statement for the record of the February 11, 2015 hearing held by the Senate Committee on the Budget on "The Coming Crisis: Social Security Disability Trust Fund Insolvency".

The CCD is a coalition of national organizations working together to advocate for federal public policy that ensures the self-determination, independence, empowerment, integration, and inclusion of the approximately 57 million children and adults with disabilities in all aspects of society. SSDI's modest but vital assistance supports these goals for approximately 11 million Americans, helping beneficiaries with disabilities and their families to meet their everyday needs -- keeping a roof over their heads, putting food on the table, paying for out-of-pocket medical and disability-related expenses, and meeting other basic living expenses.

Congress has known for the last two decades that Social Security's Disability Insurance (DI) fund will need to be replenished by 2016. The need for action now is no surprise, but stems from long-term demographic trends including an aging workforce now in its disability-prone years, and an increase in work by women that has led to an increase in women's eligibility for Social Security including SSDI based on their own work records.

Reallocation will ensure that SSDI is available to both current and future beneficiaries, including the 7 in 10 SSDI beneficiaries who are age 50 and older. SSDI benefits average just $38 per day for workers with disabilities. Benefits make up the majority of income for 4 out of 5 beneficiaries and provide the sole source of income for 1 in 3 beneficiaries. The impact of any reduction in benefits could be truly devastating.

Congress needs to act expeditiously, as it has done many times in the past, to reallocate existing payroll taxes between Social Security's DI and Old-Age and Survivors' Insurance (OASI) funds. As outlined by Social Security's actuaries, both trust funds would be able to pay full scheduled benefits through 2033 by temporarily raising the 1.8 percent DI share of the current 12.4 percent Social Security payroll contribution to 2.8 percent in 2015 and 2016, and then gradually reducing it back to 1.8 percent by 2025. Congress has reallocated between Social Security's funds in this manner about equally in both directions to keep the system on an even reserve ratio -- 6 times using a

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narrow definition of reallocation, and 11 times using a broader definition of reallocation. Reallocation does not require any new taxes and will maintain the long-term solvency of the combined Social Security trust funds at 2033, as currently projected.

Reallocation -- without accompanying cuts to Social Security coverage, eligibility, or benefits -- is the common sense, responsible solution that Congress should enact promptly. Such a reallocation is needed to keep Social Security's promise to the more than 165 million Americans who currently contribute to the system and the nearly 11 million Americans who currently receive SSDI benefits.

Maintaining our Social Security system goes far beyond dollars and cents. It is about strengthening economic security and dignity for all Americans. Consideration of any changes to this vital system must include the voices and views of people with disabilities as well as all Americans who may need SSDI in the future.

Sincerely,

ACCSES
American Academy of Pediatrics
American Association of People with Disabilities (AAPD)
American Association on Health and Disability
American Foundation for the Blind (AFB)
American Network for Community Options and Resources
Association of Assistive Technology Act Programs
Association of Jewish Family & Children's Agencies
Association of University Centers on Disabilities (AUCD)
Attention Deficit Disorder Association
Autism National Committee (AutCom)
Autistic Self Advocacy Network (ASAN)
Bazelon Center for Mental Health Law
Brain Injury Association of America
Community Legal Services
Council for Learning Disabilities
CSH
Disability Rights Education & Defense Fund
Easter Seals
Epilepsy Foundation
Goodwill Industries International
Health & Disability Advocates
Jewish Federations of North America
Lupus Foundation of America
Lutheran Services in America Disability Network
National Academy of Elder Law Attorneys (NAELA)
National Alliance on Mental Illness
National Association of Councils on Developmental Disabilities
National Association of Disability Representatives
National Association of School Psychologists
National Association of State Head Injury Administrators

National Committee to Preserve Social Security and Medicare
National Council for Behavioral Health
National Council on Aging
National Council on Independent Living
National Disability Rights Network
National Down Syndrome Congress
National Industries for the Blind
National Multiple Sclerosis Society
National Organization of Social Security Claimants' Representatives
National Respite Coalition
Paralyzed Veterans of America
SourceAmerica
Special Needs Alliance
The Arc of the United States
United Cerebral Palsy
United Spinal Association

**Submission for the Record**
**From: Ranking Member Bernard Sanders**

**Hearing on "The Coming Crisis:**
**Social Security Disability Trust Fund Insolvency"**
**February 11, 2015**
**Senate Budget Committee**

**Testimony Before the U.S. Senate Committee on Budget**

**Hearing on "The Coming Crisis:**
**Social Security Disability Trust Fund Insolvency"**

**Rebecca Vallas**
Director of Policy, Poverty to Prosperity Program
Center for American Progress

February 11, 2015

Thank you, Chairman Enzi, Ranking Member Sanders and Members of the Committee for the opportunity to submit this statement for the record. My name is Rebecca Vallas, and I am the Director of Policy for the Poverty to Prosperity Program at the Center for American Progress.

The subject of today's discussion is of the utmost importance to all of us as Americans, because any of us could find ourselves in the position of needing to turn to Social Security Disability Insurance at any time.

Imagine that tomorrow, while cleaning out your gutters, you fall off a ladder. You suffer a traumatic brain injury and spinal cord damage, leaving you paralyzed, unable to speak, and with significantly impaired short- and long-term memory. Unable to work for the foreseeable future, you have no idea how you are going to support your family. Now imagine your relief when you realize an insurance policy you have been paying into all your working life will help keep you and your family afloat by replacing a portion of your lost wages. It is our Social Security system.

I'm sure we can all agree that no one wants to see this important program weakened, or its basic but crucial benefits cut. The American people time and again have made clear their strong support for Social Security, and their strong opposition to benefit cuts. I look forward to discussing how we can work together to strengthen this vital program, so that it can continue to protect American men, women and children for decades to come.

I will make three main points today:

- **Social Security Disability Insurance provides basic but essential protection that workers earn during their working years.** Social Security protects nearly all American workers in case of life-changing disability or illness. The modest benefits from Social Security Disability Insurance are vital to the economic security of disabled workers and their families.

- **Eligibility criteria are stringent and only workers with the most serious disabilities and illnesses qualify for benefits.** According to the Organisation for Economic Cooperation and Development, or OECD, the Social Security disability standard is among the strictest in the industrialized world. The vast majority of applicants are denied, and those who qualify for benefits often have multiple serious impairments, and many are terminally ill. Few are able to work at all.

- **It's no surprise that action is needed to address the program's finances, and a traditional, routine step would put the entire Social Security system on sound footing for two decades.** Periodic rebalancing of Social Security's trust funds—so that both the retirement/survivorship and disability parts of Social Security rest on sound financial footing—has occurred in a bipartisan manner 11 times in the program's history, with funds shifted in the direction of the Old Age and Survivors Insurance trust fund about half the time, and in the direction of the Disability Insurance trust fund about half the time. As long expected by Social Security's actuaries, rebalancing is again needed and would ensure that Social Security is able to pay all promised benefits until 2033—without changing the health of the combined trust funds.

## Social Security Disability Insurance provides basic but essential protection that workers earn during their working years

Social Security was established 80 years ago to ensure "the security of the men, women and children of the nation against the hazards and vicissitudes of life."[i] In 1956, the program was expanded to include Disability Insurance in recognition that the private market for long-term disability insurance was failing to provide adequate or affordable protection to workers.[ii]

Today, nearly all Americans—91 percent of workers ages 21 to 64—are protected by Social Security Disability Insurance.[iii] In all, more than 160 million American workers and their families are protected.[iv] About 8.9 million disabled workers—including more than 1 million veterans—receive Disability Insurance benefits, as do about 157,000 spouses and 1.9 million dependent children of disabled workers.[v]

### Social Security Disability Insurance is coverage that workers earn

Both workers and employers pay for Social Security through payroll tax contributions. Workers currently pay 6.2 percent of the first $118,500[vi] of their earnings each year, and employers pay

the same amount up to the same cap. Of that 6.2 percent, 5.3 percent currently goes to the Old Age and Survivors Insurance, or OASI, trust fund, and 0.9 percent to the Disability Insurance trust fund. Due to the interrelatedness of the Social Security programs, the two funds are typically considered together, although they are technically separate. The portion of payroll tax contributions that goes into each trust fund has changed several times throughout the years to account for demographic shifts and the funds' respective projected solvency.[vii]

## Benefits are modest but vital to economic security

The amount a qualifying worker receives in benefits is based on his or her prior earnings. Benefits are modest, typically replacing half or less of a worker's earnings. The average benefit in 2014 was just over $1,140 per month—not far above the federal poverty level for an individual.[viii]

For more than 80 percent of beneficiaries, Disability Insurance is their main source of income. For one-third, it is their only source of income.[ix] Benefits are so modest that many beneficiaries struggle to make ends meet; nearly one in five, or about 1.6 million, disabled-worker beneficiaries live in poverty.

But without Disability Insurance, this figure would more than double, and more than 4 million beneficiaries would be poor.[x] Disabled workers use their Social Security benefits to meet basic needs, such as rent or mortgage, gas and electric, food, and copays on needed—often life-sustaining—medications.

**Average disabled worker benefit (Dec 2014):**

$1,165 per month
$13,980 per year

**Federal poverty level for an individual (2014):**

$972 per month
$11,670 per year

Workers who receive Disability Insurance are also eligible for Medicare after a two-year waiting period.[xi]

## Social Security Disability Insurance provides protection most of us could never afford on the private market

And there is good reason to offer disability insurance through a public program such as Social Security: private disability insurance is out of reach for most families. Just one in three private-sector workers has employer-provided long-term disability insurance, and plans are often less adequate than Social Security.[xii] Coverage is especially scarce for low-wage workers—just 7 percent of workers making less than $12 an hour have employer-provided disability insurance.[xiii]

Workers in industries such as retail, hospitality, and construction are among the least likely to have employer-provided long-term disability coverage, and coverage is highly concentrated among white-collar professions.[xiv] Access is even more limited on the individual market.

While it is difficult to compare Social Security Disability Insurance with private long-term disability plans given that private plans often exclude certain types of impairments—as well as

workers with pre-existing conditions or in high-risk occupations—purchasing a plan of comparable value and adequacy on the individual private market would be unrealistic for most Americans.

**"Coverage by private [disability insurance] carriers is certain to be restricted, because disability insurance confronts all the major impediments to widespread, affordable, and actuarially sound private insurance provision: adverse selection, moral hazard, and covariance of risks. ... Many insurers write group policies, but they differentiate strongly between groups with high and low risks. Some groups are treated as essentially uninsurable. Where risks are high, prices are high as well. The result is that private disability insurance tends to be available only to those groups who need it least; others are priced out of the market."**

Michael Graetz and Jerry Mashaw, noted social insurance experts and coauthors of *True Security*.[14]

## Eligibility criteria are stringent and only workers with the most serious disabilities and illnesses qualify for benefits

Disabled workers face a steep uphill battle to prove that they are eligible for Social Security Disability Insurance. Under the Social Security Act, the eligibility standard requires that a disabled worker be "unable to engage in substantial gainful activity"—defined as earning $1,090 per month, for 2015—"by reason of any medically determinable physical or mental impairment which can be expected to result in death or last for a continuous period of not less than 12 months."[xv] In order to meet this rigorous standard, a worker must not only be unable to do his or her past jobs, but also—considering his or her age, education, and experience—any other job that exists in significant numbers in the national economy at a level where he or she could earn even $270 per week.[xvi]

A worker must also have earned coverage in order to be protected by Disability Insurance. A worker must have worked at least one-fourth of his or her adult years, including at least 5 of the 10 years before the disability began in order to be "insured."[xvii]

The OECD describes the U.S. disability benefit system, along with those of Canada, Japan, and South Korea, as having "the most stringent eligibility criteria for a full disability benefit, including the most rigorous reference to all jobs in the labor market."[xviii]

In practice, proving medical eligibility for Disability Insurance requires extensive medical evidence from one or more medical providers designated as acceptable medical sources (licensed physicians, specialists, or other approved medical providers) documenting the applicant's severe impairment, or impairments, and resulting symptoms. Evidence from other

providers, such as nurse practitioners or clinical social workers, is not enough to document a worker's medical condition. Statements from friends, loved ones, and the applicant are not considered medical evidence and are not sufficient to establish eligibility.

Most claims for Disability Insurance are denied under this stringent standard. Nearly 80 percent of applicants are denied at the initial level, and fewer than 4 in 10 are approved after all levels of appeal.[xix] Many wait a year—and in many cases much longer—before receiving needed benefits. Underscoring the strictness of the disability standard, thousands of applicants die each year during the eligibility determination process.[xx] Of those who live long enough to receive benefits, one in five male and nearly one in six female beneficiaries die within five years of being approved.[xxi] All told, Disability Insurance beneficiaries have death rates three to six times higher than other people of their age.[xxii]

## Beneficiaries have a wide range of significant disabilities and debilitating illnesses and many have multiple impairments

Disabled workers who receive Disability Insurance live with a diverse range of severe impairments. The Social Security Administration categorizes beneficiaries according to their "primary diagnosis," or main health condition.[xxiii] As of 2012, the most recent year for which impairment data are available:

- 31.8 percent have a "primary diagnosis" of a mental impairment, including 4.2 percent with intellectual disabilities and 27.6 percent with other types of mental disorders such as schizophrenia, post-traumatic stress disorder, or severe depression.
- 29.8 percent have a musculoskeletal or connective tissue disorder.
- 8.7 percent have a cardiovascular condition such as chronic heart failure.
- 9.3 percent have a disorder of the nervous system, such as cerebral palsy or multiple sclerosis, or a sensory impairment such as deafness or blindness.
- 20.4 percent include workers living with cancers; infectious diseases; injuries; genitourinary impairments such as end stage renal disease; congenital disorders; metabolic and endocrine diseases such as diabetes; diseases of the respiratory system; and diseases of other body systems[xxiv]

**Social Security's listing of impairments is organized according to 14 body systems**

- Cardiovascular system
- Congenital disorders that affect multiple body systems
- Digestive system
- Genitourinary impairments
- Hematological disorders
- Endocrine disorders
- Immune system disorders
- Malignant neoplastic disorders
- Mental disorders
- Musculoskeletal disorders
- Neurological disorders
- Respiratory system
- Skin disorders
- Special senses and speech

A fact not well captured by Social Security's data—given that beneficiaries are categorized by "primary diagnosis"—is that many beneficiaries have multiple serious health conditions. For instance, nearly half of individuals with mental disorders have more than one mental illness,

such as major depressive disorder and a severe anxiety disorder.[xxv] Individuals with mental illness are also at greater risk of poor physical health: The two leading causes of death for individuals with mental illness are cardiovascular disease and cancers.[xxvi] Musculoskeletal disorders commonly afflict multiple joints,[xxvii] and individuals with musculoskeletal impairments—typically older workers whose bodies have broken down with age—commonly suffer additional health conditions such as cardiovascular disease, diabetes, and respiratory disease.[xxviii]

The breakdown of impairment categories among Disability Insurance beneficiaries is consistent with global health trends. According to the World Health Organization, the leading causes of disability today in most regions of the world—including the United States—are musculoskeletal impairments and mental disorders.[xxix] The rise in mental impairments around the world is often attributed to increased awareness and reduced stigma of mental illness. Likewise, the global rise in musculoskeletal impairments is attributable to the aging of the population both in the United States and globally—since the risk of experiencing musculoskeletal impairments rises sharply with age—as well as to the drop in mortality.[xxx]

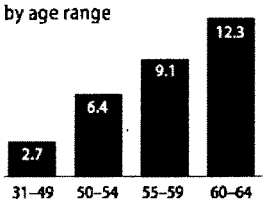
## Most beneficiaries are older and had physically demanding jobs

Most beneficiaries of Disability Insurance —7 in 10—are in their 50s and 60s, and the average age is 53. The fact that most beneficiaries are older is unsurprising given that the likelihood of disability increases sharply with age: a worker is twice as likely to experience disability at age 50 as at 40, and twice as likely at 60 as at 50.[xxxi] Before turning to Social Security, most disabled-worker beneficiaries worked at "unskilled" or "semi-skilled" physically demanding jobs.[xxxii] About half—53 percent—of disabled workers who receive Disability Insurance have a high school diploma or less.[xxxiii] About one-third completed some college, and the remaining 18 percent completed four years of college or have further higher education.[xxxiv]

**FIGURE 1**

**The likelihood of receiving Social Security Disability Insurance rises sharply with age**

Social Security Disability Insurance prevalence rates by age range




Source: Melissa M. Favreault, Richard W. Johnson, and Karen E. Smith, "How Important Is Social Security to American Workers?" (Washington: Urban Institute, 2013), available at http://www.urban.org/Uploaded-PDF/412847 How Important is social security.pdf.

## Few are able to work at all

For beneficiaries whose conditions improve, Social Security Administration policies include strong work incentives and protections to encourage beneficiaries to attempt to return to work. Beneficiaries may earn up to the substantial gainful activity level—$1,090 per month in 2015—without risking their needed monthly benefits. Beneficiaries whose conditions improve enough that they are able to earn more than the substantial gainful activity level are encouraged to work as much as they can for up to 12 months while maintaining their benefits. Those who work above the substantial gainful activity level for more than 12 months enter a nearly three-year "extended period of eligibility," during

which they receive a benefit only in the months in which they earn less the substantial gainful activity level.[xxxv] After the extended period of eligibility ends, if at any point in the next five years their condition worsens and they are not able to continue working above that level, they can return to benefits through a process called "expedited reinstatement."[xxxvi] This process allows them to restart their needed benefits without having to repeat the entire, lengthy disability-determination process.[xxxvii] These policies are extremely helpful to beneficiaries with episodic symptoms or whose conditions improve over time.

Yet, unsurprisingly given how strict the Social Security disability standard is, most beneficiaries live with such debilitating impairments and health conditions that they are unable to work at all, and most do not have earnings. According to a recent study linking Social Security data and earnings records before the onset of the Great Recession, fewer than one in five, or 19.5 percent, of beneficiaries did any work during the year.[xxxviii] The vast majority of those who worked earned very little, and just 3.9 percent earned more than $10,000 during the year—hardly enough to support oneself.[xxxix] Just 4 percent earned enough to have their benefits terminated due to earnings, and of those, about one-quarter later returned to receiving benefits.[xl]

If a significant share of beneficiaries were able to work, one would expect a sizeable percentage to take advantage of the previously described work incentives in order to maximize their earnings without losing benefits. But beneficiaries' work patterns indicate otherwise. Less than one-half of one percent of beneficiaries maintain a level of earnings just below the substantial gainful activity level.[xli] Further underscoring the strictness of the Social Security disability standard, even disabled workers who are denied benefits exhibit extremely low work capacity afterward. A recent study of workers denied Disability Insurance found that just one in four were able to earn more than the substantial gainful activity level post-denial.[xlii]

## How does the United States compare with other countries?

The Social Security disability standard is among the strictest in the industrialized world. As previously noted, the OECD describes the U.S. disability benefit system, along with those of a handful of other nations, as having "the most stringent eligibility criteria for a full disability benefit, including the most rigorous reference to all jobs in the labor market."[xliii]

Social Security Disability Insurance benefits are less generous than most other countries' disability benefit programs. With Disability Insurance benefits replacing 42 percent of previous earnings for the median earner, the United States is ranked 30th out of 34 OECD

**OECD Disability Policy Typology: Country Scores, 2007, In Descending Order**
**(OECD Average = 25.8)**

| | | | |
|---|---|---|---|
| Sweden | 37 | Belgium | 25 |
| Norway | 33 | France | 25 |
| Portugal | 33 | Greece | 25 |
| Finland | 32 | Poland | 25 |
| Germany | 32 | Austria | 24 |
| Switzerland | 32 | Czech Republic | 24 |
| Denmark | 28 | Netherlands | 24 |
| Hungary | 28 | New Zealand | 23 |
| Luxembourg | 28 | Australia | 21 |
| Mexico | 27 | Japan | 21 |
| Spain | 27 | United Kingdom | 21 |
| Ireland | 26 | Canada | 18 |
| Italy | 26 | **United States** | 17 |
| Slovak Republic | 26 | Korea | 15 |

member countries in terms of replacement rates.[xliv] Many countries' disability benefit programs replace 80 percent or more of previous earnings.[xlv]

By international standards, the United States spends comparatively little on disability benefits. In 2009, U.S. spending on Social Security Disability Insurance equaled 0.8 percent of gross domestic product, or GDP—again putting the United States near the bottom (27th out of 34 OECD member countries) in spending on equivalent programs. On average, OECD member countries spend 1.2 percent of GDP on their equivalent programs, and many—such as Denmark (2 percent), the United Kingdom (2.4 percent) and Norway (2.6 percent)—spend significantly more.[xlvi]

The share of the U.S. working-age population receiving Disability Insurance benefits—about 6 percent—is roughly on par with the OECD average of 5.9 percent.[xlvii]

In drawing international comparisons, it is well worth noting that in addition to more generous disability benefit systems with less rigorous eligibility standards, European nations tend to have universal paid leave policies, more generous health care systems, higher levels of social spending generally, and more regulated labor markets than the United States.[xlviii]

## Growth in the program was expected and is mostly the result of demographic and labor market shifts

As long projected by Social Security's actuaries, the number of workers receiving Disability Insurance has increased over time, due mostly to demographic and labor-market shifts. According to recent analysis by Social Security Administration researchers, the growth in the program between 1972 and 2008 is due almost entirely (90 percent) to the Baby Boomers aging into the high-disability years of their 50s and 60s, the rise in women's labor-force participation, and population growth.[xlix] Importantly, as early Baby Boomers have begun to age into retirement, the program's growth has already leveled off and is projected to decline further in the coming years as Boomers continue to retire.[l] Indeed the total number of beneficiaries fell last year, and the number of new applicants has declined by 14 percent since 2010.[li]

Due to the importance of these demographic factors, Social Security's actuaries analyze trends in benefit receipt using the "age-sex adjusted disability prevalence rate," which controls for changes in the age and sex distribution of the insured population, as well as for population growth. The age-sex adjusted disability prevalence rate was 4.6 percent in 2013 compared to 3.1 percent in 1980.[lii]

Key drivers of the program's growth include:

- **Aging population:** The risk of disability increases sharply with age. A worker is twice as likely to be disabled at age 50 as at 40, and again twice as likely at age 60 as at 50.[liii] Born between 1946 and 1964, Baby Boomers have now aged into their high-disability years, driving much of the growth in Disability Insurance.

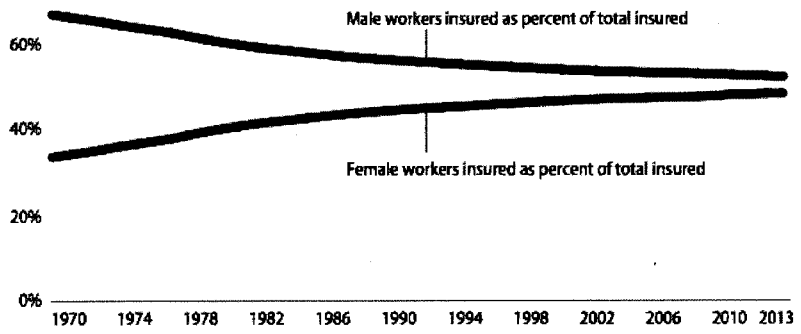
- **Increase in women's labor-force participation:** Whereas previous generations of women had not worked enough to be insured in case of disability, women today have essentially

caught up with men when it comes to being insured for benefits based on their work history.[liv]

**FIGURE 2**

**Women have caught up to men in insured status**

Number of male and female workers insured in case of disability, in thousands, 1970–2013




Source: Social Security Administration, "Estimated number of workers insured in the event of disability, by age group and sex, on December 31, 1970-2013," available at http://www.ssa.gov/OACT/STATS/table4c2D.html (last accessed June 2014).

- **Population growth**: The working-age population—ages 20 to 64—has grown significantly, by 43 percent between 1980 and 2013.[lv] The Center on Budget and Policy Priorities estimates that population growth alone—even if the population were not aging—would have resulted in an additional 1.25 million beneficiaries in 2013 compared with 1980.[lvi]

- **Women's catch-up in rates of receipt:** Just as women have caught up with men in terms of having worked enough to be insured for Disability Insurance, the gender gap in rates of receipt of benefits has closed as well. As recently as 1990, male workers outnumbered female workers by two to one, whereas today, nearly 48 percent of workers receiving Disability Insurance are women.[lvii]

- **Increase in Social Security retirement age**: The increase in the Social Security retirement age from 65 to 66, and ultimately to 67, has played a role as well, as disabled workers continue receiving Social Security Disability Insurance for longer before converting to retirement benefits when they reach full retirement age. About 5 percent of Social Security Disability Insurance beneficiaries are ages 65 and 66.[lviii]

## The Great Recession in context

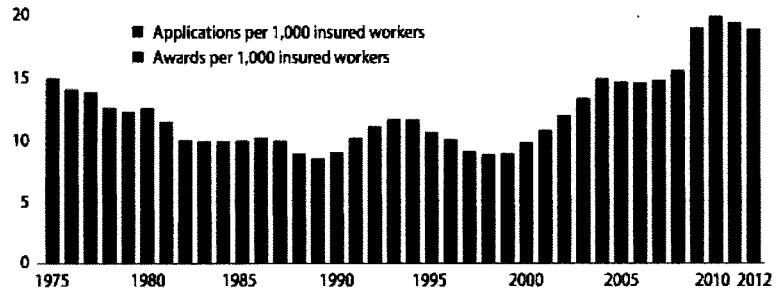
Social Security's actuaries note that the main effect of the recent economic downturn was lower revenue through payroll tax contributions—not an increase in beneficiaries.[lix] While recessions are typically associated with sharp increases in *applications* for Social Security Disability Insurance, they have a much smaller impact on *awards*. The most recent downturn was no exception, and Social Security's actuaries estimate that just 5 percent of the program's growth from 1980 to 2010 is due to the recession,[lx] likely due to workers with disabilities being disproportionately laid off from employer payrolls when times got tight.

It is important to note that while applications increased during the Great Recession, the award rate—the share of applications approved for benefits—declined,[lxi] indicating that applicants who did not meet the rigid disability standard were screened out. A study by Social Security's watchdog examined the 11 states with the highest unemployment rates and found that award rates had dropped in all of them.[lxii]

Moreover, a recent National Bureau of Economic Research study found "no indication that expiration of unemployment insurance benefits causes Social Security Disability Insurance applications."[lxiii] Furthermore, a recent report by the White House Council of Economic Advisers examining labor force participation trends since 2007 found that the increase in the number of disabled workers receiving Disability Insurance has had a minimal impact on labor force participation, noting: "in fact, if anything, the increase in disability rolls...have been [sic] somewhat lower than one would have predicted given the predicted cyclical and demographic effects."[lxiv]

FIGURE 3

**Applications and awards, disabled workers, 1975–2012**




Source: Social Security Administration, "Disabled Workers Applications For Disability Benefits & Benefit Awards," available at http://www.ssa.gov/oact/STATS/table6c7.html (last accessed June 2014).

## No surprise that action is needed to address finances, and routine action would put the entire Social Security system on sound footing for the next two decades

It comes as no surprise—and presents no crisis—that action is needed to address Social Security Disability Insurance's finances by late 2016. In 1995, Social Security's actuaries projected that the Disability Insurance trust fund would be able to pay all scheduled benefits until 2016, the OASI trust fund until 2031, and the combined trust funds until 2030.[lxv] The projections in the 2013 Social Security Trustees Report look remarkably similar, with Disability Insurance expected to remain solvent until 2016, OASI until 2035, and the combined funds until 2033.[lxvi] If policymakers did nothing, the Disability Insurance fund would be able to pay 80 percent of promised benefits after 2016—and beneficiaries would face a 20 percent across-the-board cut in their already modest benefits.[lxvii]

Furthermore, the present situation is nothing new. While the OASI fund and the Disability Insurance fund are technically separate, they are typically considered together due to the interrelatedness of Social Security's programs. For example, Social Security's programs share the same benefit formula, beneficiaries regularly move between programs,[lxviii] and changes to one program—such as raising the retirement age—affect both funds.

Since Social Security Disability Insurance was established in 1956, Congress has repeatedly rebalanced the OASI and Disability Insurance trust funds to keep both on sound footing amid demographic shifts and other changes. Rebalancing—by adjusting the share of payroll tax contributions that go into each fund—has occurred in a bipartisan manner 11 times over the years, with additional revenues being directed to the OASI fund about half the time, and to the Disability Insurance fund about half the time.[lxix] Congress has never allowed a drop in scheduled benefits to occur. Policymakers should again enact a modest, temporary reallocation of the 6.2 percent payroll tax rate between OASI and Disability Insurance to equalize the solvency of the two funds.

### 1983 Social Security reforms worsened Social Security Disability Insurance's financial health to an extent that the 1994 adjustments only partially addressed

The last round of major changes to Social Security occurred in 1983. Notable components of the 1983 legislation included an increase in the Social Security retirement age (from 65 to 67) and a cut in the share of the payroll tax allocated to the Disability Insurance trust fund.[lxx] At the time of the 1983 changes, the OASI fund was facing insolvency, while the Disability Insurance fund was healthy.[lxxi]

The impact of these changes on the Disability Insurance trust fund has been significant. As noted above, increasing the full retirement age worsens the state of the Disability Insurance trust fund since it causes workers to remain on Disability Insurance for longer before converting to Social Security retirement benefits. Additionally, the cut in the share of the payroll tax

allocated to Disability Insurance—which had been on schedule to rise from 0.825 to 1.1 percent in 1990—has caused the Disability Insurance fund to receive significantly less revenue in the years since.[lxxii]

In 1994, spurred by the worsening state of the Disability Insurance fund, Congress increased Disability Insurance's share of the payroll tax to 0.9 percent—an improvement over the 0.5-0.6 percent the fund had been receiving after the 1983 legislation, but still significantly lower than the 1.1 percent it had been scheduled to receive prior to the 1983 changes.[lxxiii] Disability Insurance's share of the payroll tax remains at 0.9 percent. Had it risen to 1.1 percent as scheduled, we would not be where we are today, and action to shore up the fund would not be needed by late 2016.

## Traditional, routine step would put entire Social Security system on sound footing for the next two decades

As noted above, reallocation of payroll tax rates has been a traditional, noncontroversial action, occurring repeatedly, as needed, over the course of the six decades since Social Security Disability Insurance was established. And as long expected, similar action is again required by late 2016. The reallocation plan outlined in the President's FY 2016 budget proposal would ensure that both funds remain fully solvent until 2033.[lxxiv] Importantly, reallocation can be done without increasing taxes or cutting benefits, and would keep the combined Social Security trust funds on their current course. Under current law, as well as under reallocation, the combined trust funds will be able to pay all scheduled benefits until 2033.[lxxv]

| Social Security Payroll Tax Rates | | | | | | | |
|---|---|---|---|---|---|---|---|
| Calendar Years | Employees and employers each | | | | Self-employed | | |
| | OASDI | OASI | DI | | OASDI | OASI | DI |
| *Rates scheduled under present law* | | | | | | | |
| 2015+ | 6.2% | 5.3% | 0.9% | | 12.4% | 10.6% | 1.8% |
| | | | | | | | |
| *Rates proposed in the President's FY2016 Budget* | | | | | | | |
| 2015 | 6.2% | 5.3% | 0.9% | | 12.4% | 10.6% | 1.8% |
| 2016-20 | 6.2 | 4.85 | 1.35 | | 12.4 | 9.7 | 2.7 |
| 2021+ | 6.2 | 5.3 | 0.9 | | 12.4 | 10.6 | 1.8 |
| | | | | | | | |

Note: Rates for 2015 and years after 2020 are unchanged under the proposal.

While the combined trust funds are set to remain on sound footing for the next two decades, action will be needed sometime during that time period to ensure the long-term solvency of the overall Social Security system. But in the near term, as Secretary of the Treasury Jacob Lew has testified before this Committee, "There is only one solution the technical experts believe can work in the timeframe between now and 2016. And that's a reallocation of the tax rate, as

we've done in the past."[lxxvi] And as Secretary of the Office of Management and Budget Shaun Donovan testified just last week before this Committee, "It's actually been done both ways, from disability to the other trust fund and back to Social Security. And so we think this is the most simple and critical way."[lxxvii]

Looking past 2016, there are a number of options for ensuring the long-term solvency of the overall Social Security system without cutting already modest benefits—something that polls consistently confirm most Americans oppose.[lxxviii] One frequently discussed policy option is eliminating the cap on earnings that are subject to payroll taxes so that the 5 percent of workers who earn more than the cap would pay into the system all year as other workers do. A recent survey conducted by the nonpartisan National Academy of Social Insurance found overwhelming support for a reform package that included this and other revenue-enhancing features, while also boosting benefits.[lxxix] An array of legislation introduced within the past two years has included this and other approaches to strengthen Social Security, reflecting their growing popularity.[lxxx]

## Income inequality has significantly worsened Social Security's financial outlook

Over the past three decades, rising income inequality has taken a substantial toll on Social Security's financial outlook. Those at the top of the income spectrum have seen tremendous gains, while most Americans have watched their wages decline or stagnate amid rising costs. In the wake of the Great Recession, the top 1 percent of households captured roughly 76 percent of inflation-adjusted income gains between 2009 and 2013.[lxxxi]

Much of the leap made by the very rich is attributable to nonwage forms of income such as capital gains, but huge disparities also persist when looking only at wages, which form the basis for Social Security tax revenues because payroll taxes only apply to wage income. In 2013, for example, the top 1 percent of earners took home about 12.9 percent of the nation's total wage income in 2013—nearly as much as the share received by the entire bottom half of workers, who captured approximately 13.7 percent of wage income.[lxxxii] This growing divide in wages—combined with the fact that wages in excess of the taxable maximum are exempt from payroll taxes—means that millionaire and billionaire earners stop contributing to Social Security early in the year, while the average worker contributes all year long. In 2015, individuals with wage incomes of $1,000,000 stop contributing on February 12; those with higher incomes stop contributing sooner.[lxxxiii]

Meanwhile, although productivity growth for American workers has more than doubled over the past two decades, incomes for the bottom 50 percent of workers have barely increased in inflation-adjusted terms, and they have actually declined for the bottom 20 percent.[lxxxiv] In short, most American workers have seen their wages decline or remain stagnant, while they have become twice as good at doing their jobs. At the same time, the costs of goods and services that support a middle-class lifestyle have risen significantly.[lxxxv]

Recent analysis published by the Center for American Progress shows what the assets of the combined Social Security trust funds would be today if the average worker's wages had kept pace with productivity growth between 1983 and 2013. We find that this wage growth would have increased the trust funds' assets by $753.8 billion.[lxxxvi] The analysis also demonstrates what the trust funds would look like today if the maximum taxable wage base had remained fixed at 90 percent of earnings over the same time period. In this case, the trust funds would have at least an additional $1.1 trillion.[lxxxvii]

This new analysis comes on top of projections made by the Social Security trustees in their annual report, finding that raising the cap to cover 90 percent of earnings—starting in 2015—would on its own close more than one-quarter of the expected 75-year shortfall in the combined trust funds.[lxxxviii]

This analysis demonstrates that while policymakers cannot undo the past, they can take action to improve Social Security's fiscal outlook by implementing policies that boost wages, combat rising inequality, and modernize the program's revenue structure to reflect today's economy.[lxxxix]

### Adequate administrative funding is needed to ensure program integrity

The Social Security Administration, or SSA, operates on an administrative budget equal to about 1.4 percent of the benefits it pays out. The agency requires sufficient administrative funding not only to process applications for and payment of benefits, but also to perform important program integrity work, such as pre-effectuation reviews of disability determinations and continuing disability reviews to ensure benefits are paid only as long as the individual remains eligible.

In recent years, the agency was significantly underfunded. It received more than one billion dollars less than the President's request in FY 2011, 2012, and 2013, and appropriations for its program integrity activities nearly half a billion dollars below the levels authorized by the Budget Control Act of 2011, in FY 2012 and 2013.[xc] As a result, during a time of increasing workload due to the Baby Boomers entering retirement and their disability-prone years, the agency lost over 11,000 employees—a 13 percent drop in its workforce—hampering the agency's ability to serve the public and keep up with vital program integrity activities.[xci] In a positive step, the budget bill enacted in 2014 provided the agency with full funding of the FY 2014 Budget Control Act level for program integrity activities.[xcii]

Adequate administrative funding is essential for SSA to make timely and accurate benefit payments[xciii] and perform vital program integrity work. Continuing disability reviews are estimated to save some $10 in benefits for every $1 spent on reviews, yet the agency reports a backlog of nearly 1.3 million reviews due to inadequate funding.[xciv] As policymakers consider options for ensuring Social Security's solvency, providing the agency with adequate administrative funding to ensure program integrity presents a common-sense step.

## Conclusion

In closing, I would like to underscore the importance of policymakers taking the traditional, routine step of rebalancing the Social Security trust funds prior to the Disability Insurance fund's depletion. In the words of Robert M. Ball, who served as Commissioner of Social Security from 1962-1973, under Presidents Kennedy, Johnson and Nixon: "I see little merit in doing anything less than financing OASI and DI on approximately equal terms. But the most important point, of course, is [...] to maintain confidence in the Social Security system as a whole."[xcv]

Social Security Disability Insurance has been a core pillar of our nation's Social Security system for nearly six decades, offering critical protection to nearly all American workers and their families in the event of a life-changing disability or illness. The program's eligibility criteria are restrictive and benefits are modest, but for those who receive benefits, it is nothing short of a lifeline, providing critical economic security when it is needed most. Policymakers have many options to ensure long-term solvency of the overall Social Security system, and a window of nearly 20 years to arrive at a package that will accomplish that goal. In the meantime, policymakers should enact a simple payroll tax reallocation to keep Disability Insurance on sound footing past 2016. Failure to do so would be nothing short of devastating to millions of disabled workers and their families—and would erode Americans' confidence in the Social Security system.

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[i] U.S. Social Security Administration, "Presidential Statement on Signing the Social Security Act. August 14, 1935," available at http://www.ssa.gov/history/fdrstmts.html#signing (last accessed July 2014).

[ii] In 1948, the Advisory Council on Social Security concluded that "present methods of protection against income loss from permanent and total disability are not adequate. More than 60 life-insurance companies offer such protection, but few individuals purchase it. The cost is high, the terms on which it is sold are restrictive, and most life-insurance companies no longer follow aggressive sales policies with respect to permanent and total disability insurance." 1948 Advisory Council Report, *Recommendations for Sociol Security Legislation: The Reports of the Advisory Council on Social Security to the Senate Committee on Finance* (Government Printing Office, 1949), p. 69, available at http://www.ssa.gov/history/pdf/48advise6.pdf.

[iii] U.S. Social Security Administration, "Fact Sheet on the Old-Age, Survivors, And Disability Insurance Program."

[iv] Ibid.

[v] Ibid. For veterans figure, see Bailey and Hemmeter, "Characteristics of Noninstitutionalized DI and SSI Program Participants, 2010 Update."

[vi] The payroll tax cap is adjusted annually. It is $118,500 for 2015. Social Security Administration, "Contribution and Benefit Base," available at http://www.ssa.gov/oact/COLA/cbb.html#Series.

[vii] U.S. Social Security Administration, "Social Security Tax Rates," available at http://www.ssa.gov/oact/progdata/oasdiRates.html (last accessed July 2014).

[viii] U.S. Social Security Administration, "Monthly Statistical Snapshot, December 2013," available at http://www.ssa.gov/policy/docs/quickfacts/stat_snapshot/2013-12.html (last accessed July 2014).

[ix] Bailey and Hemmeter, "Characteristics of Noninstitutionalized DI and SSI Program Participants, 2010 Update."

[x] Authors' calculation based on Ibid.

[xi] There are exceptions to the two-year waiting period for individuals with amyotrophic lateral sclerosis, or ALS, and end-stage renal disease. Beneficiaries with very low incomes and assets may qualify for Medicaid during the two-year waiting period for Medicare.

[xii] Bureau of Labor Statistics, "Table 16. Insurance benefits: Access, participation, and take-up rates, civilian workers, National Compensation Survey, March 2012," available at http://www.bls.gov/ncs/ebs/benefits/2012/ownership/civilian/table12a.htm (last accessed July 2014).

[xiii] Ibid.

[xiv] Ibid.

[xv] This is the statutory definition of disability set forth in the Social Security Act, 42 U.S.C. 416 (i)(1). Substantial gainful activity is set at a different level for individuals who are blind. For 2014, this amount is $1,800. Social Security Administration, Substantial Gainful Activity, available at http://www.socialsecurity.gov/oact/cola/sga.html (last accessed July 2014).

[xvi] *Code of Federal Regulations,* title 20, sec. 416 (960)

[xvii] National Academy of Social Insurance, "What is Social Security Disability Insurance?", available at http://www.nasi.org/learn/socialsecurity/disability-insurance (last accessed May 2013).
[xviii] Organisation for Economic Co-operation and Development, "Sickness, Disability, and Work: Breaking the Barriers: A Synthesis of Findings across OECD Countries."
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[lxvii] Virginia P. Reno, Elisa A. Walker, and Thomas A. Bethell, "Social Security Disability Insurance: Action Needed to Address Finances" (Washington: National Academy of Social Insurance, 2013), available at http://www.nasi.org/sites/default/files/research/SS_Brief_041.pdf.

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[lxix] U.S. Social Security Administration, "Social Security: Summary of the Major Changes in the Cash Benefits Program."

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[lxxv] The Board of Trustees, Federal OASI and Federal DI Trust Funds, *The 2013 Annual Report of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Fund.*

[lxxvi] U.S. Secretary of the Treasury Jacob Lew testified at a March 2014 budget hearing that "there's only one solution the technical experts believe can work in the timeframe between now and 2016. And that's a reallocation of the tax rate, as we've done in the past." Jacob Lew, Testimony before the U.S. Senate Budget Committee, March 6, 2014. Video of Secretary Lew's testimony available at http://www.bloomberg.com/video/lew-testifies-before-senate-on-obama-budget-plan-s0NJ4eyFTSmkoX19pfkdoA.html.

[lxxvii] Testimony of Shaun Donovan before the Senate Budget Committee, February 3, 2015. Video of Secretary Donovan's testimony available at http://www.budget.senate.gov/republican/public/index.cfm/hearing-schedule?ID=e8bab703-bf00-49a2-80a5-456ebcc9b54b.

[lxxviii] Most recently, a Pew survey released in June 2014 found that 67 percent of Americans, and large majorities of Americans of both political parties, oppose cutting Social Security benefits in any way. Pew Research Center, "Political Polarization in the American Public" (2014), available at http://www.people-press.org/files/2014/06/6-12-2014-Political-Polarization-Release.pdf.

[lxxix] The most popular reform package, preferred to the status quo by seven in 10 individuals polled—across generations, income levels, and political affiliations--would: 1) Gradually, over 10 years, eliminate the cap on earnings taxed for Social Security; 2) gradually, over 20 years, raise the Social Security tax that workers and employers each pay from 6.2% of earnings to 7.2%; 3) increase the cost of living adjustment formula, or COLA; and 4) increase Social Security's minimum benefit. Jasmine V. Tucker, Virginia P. Reno and Thomas A. Bethell, "Strengthening Social Security: What Do Americans Want?" (Washington: National Academy of Social Insurance, 2013), available at http://www.nasi.org/sites/default/files/research/What_Do_Americans_Want.pdf.

[lxxx] Examples include: the Strengthening Social Security Act of 2013, S. 567 and H.R. 3118, introduced by Sen. Tom Harkin (D-IA) in the Senate and Rep. Linda Sanchez (D-CA) in the House; the Protecting and Strengthening Social Security Act, S. 308 and H.R. 649, introduced by Sen. Mark Begich (D-AK) in the Senate and Rep. Theodore Deutch (D-FL) in the House; the Keeping Our Social Security Promises Act, S. 500, introduced by Sen. Bernie Sanders (I-VT), and the No Loopholes in Social Security Act, H.R. 1029, introduced by Rep. Peter DeFazio (D-OR); the Social Security Enhancement and Protection Act of 2013, H.R. 1374, introduced by Rep. Gwen Moore (D-WI); the RAISE Act, S. 2455, introduced by Sens. Begich and Patty Murray (D-WA).

[lxxxi] Rebecca Vallas and others, "The Effect of Rising Inequality on Social Security," Center for American Progress (February 10, 2015), available at https://cdn.americanprogress.org/wp-content/uploads/2015/02/SocialSecurity-brief2.pdf.

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[lxxxvi] Vallas and others, "The Effect of Rising Inequality on Social Security."
[lxxxvii] Ibid.
[lxxxviii] See Provision E3.1 in Social Security Administration, Office of the Chief Actuary, "Summary of Provisions That Would Change the Social Security Program" (2014), available at http://www.ssa.gov/oact/solvency/provisions/summary.pdf.
[lxxxix] For a detailed discussion of policies to ensure inclusive prosperity, see Lawrence H. Summers and Ed Balls, co-chairs, "Report from the Commission on Inclusive Prosperity," (Washington: Center for American Progress, 2015), available at https://www.americanprogress.org/issues/economy/report/2015/01/15/104266/report-of-the-commission-on-inclusive-prosperity/. Additionally, as Christian E. Weller and Farah Z. Ahmad point out in a recent Center for American Progress report, lifting wages, bolstering employment, and reducing poverty in our nation's rapidly growing communities of color would provide a particularly strong boon to Social Security's financial outlook. See Weller and Ahmad, *A Win-Win for An All-In Nation* (Washington: Center for American Progress, 2014), available at https://cdn.americanprogress.org/wp-content/uploads/2014/08/SocialSecurity-report2.pdf.
[xc] See Testimony of Carolyn Colvin, Acting Commissioner of Social Security, before the U.S. House of Representatives, Committee on Ways and Means, Subcommittee on Social Security, February 26, 2014, available at http://www.ssa.gov/legislation/testimony_022614.html.
[xci] Ibid.
[xcii] Ibid.
[xciii] Adequate administrative funding is also needed for SSA to process beneficiaries' earnings reports and adjust benefits timely for beneficiaries who work. The agency reports that the average processing time for earnings reports is 270 days, which results in needless improper payments, and can be tremendously disruptive to beneficiaries who are all of a sudden—through no fault of their own—hit with an overpayment that they are required to repay.
[xciv] Ibid.
[xcv] Testimony of Robert M. Ball before the U.S. House Committee on Ways and Means, Subcommittee on Social Security, April 22, 1993, cited in Reno, Walker, and Bethell, "Social Security Disability Insurance: Action Needed to Address Finances."

**Submission for the Record**
**From: Ranking Member Bernard Sanders**

**Hearing on "The Coming Crisis:**
**Social Security Disability Trust Fund Insolvency"**
**February 11, 2015**
**Senate Budget Committee**

Joint Statement for the Record

Of
Paralyzed Veterans of America

And

Vietnam Veterans of America

To the

Senate Committee on the Budget

Concerning the Social Security Trust Fund

February 11, 2015

Paralyzed Veterans of America (PVA) and Vietnam Veterans of America (VVA) appreciate the opportunity to share with the Senate Budget Committee this statement to its hearing, "The Coming Crisis: Social Security Disability Trust Fund Insolvency." PVA is the only Congressionally-chartered veterans' service organization devoted solely to representing veterans with spinal cord injury and/or dysfunction. Since 1947, PVA has been a strong advocate for programs and services affecting the quality of life of its members. Founded in 1978, Vietnam Veterans of America is the only national Vietnam veterans' organization congressionally chartered and exclusively dedicated to Vietnam-era veterans and their families. Together, our organizations represent millions of Americans for whom Social Security is a foundation of their economic security.

According to the Social Security Administration, there are about 9.4 million military veterans receiving Social Security benefits. This means that nearly one out of every four adult Social Security beneficiaries has served in the United States military. Millions of men and women who raised their right hand and took the oath to protect democracy also paid into a system that promised them financial support upon reaching retirement age or becoming too disabled to work. Most of these veterans are over age 62 and had served during the Vietnam War or earlier. They served their country and upheld their part of the deal; now it seems our government's part of the transaction may have been written with disappearing ink.

In a rules change adopted on the opening of the 114th Congress, the House of Representatives created new hurdles to fixing the Social Security system and exposed disability insurance benefits to the possibility of a 20 percent reduction in 2016. More than ten times since 1968, it has been necessary for Congress to adjust the formula allocating payroll taxes between the Old Age, Survivors and Disability Insurance trust funds to keep the overall Social Security system in balance. This has always been done in a bipartisan manner and has kept America's promise to veterans receiving Social Security benefits while sustaining the system for decades. If this simple rebalancing is used again to put the entire Social Security program on an equal footing, benefits will remain payable at least until year 2033. This would provide time for a thorough, thoughtful and much needed discussion about the future of the overall Social Security system, including both solvency and benefit adequacy. Without this reallocation, Social Security disability insurance benefits face the aforementioned 20 percent cut in 2016. However, the House leadership has created a Hobson's choice with its adoption of a rule that states: "We will prevent the 20 percent cut in disability benefits but only if we cut benefits or raise revenues." And the likelihood of the latter action occurring going into the 2016 election year is minimal.

With the country still recovering from an era that saw the terrorist attacks on September 11, 2001 followed by the longest war in its 235-year history, PVA would assume that any benefits that accrue to our nation's veterans, particularly the most vulnerable, are worthy of preservation. Those who volunteer to serve in our military have a right to expect that those Americans they protect will, in turn, afford them some semblance of protection when they need it. Otherwise, military service will not seem as attractive a career option. In World War II, 11.2 percent of the nation served during the four years of war. In Vietnam, 4.3 percent served during the 12 years of war. Since 2001, only 0.45 percent of the American population has served in the wars in Iraq and Afghanistan. Eroding the safety net to which service members contributed is no way to ensure an adequate fighting force for future conflicts.

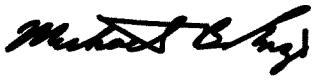
By rebalancing the Social Security Trust Funds using a simple adjustment in the amount of payroll taxes going into the retirement and survivors and disability trust funds, and doing so without any new taxes or cuts in benefits, Congress can ensure the stability of the system for the next 18 years and the readiness of our military by making service an attractive career option. But if Congress stays on its present course, we may get neither.

We urge Congress to adopt a clean reallocation of payroll taxes between the two Social Security trust funds to avoid a 20 percent reduction in disability benefits in 2016.

We thank you for the opportunity to offer our views for the record and we would be happy to answer any questions the Committee may have.

**Submission for the Record**
**From: Ranking Member Bernard Sanders**

**Hearing on "The Coming Crisis:**
**Social Security Disability Trust Fund Insolvency"**
**February 11, 2015**
**Senate Budget Committee**



Senator Orrin Hatch
Statement on the Senate Floor
On the Disability Insurance Trust Fund Reserve Depletion
February 10, 2015

Mr./Mdm. President, I rise to speak about the impending exhaustion of the disability trust fund administered by the Social Security Administration.

The Social Security system contains two important programs. One is the Old-Age and Survivors Insurance – or OASI – program, often referred to as the retirement program. That program provides income to insured workers and their families at retirement or death, based on their payroll tax contributions to the OASI trust fund.

The other is the Disability Insurance – or DI – program, which provides income to insured workers who suffer from a disabling condition, based on their payroll tax contributions to the DI trust fund.

Unfortunately, both trust funds face trillions of dollars in unfunded obligations.

Each trust fund is legally distinct, though they have been comingled in the past into an imaginary fund labeled the OASDI trust fund or mingled with the General Fund.

Reserves in the DI trust fund are projected to be exhausted sometime late in calendar year 2016, after which beneficiaries face benefit cuts of around 20 percent. The DI program alone faces unfunded obligations over the next 75 years of more than $1.2 trillion.

Reserves in the OASI trust fund are projected to be exhausted in 2034, after which retirees and their survivors face benefit cuts of around 25 percent. The retirement program alone faces unfunded obligations of around $9.4 trillion over the next 75 years.

Financial operations of the OASI and DI trust funds are overseen by a Board of Trustees composed of six members. Four of them serve based on their positions in the federal government and two are appointed by the President and confirmed by the Senate.

Currently, Treasury Secretary Lew, Labor Secretary Perez, HHS Secretary Burwell, and Social Security's Acting Commissioner Colvin serve on the board. This is not what anyone would consider a band of fiscal hawks. Yet, in their most recent report, those Trustees – who are, once again, high-ranking officials in the Obama Administration – urged Congress take action "as soon as possible to address the DI program's financial imbalance."

Those are pretty clear words.

Those are not the words of any Republican trying to manufacture a crisis. They are not the words of any Republican trying to hold anyone or anything hostage, as some of my friends on the other side have claimed. Rather, they come from Obama administration officials who, in their roles as trustees, are forced to acknowledge reality.

Mr./Mdm. President, I want to take this opportunity to once again urge the administration and my colleagues – particularly those on the other side of the aisle – to begin to work with me to find solutions that will at least begin to chip away at the known financial imbalances in the DI trust fund so that we can prevent the coming benefit cuts.

Last year, in a Finance Committee hearing on the DI program, I made clear my willingness to work with anyone in Congress or the administration to examine options and ideas about the DI program before the DI trust fund becomes exhausted. Indeed, I have been trying for years to get the administration to engage on this issue. Unfortunately, to date, I have heard nothing from the administration and very little from my friends on the other side of the aisle about this issue.

What I have heard is fear-mongering about supposed Republican plans to slash benefits or engineer a false crisis or hold beneficiaries hostage. I'm not exaggerating, Mr./Mdm. President, those are the very words they've used.

In budget after budget, the President has all but ignored Social Security in general, and the DI program in particular. The President's budgets generally only include calls for more administrative funding for the Social Security Administration or the occasional idea for an experimental trial.

After years of my asking the administration to engage on the DI program's financial challenges, the President quietly inserted his policy position on DI just recently. And, with his FY 2016 budget, we finally learned that the President supports a "stand-alone reallocation" of incoming tax receipts away from the retirement trust fund over to the disability insurance trust fund.

Oddly, one of the objectives appears to be to make a reallocation so that both the disability and the retirement trust funds become exhausted in the same future year, which, according to the budget, is 2033.

Needless to say, having a joint trust fund exhaustion as a target doesn't solve any fundamental financial problem facing the long-run financial challenges of Social Security. Moreover, it takes away any urgency for Congress to improve the disability program now, before it becomes harder to do so down the road.

By stand-alone reallocation, the administration means that it wants to shift funds from the retirement fund to the DI fund for with no accompanying policy changes of any kind.

No change in overall payroll taxes.

No change in benefits.

No substantive changes in program integrity, aside from the persistent call for more mandatory administrative funds.

Not even a study.

Mr./Mdm. President, there have recently been many misconceptions and misstatements about the idea of a reallocation in general and a stand-alone reallocation in particular.

The last time Congress made a reallocation from the retirement trust fund to the DI trust fund was in 1994. At that time, Social Security trustees wrote the following about the reallocation and the DI trust fund:

"While the Congress acted this past year to restore its short-term financial balance, this necessary action should be viewed as only providing time and opportunity to design and implement substantive reforms that can lead to long-term financial stability..."

Unfortunately, those reforms never came. And now, also unfortunately, the President wants to tell the American people same story: Punt now to provide time for later action.

In addition, the financial challenges facing Social Security are very different from past trust fund account reshuffling, including the one in 1994.

As the public trustees of the Social Security trust funds wrote just last year:

"The present situation is very different from that of 1994...The DI Trust Fund's impending reserve depletion signals that the time has arrived for reforms that strengthen the financing outlooks for OASI and DI alike."

Mr./Mdm. President, some of my friends on the other side of the aisle say that we have had many reallocations between the DI and OASI trust funds in the past and that it's just ordinary housekeeping, or a technical change. It's something we do all the time, they say, so there's nothing really to see here.

True, there have been trust fund reallocations in the past.

Sometimes from OASI to DI.

Sometimes the other way around.

Sometimes with overall payroll tax rate changes, and sometimes not.

But, there has never – let me repeat that, Mr./Mdm. President – NEVER been a standalone reallocation from the retirement to the disability trust fund.

Most people who would dispute this talk about the reallocation of 1994, which I mentioned earlier.

But, if the 1994 reallocation is somehow to be considered a model of ordinary housekeeping that we should repeat today, I think it is a bad model for the reasons I just identified. Following that model, we would defer action until later, all the while claiming that real changes were on the horizon. And, following that model, we would continue to do nothing to place Social Security on a more stable financial footing.

Moreover, thinking of reallocation as just a normal way of doing business raises many questions.

Why was a separate DI trust fund set up to begin with?

Why do we even call them trust funds, if they are merely fungible accounting devices?

Why not merge the OASI and DI funds and call them the singular Social Security trust fund?

More generally, given the recent, stimulus-inspired mingling of General Fund revenues with the OASI and DI trust funds, why have Social Security trust funds at all?

And, if historical reallocations are to be used to guide what we should do today, then perhaps the recent reallocations from the general fund to both the OASI and DI trust funds, having been the most recent historical reallocation episodes, should be the most prominent precedents.

Mr./Mdm. President, when circumstances make us focus on the solvency of any trust fund, there are two options.

Option one – we can face up to known financial challenges, examine what can be done about them in a bipartisan way, and try to enact solutions.

Option two – we can kick the proverbial can further down the road by taking the most expedient route to reshuffle resources temporarily in order to get the problem out of the way in the short term.

Unfortunately, the President and his allies here in Congress seem to prefer the latter, kick-the-can strategy. This is especially disappointing given what the President said about Social Security when he took office in 2009.

At that time, the President said about Social Security: "What we have done is kicked this can down the road. We are now at the end of the road and are not in a position to kick it any further. We have to signal seriousness in this by making sure some of the hard decisions are made under my watch, not someone else's."

Well, the President has been on watch for six years now. And, if we look at his administration's proposed solution to the coming DI trust fund exhaustion, he seems more than content to push ANY hard decisions off until his term is over. President Obama now not only wants to kick the can down the road, but he also wants to do it in a way that has never been done before.

Mr./Mdm. President, elementary budget arithmetic makes clear that you simply cannot strengthen the financial outlooks for our two Social Security programs and their trust funds simply by shifting resources from one to the other. Indeed, Director Elmendorf of the nonpartisan Congressional Budget Office recently said: "if you want to help both programs you're not going to accomplish that by just moving money around between them."

Rather than engaging in yet another unnecessary partisan battle, we need to take this opportunity to work together to see what can be done in a bipartisan way to address the impending exhaustion of reserves in the DI trust fund. Once again, I urge the administration and my friends on the other side of the aisle to work with me on this issue.

Mr./Mdm. President, I'll have more to say on this issue in the coming days. For now, I yield the floor.

**STATEMENT FOR THE RECORD BY**
**MAX RICHTMAN**
**PRESIDENT AND CEO**
**NATIONAL COMMITTEE TO PRESERVE SOCIAL SECURITY AND MEDICARE**
**COMMITTEE ON THE BUDGET**
**UNITED STATES SENATE**
**HEARING ON**
**"THE COMING CRISIS: SOCIAL SECURITY DISABILITY TRUST FUND INSOLVENCY"**
**FEBRUARY 11, 2015**

Chairman Enzi and Ranking Member Sanders:

On behalf of the millions of members and supporters of the National Committee to Preserve Social Security and Medicare, I want to thank Chairman Michael Enzi and Ranking Member Bernie Sanders for holding this hearing entitled "The Coming Crisis: Social Security Disability Trust Fund Insolvency."

While we regret the mischaracterization chosen by the Committee to describe this hearing, and by implication the current situation with regard to the Social Security Disability Insurance (SSDI) trust fund, we encourage Committee Members to work together to resolve this critically important issue. The economic well-being of the 11 million disabled workers and their family members who receive DI benefits each month depends on all of the Congress working together in a bipartisan fashion.

As far back as 1995, the SSDI trust fund has been projected to face a funding shortfall within the next few years. The reasons for this, which I will discuss in more detail later, have been well known for many years, are primarily demographic in nature and are expected to stabilize in the near future.

The 2014 report of the Social Security Trustees projects that the DI trust fund will be substantially depleted sometime in late 2016. In addition, the trustees reported that the income to the DI trust fund at that time will equal only about 80 percent of the trust fund's obligations. Without action by Congress, in 2016 disability benefits that are currently being paid to about 11 million disabled workers and their dependents will either be delayed or will be reduced across-the-board by 20 percent.

This is a heavy burden on the minds of these millions of disabled Americans who constitute some of the most vulnerable members of our society. Congress should take action now to ease that burden by rebalancing the revenue flow into the DI Trust Fund so that it remains able to pay all benefits it owes to disabled beneficiaries and to do so on time.

This rebalancing has been done a total of eleven times since the DI trust fund was established in 1956, and can be done today without compromising the ability of the overall Social Security

program to pay benefits for nearly 20 years. Rebalancing should be done now and it should be done on a bipartisan basis, as all of the prior rebalancing decisions have been made.

**Importance of Disability Insurance to the American People**

Social Security provides peace of mind for all Americans. Not only does it provide a foundation for a secure retirement, it also protects nearly all American workers and their families against the possibility of a life-changing disability or illness that prevents them from working.

The peace of mind provided by SSDI is even more important given the harmful effect of the near total disappearance of employer-provided pensions. Compounding the problem is the impact of the recent economic downturn on Americans' ability to save for retirement, especially when an individual's working years have been shortened by an unexpected onset of disability.

The U.S. Census Bureau estimates that about 57 million Americans—one in five—live with disabilities. Of these, about 38 million, or 1 in 10, have a severe disability. Only those with the most limiting impairments receive support from Social Security.

SSDI currently pays benefits to 8.9 million disabled workers and two million spouses and children. SSDI beneficiaries include more than a million military veterans, 4.4 million women, 700,000 widow(ers), 1.8 million African Americans and one million Hispanics.

Benefits paid by SSDI are modest but vitally important to the workers and families who receive them. The average monthly benefit for a disabled worker is about $1,165, just over the federal poverty line. The importance of these benefits is illustrated by the fact that about 1 in 3 disabled Americans have no other sources of income.

SSDI keeps millions of Americans out of poverty and homelessness. Poverty rates are substantially higher for people who report significant disabilities but are not receiving SSDI benefits than for people who have been receiving SSDI benefits for at least five years. Without SSDI, an estimated 50 percent of beneficiaries would live in poverty. Even with benefits, it is estimated that about 1 in 5 SSDI beneficiaries live in poverty.

Alternatives to SSDI are limited. According to the Department of Labor, only about 1 in 3 civilian workers has long-term disability insurance through their employer, and the benefits these policies provide are often less adequate than the protections provided by Social Security. It has been estimated that in order to replace the family protections provided by Social Security, individuals would have to purchase life insurance policies with a face value of nearly $500,000. The premiums on such policies would cost families thousands of dollars each year.

**The Current Shortfall is the Product of Known Demographic Trends**

As far back as 1995, the Social Security trustees projected that the DI trust fund's outlays would exceed revenues starting in 2016. The most recent Trustees Report, released in May 2013, confirms this projection. Moreover, it estimates that after the DI trust fund is depleted, revenue coming into the DI trust fund will equal only 80 percent of the fund's benefit obligations. These projections are consistent with those made recently by the Congressional Budget Office.

What accounts for these developments? For decades, demographic shifts have been underway that have led to increases in the number of SSDI beneficiaries with corresponding increases in the cost of the program. The following factors account for most of the growth in the number of individuals receiving benefits from the SSDI program:

- **Growing Labor Force.** During this time, the working-age population (age 20 through 64) increased by about 43 percent. As this population grew, so did the labor force, leading to more Social Security-covered workers who might at some point during their working lives become entitled to SSDI benefits.

- **Aging Population.** The risk of disability increases with age. A worker is far more likely to be disabled at age 50 than at 40 and twice as likely at age 60 than at 50. The baby boomers, who were born between 1946 and 1964, have now aged into their high-disability years, driving much of the growth in the SSDI program.

- **Women's Labor Force Participation.** The number of women entering the workforce since 1970 resulted in a significant increase in the number of women insured for SSDI benefits. In 1980, only 50 percent of women had worked enough to be eligible for SSDI if they were to become disabled. By contrast, women today have essentially caught up with men when it comes to being insured for benefits based on their participation in the labor force.

- **Women's Recipiency Rates Equal Men's.** Women have also caught up with men in terms of the rate at which they become disabled. As recently as 1990, disabled male workers outnumbered disabled female workers by 2 to 1. Today, nearly half of workers receiving SSDI are women.

- **Effect on SSDI of Increasing the Social Security Retirement Age.** Increasing the full retirement age from 65 to 67 has also played a role in increasing the cost of the SSDI program. Keeping disabled workers on SSDI for an additional one to two years before converting to retirement benefits has driven up the cost of SSDI; yet another example of a change to the program, the effect of which was well understood long ago.

As the foregoing discussion of the factors that account for the recent growth in the SSDI program indicates, the vast majority of the increase in the program was predicted many years ago, and they can by no means be characterized today as a surprising development or as an impending crisis. Heated rhetoric from policy makers will impede, not facilitate, the resolution of this issue.

**SSDI Awaits Routine Technical Correction**

Within the next two years, a routine adjustment is required to ensure that the SSDI trust fund will continue to pay 100 percent of promised benefits. As stated earlier, prior Congresses, on eleven occasions, have rebalanced the revenue between Social Security's trust funds without controversy. Congress should do so now.

The projected DI shortfall can be easily eliminated by rebalancing the flow of revenue between the DI and the Old-Age and Survivors Insurance (OASI) trust funds so that they remain on an equal footing and remain fully solvent through 2033. This adjustment can ensure Social Security's solvency for the nearly twenty years without increasing contributions or decreasing benefits.

More important, this rebalancing will provide peace of mind to the 11 million Americans who receive benefits from the DI trust fund by assuring them that they can be confident their benefits will continue uninterrupted by a predicted and preventable shortfall. Now is the time for all members of Congress to stand up and show their commitment to Social Security and the Americans who have earned benefits from this vitally important program.

**Chairman Mike Enzi's Questions for the Record**
*Responses by Professor Mark Duggan*

1. The ACA is likely to have a relatively minor effect on the SSDI trust fund. Recent research by Maestas, Mullen, and Strand (2014) has explored the change in SSDI applications in Massachusetts following that state's health reform in 2006. The authors conclude that "viewing the MA reform as a test case for the Affordable Care Act . . . our estimates point to a likely decrease in the overall SSDI and SSI caseload relative to other trends." On the other hand, the Congressional Budget Office estimates that the ACA will reduce labor market compensation by 1 to 1.5 percent and this will mechanically lower SSDI tax revenue. The available evidence is not sufficiently precise to determine which factor will outweigh the other though the magnitude of the net effect is likely 1 percent per year or less of total SSDI revenues.

2. In 2010-2011, I served with nine other individuals on a Technical Panel for the Social Security Advisory Board in which we analyzed the assumptions and methods used by the SSA's Office of the Actuary when projecting future DI enrollments. As documented by Daly, Lucking, and Schwabish (2013), the OACT has tended to underestimate the growth in SSDI enrollment over the past 25 years. Additionally, in our report to SSAB "2011 Technical Panel on Assumptions and Methods" my colleagues and I on the panel recommended that OACT increase future incidence rates, lower future mortality rates, and lower assumed recovery rates in their projections. All three factors increase projected SSDI enrollment. The panel also recommended that OACT explore further the importance of the shift in diagnoses (e.g. toward musculoskeletal conditions) in affecting future DI enrollment and expenditures.

3.The "bend points" in SSDI's 90-32-15 formula are indexed to average wage growth. Wage growth has been slower than average among less-educated workers. Because of this, a larger fraction of their current earnings would be replaced at a 90 percent rate if they qualified for SSDI. The indexation of earnings amplifies this effect because earnings in a previous year are scaled by the ratio of average current earnings to average earnings in that year. Suppose for example that wages for low-skilled individuals were unchanged at $20,000 from 1990 to 2010 but that during that period average earnings grew by 50 percent. In this example, 1990 indexed earnings would be $30,000 and this would increase the worker's average indexed monthly earnings (that is used to calculate SSDI benefits) and thus his/her potential SSDI benefit. Autor and Duggan (2003) explain this on pages 163-164.

Thank you for these questions and please feel free to contact me if I can assist in any other way.

Autor, David and Mark Duggan. 2003. "The Rise in the Disability Rolls and the Decline in Unemployment." *Quarterly Journal of Economics.*

Congressional Budget Office. 2014. "The Budget and Economic Outlook." http://www.cbo.gov/sites/default/files/45010-Outlook2014_Feb_0.pdf

Daly, Mary; Brian Lucking, and Jonathan Schwabish. 2013. "The Future of Social Security Disability Insurance." FRBSF Economic Letter June 24, 2013. http://www.frbsf.org/economic-research/publications/economic-letter/2013/june/future-social-security-disability-insurance-ssdi/

Maestas, Nicole; Kathleen Mullen, and Alexander Strand. 2014. "Disability Insurance and Health Insurance Reform: Evidence from Massachusetts." *American Economic Review, Papers and Proceedings* 104:5, 329-335.

Report to Social Security Advisory Board. 2011. "2011 Technical Panel on Assumptions and Methods." http://www.ssab.gov/Reports/2011_TPAM_Final_Report.pdf

**Senator Angus King's Questions for the Record**
*Responses by Professor Mark Duggan*

1. As I have written with various co-authors over the years, the SSDI program substantially lowers the incentive to work among people on or applying for the program. It has a similar effect among those who are considering applying for the program. In addition to intervening sooner for individuals with disabilities (see report cited in my response to next question), one could consider moving to a graduated system similar to the VA's Disability Compensation (DC) program rather than the current "all-or-nothing" SSDI system. This could include variation in monthly benefits (as the DC program has) or variation in the potential duration of benefits for an award. Moving away from the current "one-size-fits-all" SSDI program could improve economic well-being among many individuals with disabilities while simultaneously improving the financial health of the SSDI program. Recent research for Norway has also shown that increasing the incentive to work among disability insurance recipients can substantially increase program exit rates and employment rates (Kostol and Mogstad, 2014).

2. David Autor and I have a detailed proposal that explains why involving private disability insurers could substantially improve the SSDI program. Our proposal is similar in some respects to the reforms undertaken in the Netherlands that Professor de Jong and others have studied. Here is a link to the proposal:

http://www.brookings.edu/~/media/research/files/papers/2010/12/disability-insurance-autor/12_disability_insurance_autor.pdf

3. The rise in the number of SSDI recipients with a mental disorder as the primary diagnosis has outpaced the increase in the number of individuals with mental illness in recent decades. For example, a 2005 New England Journal of Medicine study found that the prevalence of mental disorders did not change from 1990 to 2003 and yet during that time the number of SSDI recipients with mental disorder as the primary condition grew rapidly. A key reason for the enrollment growth is that health care providers have become better at diagnosing mental illness and the stigma of mental illness has also fallen. While I am admittedly not an expert in the treatment of mental illness, my reading of the literature is that there have been substantial improvements in the quality of treatment that suggest many individuals who in the past may have been unable to work now potentially could. Connecting individuals with the right treatment could allow many of them to remain in the workforce while increasing their health and economic well-being.

Thank you for these questions and please feel free to contact me if I can assist in any other way.

Kessler, Ronald C. et al. 2005. "Prevalence and Treatment of Mental Disorders: 1990 to 2003." *New England Journal of Medicine*, 2515-2523.

Kostol, Andreas and Magne Mogstad. 2014. "How Financial Incentives Induce Disability Insurance Recipients to Return to Work." *American Economic Review*.

**Senator Ron Wyden's Questions for the Record**
*Responses by Professor Mark Duggan*

Recent research by Maestas et al (2013) and French and Song (2014) demonstrates that there is substantial variation across both disability examiners and administrative law judges in their propensity to make SSDI awards. The authors of both studies find that up to one-third of individuals allowed by lenient examiners (judges) but denied by strict examiners (judges) work when they are denied SSDI benefits. This likely understates the potential to work among these individuals, as the application process requires individuals to be out of the labor force and thus their earnings potential declines. Research by von Wachter et al (2011) further suggests that work potential among younger SSDI recipients and among those with more subjective conditions (e.g musculoskeletal conditions) is substantial.

I chose 1989 simply because it was shortly after the mid-1980s liberalization of the SSDI program's medical eligibility criteria. As an examination of Figure 1 of my testimony suggests, the changes in SSDI enrollment by age and gender would be almost identical if I took 1985 or 1990 as the base year.

Thank you for these questions and please feel free to contact me if I can assist in any other way.

French, Eric and Jae Song. 2014. "The Effect of Disability Insurance on Labor Supply." *American Economic Journal: Economic Policy.*

Maestas, Nicole, Kathleen Mullen, and Alexander Strand. 2013. "Does Disability Insurance Receipt Discourage Work? Using Examiner Assignment to Estimate Causal Effects of SSDI Receipt." *American Economic Review.*

Von Wachter, Till, Jae Song, and Joyce Manchester. 2011. "Trends in Employment and Earnings of Allowed and Rejected Applicants to the Social Security Disability Insurance Program." *American Economic Review.*

# JUSTICE IN AGING

FIGHTING SENIOR POVERTY THROUGH LAW

## Answer to Question for the Record Following a Hearing on Social Security Disability Trust Fund Insolvency Conducted by the Senate Committee on the Budget (February 11, 2015)

**Senator Wyden**

**Question:** One issue that did not come up during the hearing that I would like you to comment on is that the decision to apply for SSDI is often a last resort for many workers. The National Council on Disability summed this up well:

*"Receipt of Social Security disability benefits is merely the last stop on a long journey that many people with disabilities make from the point of disability to the moment at which disability is so severe that work is not possible. All along this journey, individuals encounter the policies and practices of the other systems involved in disability and employment issues."*

I think this quote makes the point that many programs offer support for workers with disabilities before they apply for SSDI and there is more we could do to improve that support. Do you agree and what improvements would NSCLC suggest?

**Answer:** While there are some reforms that could make it easier for those who receive Disability Insurance benefits to test their ability to return to work, such as simplifying the program's work rules and improving SSA's processing of earnings reports, most Disability Insurance beneficiaries live with such significant disabilities that substantial work is unlikely. We at Justice in Aging (formerly NSCLC) agree that to achieve the goal of supporting people with disabilities in having the opportunity for gainful employment and economic security, there are many improvements that could be made in the policies and practices of various programs that they encounter before they reach the point of applying for SSDI.

Three improvements that we suggest are:

- **Improve access to long-term supports and services**: Ensuring access to long-term services and supports for workers with disabilities through a national Medicaid buy-in program with generous income and asset limits would remove a major barrier for employed individuals with disabilities. No person with high support needs should be required to remain poor in order to gain access to the services and supports they need in order to work.

- **Investigate early interventions**: SSA's FY 2015 budget includes $50 million for research into early invention demonstration projects to evaluate their effectiveness.

WASHINGTON
1444 Eye Street, NW, Suite 1100
Washington, DC 20005
202-289-6976

LOS ANGELES
3660 Wilshire Boulevard, Suite 718
Los Angeles, CA 90010
213-639-0930

OAKLAND
1330 Broadway, Suite 525
Oakland, CA 94612
510-663-1055

These and other approaches should be investigated and then developed as pilot programs to provide an evidence base for what works in this area.

- **Reform asset limits**: To remove barriers to savings and ownership for people with disabilities, Congress must take action to update SSI's outdated asset limits, as the SSI Restoration Act would do. Additionally, myRA accounts, a new type of retirement savings accounts established in 2014, should be excluded from counting against asset limits in programs such as SSI and Medicaid.

Submitted by

Kate Lang
Senior Staff Attorney
Justice in Aging
1444 Eye Street NW, Suite 1100
Washington, DC 20005
(202) 683-1997
klang@justiceinaging.org

# Disability Insurance Benefit Rates, (2011)

**Highest County Rates**

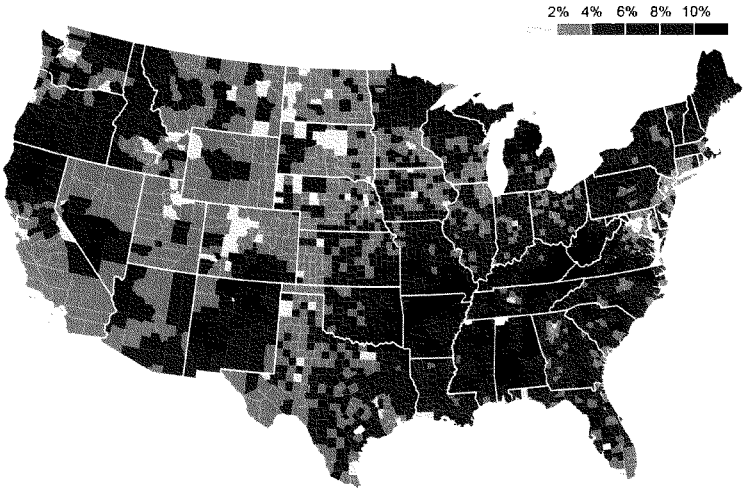
| County | Rate % |
|---|---|
| Buchanan Cnty, VA | 20.0 |
| Dickenson Cnty, VA | 18.4 |
| Floyd Cnty, KY | 17.2 |
| Pike Cnty, KY | 16.8 |
| Mingo Cnty,WV | 16.6 |
| Wyoming Cnty, WV | 15.4 |
| Johnson Cnty, KY | 15.0 |
| Lee Cnty, VA | 14.9 |
| Russell Cnty, VA | 14.8 |
| Letcher Cnty, KY | 14.5 |

**Lowest County Rates**

| County | Rate % |
|---|---|
| Pitkin Cnty, CO | 0.6 |
| Summit Cnty, CO | 0.7 |
| Eagle Cnty, CO | 0.7 |
| Arlington Cnty, VA | 1.0 |
| Fairfax Cnty, VA | 1.1 |
| Loudoun Cnty, VA | 1.1 |
| Teton Cnty, WY | 1.3 |
| Madison Cnty, ID | 1.3 |
| Alexandria (City), VA | 1.3 |
| Blaine, ID | 1.4 |

**Source: Urban Institute**

# Share of Adult Population Receiving SSDI Benefits (2011)




Source: Urban Institute

Senator Ron Wyden
221 Dirksen Senate Office Building
Washington, DC 20510
U.S.A.

The Hague, February 18, 2015

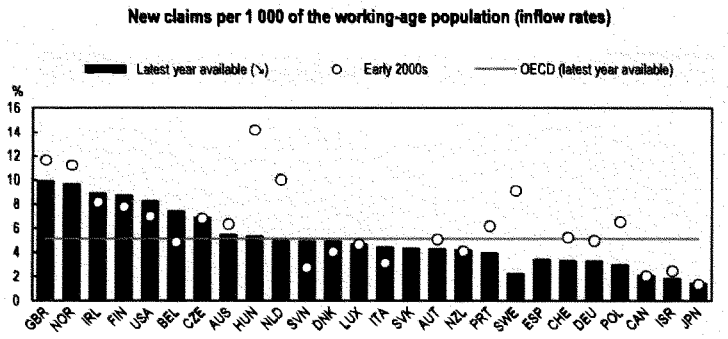
Ref: Questions on Dutch Social Welfare

Dear Senator,

In reaction to my testimony for the Senate Budget Committee on February 11, 2015, you asked two questions. Please find my answers below.

Your first question regards rates of disability awards (inflow rates) in the Netherlands versus the U.S.

According to the latest OECD data, the inflow rate in the Netherlands is **5** per 1,000 of the working-age population, whereas it is **8** per 1,000 in the U.S.




Source: OECD, Mental Health and Work: Netherlands, Paris, November 2014, p. 29.

Your second question is about other examples about how the Dutch safety net differs from that in the U.S. First, since 2006, the Dutch population is covered by a basic *health*

# THE COMING CRISIS: AMERICA'S DANGEROUS DEBT

**WEDNESDAY, FEBRUARY 25, 2015**

UNITED STATES SENATE,
COMMITTEE ON THE BUDGET,
*Washington, D.C.*

The Committee met, pursuant to notice, at 10:30 a.m., in Room SH–216, Hart Senate Office Building, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Grassley, Sessions, Crapo, Johnson, Ayotte, Wicker, Perdue, Sanders, Wyden, Stabenow, Whitehouse, Warner, Kaine, and King.

Staff Present: Eric Ueland, Republican Staff Director; and Warren Gunnels, Minority Staff Director.

## OPENING STATEMENT OF CHAIRMAN ENZI

Chairman ENZI. I will call this hearing to order. Good morning, colleagues, and welcome to this hearing.

We gather together facing the biggest debt our country has ever owed. That debt endangers our Government, hurts our economic potential, and threatens our children and grandchildren. Moreover, if you like your country to be able to stand up to enemies like ISIL, help its seniors with programs like Social Security, and help us all get from here to there with a good transportation infrastructure, then you will not like where America is headed.

Our increasing national debt threatens these functions of Government and much more. If we do not stand up to our debt and stop overspending, we will ruin what so many generations before us worked to build and the hopes of the generations to come. Unfortunately, our President's budget plan just makes matters worse. I will refer you to the chart.

How large is the dangerous debt that we face? The President's chronic overspending will make debt boom. As you can see on the screen, with the debt already at over 18,000 billions owed, the President's runaway overspending plan in his budget will push the debt to 26,000 billion owed. I like to call it "26,000 billion" instead of $2.6 trillion, because that sounds like a smaller number. We get to work in billions. We are finally understanding what billions are, so 26,000 billions owed in just 10 years.

They are incredibly large numbers, and that is why I do break them down by the amount every man, woman, and child will owe on it over the next 10 years. As you can see on the screen, under the President's plan, the amount every American will owe on the debt over the next 10 years will march steadily upward. At the end

of last year, each American's share of the debt stood at $55,683. In just 10 years, it will be $75,610—$20,000 more.

These are big numbers, and they are bad enough. But the staggering amount of what we owe is not the only thing that the numbers show. Take a look at the screen again. The debt threatens to overwhelm the size of our economy as well. According to CBO, just 15 years ago, the debt held by the public was one-third the size of our economy. Today the accelerating debt is 74 percent of our economy. In 2028, it will be the same size as our economy, and in just two short generations, by 2050, our debt will be more than twice the size of our economy.

Colleagues, dive a little deeper into the debt forecast. If you look again at the video screens, you will see a comparison of the CBO forecast for the economy, the blue bars, between now and 2050, and the publicly held debt, the red bars. CBO expects debt to rise three times faster than the economy over the next 35 years.

After 2050, CBO will not make public what could happen. They simply report that the debt will be greater than 250 percent of the GDP. You know you are in a lot of trouble when your own accountant refuses to tell you exactly how bad your financial condition is because they cannot calculate a number that big.

These millions of retirees are a significant element of CBO's high debt forecast, but there is another factor as well. CBO assumes that Congress and the President will not tackle our overspending, and CBO is probably right.

However, entitlements are not the only reason that the debt of the United States is growing so fast and so large. There are two other features with long-term consequences for the pace of the Federal debt growth.

First, President Obama's policies have created the slowest economic recovery since World War II. More debt is on our books with a weak and anemic economy. Let me explain.

If you will look again at the video monitors, this chart shows how slowly labor markets recovered from the Great Recession. It took over 6 years, until the spring of 2014, for total employment to get back to its level when the recession started in December of 2007. That is the blue line.

Compare that to the equally severe recession of 1981. The unemployment rate was worse in that recession, but total employment recovered in 27 months as opposed to 76 months, or a little over 2 years.

One of the reasons for so many suffering for so long was our debt. Economists who studied the interaction of debt and economic growth point out that the large debt leads to slow economic growth. Recent studies from the World Bank, the International Monetary Fund, from Ken Rogoff and Carmen Reinhart, the International Bank of Settlement, and the European Central Bank all connect high and growing debt to slower growth. For the average American, this means that an exploding debt could result in fewer job opportunities, longer unemployment, and a more uncertain future.

Second, this slow growth has delayed the launch of the millennial generation, which worsens our ability to slow the growth of future debt. For the estimated 65 million young people between the ages of 16 and 29 in 2012, economically slow times have been very

bad news. This large group of Americans is crucial for our economic and fiscal future, and they suffered extensively during the recovery. Unemployment among the 16-to-19 age group averaged 22 percent. Among the older 20-to-24 age group, it averaged 13.6 percent. Lack of job opportunities has forced millions to delay beginning their lives, earning and saving.

Professor Lawrence Katz of Harvard University recently estimated that one of five males have been idle since the recovery started. They are not working. Idleness among young women is almost as high. Lack of job opportunities caused incomes to stall and fall to levels last seen in the late 1970s among all working households and especially the young. Instead of launching the next generation of workers and entrepreneurs after the crisis of 2008 and 2009, we launched the debt-paying generation.

Let me say that again. We launched the debt-paying generation. I see several out in the audience who are in the debt-paying generation.

Rapidly growing debt will press down on their dreams and opportunities throughout their life. In the meantime, the steady march to a larger debt will continue. When it comes to the dangerous debt, our President can and should do and will have to do better.

Senator Sanders?

**OPENING STATEMENT OF SENATOR SANDERS**

Senator SANDERS. Mr. Chairman, thank you very much for holding this important hearing, and I thank our guests and panelists for being with us today.

I think when we talk about debt and deficit, it is also important to understand how we got to where we are today. And it might be useful to remember that when President Clinton left office in 2001, the Federal Government enjoyed a healthy surplus of $236 billion, and the national debt was on track to be eliminated by the year 2009. Economists were telling us we were looking at surpluses into the foreseeable future.

What happened? Well, let me give you some examples of what happened. Some of my so-called deficit hawk friends went to war in Afghanistan and Iraq, and they forgot to pay for those wars. We do not know exactly what those wars will cost, but the guess is they may end up costing something like $6 trillion by the time we take care of the last wounded veteran.

So I find it a little bit strange that some of my deficit hawk friends who want to cut Social Security or Medicare or Medicaid forgot to pay for two wars.

Under President Bush, my Republican colleagues passed huge tax breaks for millionaires and billionaires and some of the most profitable corporations in this country. But they forgot to offset or pay for those tax breaks.

Under President Bush, my Republican colleagues passed an overly expensive Medicare prescription drug program written by the insurance and drug companies, which, among other things, does not allow Medicare to negotiate drug prices with the pharmaceutical industry.

And, finally, Mr. Chairman, what I would say in that regard is that for all of those people who believe in the virtues of deregula-

tion, well, in a bipartisan manner—not just Republicans—that happened, and we deregulated Wall Street. And as a result of the illegal and reckless behavior on Wall Street, we were plunged into the worst recession in the modern history of this country, which obviously had a huge impact on our deficit and our national debt.

Now, having said that, there is some good news, and that is that when President Obama came into office, he inherited a record-breaking $1.4 trillion Federal deficit and a growing national debt, and the good news is that, in fact, the Federal deficit has been reduced by more than two-thirds while more than 11 million private sector jobs have been created over the past 58 months. So some progress is being made.

Point number two that I want to make: When we look at the budget, it is important that we look not only at our national debt, but that we take a serious look at what is happening in the economy and how the American people are doing. Today millions of Americans are working longer hours for low wages. We have the highest rate of childhood poverty of any major country on Earth. And we have more income and wealth inequality than we have had in this country since 1929.

It seems to me, Mr. Chairman—and I respectfully request that we could do a hearing on this issue—that we take a look at the grotesque level of income and wealth inequality, because this is not just a moral issue. It, in fact, becomes an economic issue, which touches on the issues that you and I and our Committee are discussing today.

Today the top one-tenth of 1 percent of Americans own nearly as much wealth as the bottom 90 percent, and the top 1 percent earn more income than the bottom 50 percent. This has not only hurt our economy, but it has increased our debt and harmed the solvency of Social Security.

The fact of the matter is that over the last 40 years, under Democratic and Republican leadership, we have witnessed an enormous transfer of wealth from the middle class and the poor to multimillionaires and billionaires. This is the Robin Hood principle in reverse. We take from the poor and we give to the very, very rich.

In 1985, the share of the Nation's wealth going to the bottom 90 percent was 36 percent. In 2013, it went down to below 23 percent. If the bottom 90 percent had simply maintained the same share of our Nation's wealth as they did 30 years ago, they would have $10.7 trillion more in wealth than is currently the case today, which would have profound implications on debt and deficit, not to mention the well-being of the middle class.

Meanwhile, the share of the Nation's wealth going to the top one-tenth of 1 percent has gone up from 10 percent in 1985 to 22 percent in 2013, which means they have accumulated, the top one-tenth of 1 percent, $8 trillion more. So what you are seeing is a collapse in wealth in the middle class and almost all of that going to the top one-tenth of 1 percent.

Mr. Chairman, if that massive transfer of wealth and income did not take place, Social Security would be in much better financial shape, the middle class would be more secure, and our national debt—the issue of today's discussion—would be much lower. And I

really do hope that we could have a hearing to discuss the implications of this huge transfer of wealth from the middle class to the top one-tenth of 1 percent.

The third point I want to make, Mr. Chairman, is that while we are here talking about the national debt, I have the feeling that in a couple of weeks, when we begin to talk about the deficit—now, I may be wrong on this, so I am speculating, and maybe you will suggest that I am wrong here. But I have a feeling that the budget that your Committee majority will bring forth in order to deal with the debt is to say to the American people, "Yeah, we forgot to pay for the war in Iraq; therefore, we are going to cut Medicaid, we are going to cut education, we are going to cut food stamps, we are going to cut nutrition programs. And, by the way, we are going to give more tax breaks to the very, very rich and to the large multinational corporations."

I may be wrong. I have not seen your budget yet. My guess is that it will emulate what the Ryan budget was, and it will not be good for working families.

The last point that I want to make is that if we are serious about deficit reduction, then we have to take a look at such facts as the reality that from 2008 to 2013, not only did a company like General Electric pay nothing in Federal income taxes, it received a huge tax break from the IRS of nearly $3 billion. If we are serious about dealing with the deficit, you know what we are going to have to do? We are going to have to look at revenue. We are going to have to ask why the wealthiest, some of the largest and most profitable corporations in this country pay nothing in Federal income tax, while the effective tax rate for hedge fund millionaires is in some cases lower than it is for truck drivers or nurses.

So, Mr. Chairman, there is a lot to discuss, and I look forward to this hearing.

Chairman ENZI. Thank you, Senator Sanders. And one thing I am trying to change, we talk about deficit and we talk about debt, and people are kind of confusing the two. So I am trying to change deficit to our amount of overspending, because that is our annual amount of overspending—

Senator SANDERS. Well, or it could be—

Chairman ENZI. —that adds to the debt.

Senator SANDERS. Well, that is one way of looking at it.

Chairman ENZI. It has been reduced by two-thirds, but our debt has not been reduced by two-thirds, and some people are confusing that. And I would like to keep from getting that confusion.

Senator SANDERS. Well, the answer is spending is one cause of deficit, but not raising revenue is another cause of deficit.

Chairman ENZI. Okay. Now we will turn to the witnesses. The capacity of this Government to accumulate more debt ultimately is limited by financial and moral factors. If those individuals and organizations that buy our debt begin to wonder if we can effectively manage our financial affairs and solve problems that threaten our financial help, then we will need to pay people for the greater risk to hold our debt. As a result, interest rates could rise even further than currently forecasted, thus worsening even more our financial condition.

The other factor is moral. How long can this Government continue to pass ever higher debts to the next two generations? With higher and higher debt comes the possibility of higher Federal taxes and lower Federal benefits for Americans who today are under 30, many of whom are not old enough to vote. How long can Congress authorize the enormous deficits and, thus, greater levels of debt without a financial plan to reduce and eliminate overspending and stop the growth of debt?

I cannot help but believe that elected officials ultimately will pay a heavy political price for their indifference to the next two generations. So today's witnesses will speak to us about these and other dimensions of the fiscal future. Let me introduce at this time.

Our first witness is Dr. Larry Kotlikoff. Dr. Kotlikoff is widely viewed as the leading expert on the economic effects of debt and its intergenerational costs. He is the William Fairfield Warren Professor at Boston University, a professor of economics at Boston University; a fellow of the American Academy of Arts and Sciences; a fellow of the Econometric Society, a research associate of the National Bureau of Economic Research; president of Economic Security Planning, Incorporated, a company specializing in financial planning software; and the director of the Tax Analysis Center. On this subject he is best known for his best-selling book, "The Coming Generational Storm: What You Need to Know about America's Economic Future," written in 2005.

Our next witness is Heather Pfitzenmaier, the director of the Young Leaders Program at the Heritage Foundation. She works closely with the millennial generation on a broad range of public policies. In December of 2012, Forbes Magazine named her one of the 30 Under 30 young Americans who are making the greatest impact on law and policy. She serves on several boards of organizations focused on young Americans and is a graduate of the University of Michigan.

Our final witness is Bruce Bartlett. Mr. Bartlett has served in several capacities in Government, perhaps most notably as the Deputy Assistant Secretary for Economic Policy in the Treasury Department during the administration of George H.W. Bush.

I welcome all of the witnesses, and we will begin with you, Dr. Kotlikoff.

You will have to push the button to get the microphone to work.

Mr. KOTLIKOFF. Sorry. Let us see.

Chairman ENZI. Thank you.

Mr. KOTLIKOFF. Still not working? Is that better?

Chairman ENZI. Yes. It has to be pointed at you.

Mr. KOTLIKOFF. Okay. Sorry.

Chairman ENZI. Thanks.

## STATEMENT OF LAURENCE J. KOTLIKOFF, PROFESSOR OF ECONOMICS, BOSTON UNIVERSITY

Mr. KOTLIKOFF. Senator Enzi and Senator Sanders and other distinguished members of the Senate Budget Committee, it is an honor to speak to you about the Nation's fiscal position.

The last time I had a conversation with Senators, I was testifying at the request of Senator Bradley back in 1990 to the Senate Finance Committee, and we were focused on the same questions we

are focused on today. Unfortunately, the situation has gotten much worse, fiscally speaking.

I mention that in part to reference what has changed through time, but also to mention that I was invited at that point by a Democrat; today I was invited by a Republican. I am not political. I am coming as an economist. I think economics has something to say that is independent of politics, and the best economists are neither Republicans nor Democrats. They are just focused on what economic science tells us, and that is what I am here to try and relate to you today.

The first point I want to get across is that our Nation is broke. Our Nation is broke, and it is not broke in 50 years or 75 years or 30 years, 10 years or 5 years. It is broke today. Just like Detroit is broke today in terms of looking at all the obligations it has to pay and all the revenues it has to collect, that it projects to collect, it is an entity that is broke, and it is not broke in the future. It is really broke today.

And that is the case for the U.S., and that analysis is not based on looking at what Congress declares to be its official liabilities but, rather, by looking at all the liabilities that the U.S. Government faces, and those include not just official servicing of what is called the "official debt," but also paying for Social Security, Medicare, Medicaid, defense spending, paying for the President's lunch, for the Supreme Court members' salaries, for fixing up the highways. But those are the obligations into the future that are projected by the CBO, and that is also assets which are the present value of all the taxes that are being projected.

And economics tells us that we need to focus on not a subset of the obligations that have to be paid, not the payment for principal and interest on what is called "official debt," but we have to look at all the obligations, regardless of what it is called, because Congress has enormous leeway, indeed infinite leeway in terms of classifying certain payments that it has to make as repayment of principal plus interest versus repayment of—versus transfer payments. And that leeway means that the official debt is really not a well-defined economic concept, and that is the thrust of my testimony today, that we are kind of tracking our fiscal position based on a non-measure of fiscal solvency.

And what economics says and what economists as a group are saying is that we need to study and look at the fiscal gap, the infinite horizon fiscal gap, which is the present value, the value in the present, of all the expenditure commitments, no matter what they are called, whether they are called Social Security or defense spending or paying—servicing what is called the official debt, less the present value of all the projected tax receipts.

Now, that fiscal gap calculation has been endorsed by over 1,200 economists. If you go to theinformact.org, there is a bill, a bipartisan bill, that was introduced last year. I hope it will be passed this year. It is a bill to require the CBO, the GAO, and the OMB to do fiscal gap accounting on a routine basis and to put everything on the books, to stop this Enron-type accounting that has been going on for decades under both parties.

The fiscal gap which is being recommended as the basis for our budgetary analysis, it is not just being endorsed by 1,200 econo-

mists from every top department in the country, people that are on both sides of the political aisle—you have got Jeff Sachs, who is viewed as left of center; you have got Glenn Hubbard, who is viewed as right of center; you have got former Secretary of State and Secretary of Treasury and the head of the Commerce Department and the Director of OMB. I am talking about George Shultz. He is also endorsing this bill. There are also 17 Nobel Prize winners in economics. The majority of these folks are Democrats, as far as I can tell, starting with Ken Arrow,, who is probably the leading economist after Paul Samuelson of the post-war period. All of these folks have endorsed the fiscal gap analysis.

We have a $210 trillion fiscal gap at this point, so we are not talking about $13 trillion of obligations in the hands of the public. That is the official debt. But we are talking about a $210 trillion fiscal gap, and as my testimony indicates, the longer we wait to start dealing with and paying off this fiscal gap, the bigger the problem will be. We have to immediately and permanent raise taxes, all Federal taxes, by 58 percent to come up with $210 trillion in present value. So we are 58 percent underfinanced. In contrast or comparison, Detroit was about 25 percent underfinanced at the time it declared bankruptcy. So the country is in far worse shape than Detroit, fiscally speaking.

The other alternative to raising taxes is to cut spending, and if you cut all the spending, apart from servicing the official debt, you would have to have an immediate and permanent 38-percent cut in every expenditure. Defense spending, gassing up Air Force One, transfer payments of all kinds—all would have to be cut 38 percent.

Now, this calculation of this enormous fiscal hole is coming right out of the CBO's July—I think it was around July 30th—projection of long-term expenditures and taxes called their "Alternative Fiscal Scenario."

Now, what economic science tells us is that if governments take from young people and give to old people and then promise young people future transfer payments, what is going to happen is that the old people will consume more, the young people will not consume anything less; they might actually consumer more themselves. The Nation as a whole will consume less, and we will have less national saving, and we will likely have less national investment.

Now, I refer you to the charts in the testimony which show that there has been an enormous increase in consumption as a share of national income, so that in 1950, we had a national saving rate of 15 percent. Today we have a national saving rate of around 4 percent. It has just gone straight downhill. With some gyrations, over time our national saving rate has gone down. If you simulate the policy we have been running under both parties in the post-war, one administration after the next taking from the young, giving to the old, we have what you find occurring in reality, and the computer models show a decline in national saving and investment. And sure enough, that is what we see in the data, and you see this in Chart 2.

Chairman ENZI. I will have to ask you to kind of summarize at this point.

Mr. KOTLIKOFF. I will just finish up. And you also see in Chart 3 an enormous increase in the absolute and relative consumption of the elderly.

So we have a huge hole. We have, in effect, been engaging in a war against our children. So I agree, Senator Sanders, that we have a big problem of inequality within a generation between the rich of a given age and the poor of a given age. And I am very concerned about that, too. It is not that that is not a big concern of mine and other economists. But we also have a big concern about how we are treating poor kids in the future versus poor kids today and rich kids in the future versus rich kids today. There is an enormous generational redistribution going on. I do think we have to address this. We have to pass the INFORM Act, and we have to do that immediately and be honest with our children about what kind of fiscal burdens we are leaving them.

Thank you.

[The prepared statement of Mr. Kotlikoff follows:]

# America's Fiscal Insolvency and Its Generational Consequences

**Testimony to the Senate Budget Committee**

**February 25, 2015**

**Laurence J. Kotlikoff**

Professor of Economics, Boston University

**Chairman Enzi and Other Distinguished Members of the Senate Budget Committee,**

I am honored to discuss with you our country's fiscal condition. Let me get right to the point. Our country is broke. It's not broke in 75 years or 50 years or 25 years or 10 years. It's broke today. Indeed, it may well be in worse fiscal shape than any developed country, including Greece.

This declaration of national insolvency will, no doubt, shock those of you who use the officially reported federal debt as the measuring stick for what our country owes. After all, federal debt in the hands of the public is only 74 percent of the GDP. Yes, this is double the debt-to-GDP ratio recorded a decade ago. But it's still a far cry from Italy's 135 debt-to-GDP ratio or Greece's 175 percent ratio.

Unfortunately, the federal debt is not an economic measure of anything, including our nation's fiscal position. Instead, the federal debt and its annual change, the deficit, are purely linguistic constructs that reflect how you members of Congress choose to label government receipts and payments.

To see this point, consider the almost $750 billion the government is collecting this year from workers under the heading Social Security payroll taxes and the future Social Security transfer payments these FICA contributions secure. The $750 billion could just as well be called government borrowing and the future transfer payments could just as well be called principal plus interest on this borrowing plus a future tax (positive or negative) if the future payments don't correspond precisely to principal plus interest.

This simple change in language would more than double this year's reported federal deficit. Indeed, were we to go back in time and re-label all past Social Security taxes as borrowing, official federal debt held by the public would not be $13 trillion, but $38 trillion, which is 211 percent of U.S. GDP.

**Driving in NY With a Map of LA**

Economic theory doesn't tell us what language to use to discuss its equations. Whether we use English, French, or Chinese, the real economic outcomes predicted by the math are the same. Fiscal labeling conventions are simply a choice of language. And federal debt is a word game, not a well-defined measure of fiscal policy. Its use in understanding fiscal sustainability and generational policy is no different from driving in Los Angeles with a map of New York.

Economics is not the only field where language can mask reality. In physics, time and distance were once viewed as fundamental concepts. Today they are understood for what they are – reflections of our physical frame of reference, which is itself a language. And just as there are an infinite number of alternative measures of time and distance, there are an infinite number

of alternative measures of the federal debt. Choose the right words and you can make the federal debt any number, positive or negative, you want.

Moreover, the fact that Congress has chosen particular fiscal labels over time does not make those labels economically more valid than any other set of internally consistent labels. Each of us is free to come up with his own labeling convention and produce his own utterly useless measure of government debt.

**My Mother's Treasury Checks**

One way to clearly see the vacuity of standard fiscal accounting is to consider the two sets of checks my 95-year old mother receives from the U.S. Treasury. The checks look physically identically. They are both the same size, color, and have the same words in the same font. The only way they differ is in their amount. This is how I know that one set of checks is for Social Security benefit payments and the other is for coupon payments on Treasury bonds.

Despite the identical nature of their appearance, only the present value of the Treasury bond payments is included as part of government debt. The present value of the Social Security payments my mom receives each month is not.

Why is that?

Yes, the Treasury bonds bear "the full faith and credit of the U.S. government." But those fancy, legal words don't make those bonds safe in any real economic sense. Our government has periodically defaulted on the real value of official debt by running inflation. In 1946, for example, it wiped out a quarter of the real value of War Bonds by lifting price controls. In the 1970s, our government used inflation to wipe out hundreds of billions of dollars in the real value of federal debt.

So my mom's payments that Congress is currently calling debt payments are hardly safe. In contrast, her Social Security benefits, which are inflation-indexed and backed by the lobbying power of 50 million members of the AARP, are secure against both inflation and changes in legislation. Yet, Congress includes not a penny of these liabilities in its tally of what the federal government owes.

What economics tells us is that we can't choose what to put on the books. All government obligations and all government receipts, no matter what they are called, need to be properly valued in the present taking into account their likelihood of payment by and to the government.

**Cooking the Books**

Congress's economically arbitrary decisions as to what to put on and what to keep off the books have not been innocent. Successive Congresses, whether dominated by Republicans or

Democrats, have spent the postwar accumulating massive net fiscal obligations virtually all of which have been kept off the books.

Net fiscal obligations refers not just to formal and informal commitments to high future transfer payments, but also formal and informal commitments to low future levels of taxation.

Spending six decades raising or extending transfer payments and cutting or limiting taxes helped members of Congress get reelected. But it has placed our children and grandchildren under a fiscal Sword of Damocles that gravely endangers their economic futures.

**The Fiscal Gap**

Economic theory is unequivocal in telling us what not to measure when it comes to fiscal sustainability and generational policy. It's also crystal clear in telling us what to measure, namely *the infinite-horizon fiscal gap*. The infinite-horizon fiscal gap tells us whether the government has, over time, enough receipts to cover its projected spending. It equals the present value of all projected future expenditures less the present value of all projected future receipts.

The infinite-horizon fiscal gap has five important properties.

First, it puts everything on the books. All expenditures, regardless of whether they are called debt service, transfer payments, or discretionary spending are included in forming the present value of future outlays. It also puts all receipts on the books, including income the government receives on its real and financial assets.

Second, the infinite-horizon fiscal gap takes on the same value regardless of what internally consistent labeling convention is used to characterize fiscal outlays and receipts. In contrast, any finite-horizon fiscal gap, such as the 75-year fiscal gaps calculated for the Social Security and Medicare programs, are, like the federal debt, creatures of nomenclature. I.e., they can be set to any value one wants simply by choosing the right fiscal labels.

Third, a positive fiscal gap means the government is attempting to spend, over time, more than it can afford. Doing so violates what economists call the government's *intertemporal budget constraint*. Hence, a positive fiscal gap is a direct measure of the unsustainability of current fiscal policy.

Fourth, eliminating the infinite-horizon fiscal gap is a zero-sum game across generations. Hence, the fiscal gap tells us the fiscal burden that will be imposed on today's and tomorrow's children if current adults don't pay more to or receive less from the government. Understanding the fiscal burdens our kids could face from the fiscal gap is called *generational accounting*.

Fifth, the machinery of fiscal gap accounting tells us the size of the adjustment needed to balance the government's intertemporal budget constraint and how the magnitude of the requisite adjustments depend on when the adjustment begins.

**The U.S. Fiscal Gap**

The U.S. fiscal gap currently stands at $210 trillion. This figure is my own calculation based on the Congressional Budget Office's July 2014 75-year Alternative Fiscal Scenario (AFS) projection.

Constructing the infinite-horizon fiscal gap from the CBO's AFS projection takes less than five minutes. One simply needs to extend CBO's projection into the future and engage, via Excel, in some high-school algebra to form the appropriate present values of expenditures and revenues. Yet the CBO refuses to make the infinite horizon fiscal gap calculation and continues to focus attention almost exclusively on official debt. In so doing, the CBO is, in my opinion, deliberately misleading the public and Congress about our nation's true fiscal condition.

The size of the U.S. fiscal gap -- $210 trillion -- is massive. It's 16 times larger than official U.S. debt, which indicates precisely how useless official debt is for understanding our nation's true fiscal position.

U.S. GDP currently stands at $18 trillion. Hence, the fiscal gap represents almost 12 years of GDP. The fiscal gap can also be compared with the present value of the CBO's projection of GDP extended through the infinite horizon. Doing so indicates that the fiscal gap is 10.5 percent of GDP. This means we need to either reduce the time path of government expenditures by 10.5 percent of GDP or raise the time path of government revenues by 10.5 percent of GDP. Alternatively, we can enact a combination of spending cuts and tax increases that amount to 10.5 percent of annual GDP. This adjustment needs to begin immediately and continue forever. Waiting to adjust will leave current adult generations either fully or partially off the hook and make the fiscal burden on young and future generations that much larger.

**What's Needed to Close the Fiscal Gap?**

Our $210 trillion fiscal gap represents 58 percent of the present value of projected future taxes. Hence, eliminating the fiscal gap via tax hikes requires an immediate and permanent 58 percent hike in federal taxes. Stated differently, the overall federal government is 58 percent underfinanced.

By way of comparison, the Social Security system, taken by itself, is 33 percent underfinanced. (I.e., its infinite-horizon fiscal gap, reported in table VIF1 of the 2014 Trustees Report, is 33 percent of the present value of projected Social Security taxes.) Another comparison is Detroit prior to declaring bankruptcy. The city appears to have been roughly 25 percent underfunded. Hence, the U.S. is in far worse fiscal shape than was Detroit before it went broke.

Another option is to cut spending on all expenditures, apart from servicing official debt, to close the fiscal gap. Doing so requires an immediate and permanent 38 percent spending cut.

**The Price of Delay**

Table 1 below shows the requisite tax hike or spending cuts needed to eliminate the fiscal gap if such adjustments are postponed into the future. Waiting, for example, for a decade to permanently raise revenues requires a 64.4 percent tax hike starting at that date. Alternatively, spending would need to be cut not by 37.7 percent, but by 40.4 percent starting in 2025. Obviously, the longer we wait to adjust, the worse the impact on our children and grandchildren. If, for example, we wait until 2035 before adjusting via tax hikes, we'll sentence today's newborns to lifetime tax payments that are 70.4 percent larger than would arise under current law.

**Table 1**
**Percentage Revenue Increase or Cut in Spending (apart from debt service) Needed to Eliminate U.S. Fiscal Gap for Different Adjustment Starting Year**

| Start year | Revenue Increase | Cut in Spending |
|---|---|---|
| 2015 | 58.5 | 37.7 |
| 2025 | 64.4 | 40.4 |
| 2035 | 70.4 | 43.2 |
| 2045 | 77.0 | 46.5 |

Source: calculations by Laurence Kotlikoff based on CBO's 2014 Alternative Fiscal Scenario

**Our Nation's True Deficit**

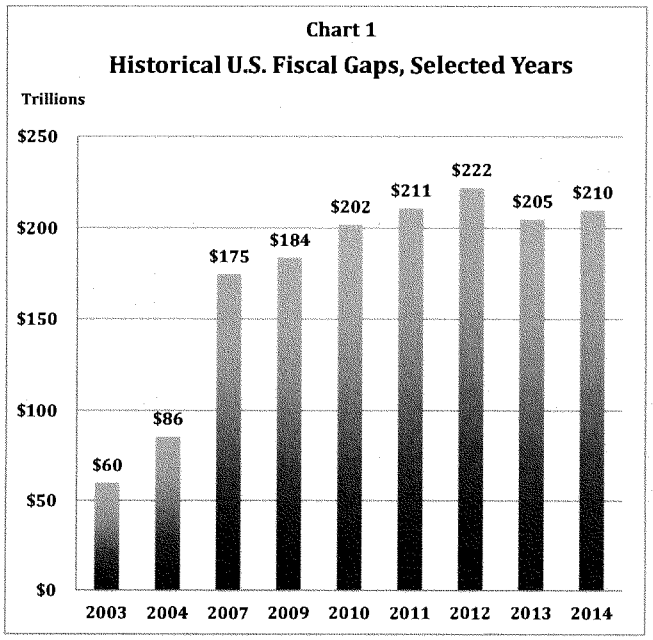
In 2013 the fiscal gap stood at $205 trillion. In 2014 it was $210 trillion. Hence the country's true 2014 deficit – the increase in its fiscal gap – was $5 trillion, not the $483 billion increase in official debt reported by the CBO.

Why did the fiscal gap rise so dramatically? A major reason is that the baby boom generation got one year closer to collecting what will ultimately be about $40,000 in Social Security, Medicare, and Medicaid benefits per person per year. Hence, the present value of these obligations rose due simply to interest. Stated differently, the fiscal gap is, in effect, our

nation's credit card bill and like our own credit card balances, the fiscal gap accrues interest. If we fail to pay interest on the fiscal gap it will get larger.

**The Growth in the U.S. Fiscal Gap**

As indicated in the chart below, the fiscal gap has risen dramatically over the past dozen years. This reflects interest accrual. But the major reasons for the growth in the fiscal gap from $60 trillion in 2003 to $210 trillion today are tax cuts, increases in Medicaid and Medicare benefit levels, additional defense spending, and the introduction of Medicare Part D. The U.S. fiscal gap was reduced, from $222 trillion to $205 trillion, in 2013 due to tax and spending legislation.




Source: Calculations by Laurence Kotlikoff based on CBO Alternative Fiscal Scenario Projections.

**Fiscal Gaps in Other Developed Countries**

Table 2 compares the 2012 fiscal gaps in the U.S. with those in major European countries. The fiscal gaps for the EU countries were calculated by the European Commission. As is immediately clear, among the countries listed the U.S. is in the worst fiscal shape by a considerable margin. It's also clear that there is little correspondence between official debt to GDP ratios and fiscal gaps measured as a ratio of the present value of future GDP. In 2012 both the U.S. and the Netherlands had debt-to-GDP ratios of roughly 70 percent. Yet the U.S. fiscal gap, scaled by the present value of GDP, was over twice that of the Netherlands. Or consider Italy with its 127 percent 2012 debt to GDP ratio. Its 2012 fiscal gap is negative 2.3 percent of the present value of future GDP.

What explains Italy's negative fiscal gap? The answer is tight projected control of government-paid health expenditures plus two major pension reforms that have reduced future pension benefits by close to 40 percent.

Table 2

2012 Fiscal Gaps In Major Developed Countries

| Country | Fiscal Gap as a Share of the Present Value of GDP |
|---|---|
| U.S. | 13.7 |
| Germany | 1.4 |
| UK | 5.4 |
| Netherlands | 5.9 |
| France | 1.6 |
| Spain | 4.8 |
| Italy | -2.3 |
| Sweden | 1.7 |

Source: Laurence Kotlikoff calculation for the U.S. and European Commission (http://ec.europa.eu/economy_finance/publications/european_economy/2012/pdf/ee-2012-8_en.pdf)

**Infinite-Horizon Fiscal Gap Accounting Has Almost Universal Support Among Economists**

Claiming, as I am, that the United State is broke, that official government debt is economically meaningless, that the use of federal debt by Congress and the Congressional Budget Office and other parts of the government to guide fiscal policy is deeply misguided, and that fiscal gap accounting over the infinite horizon is the only meaningfully way to assess a country's fiscal condition could readily be dismissed as the strong views of an extreme economist.

Unfortunately, that's not the case. At www.theinformact.org, over 1200 of our nation's economists have endorsed The Inform Act – a bipartisan bill that requires the Congressional Budget Office, the Office of Management and Budget, and the General Accountability Office to do both fiscal gap and generational accounting on an ongoing basis. The list of economists includes a Who's Who of the profession. Each of the top 25 economics departments is well represented on the list. What's more, 17 Nobel Laureates in Economics have endorsed The Inform Act. In addition to economist, the site records endorsements from former top government officials like former Secretary of Treasury, former Secretary of State, former Director of the Office of Management and Budget, and former Secretary of Commerce, George Shultz. The other remarkable aspect of this list is its inclusion of economists from both ends of the political spectrum.

The fact that essentially the entire economics profession is publicly and very strongly endorsing fiscal gap accounting should not be taken lightly as, unfortunately, has been the case to date by the CBO, OMB, and GAO. These agencies shouldn't need an act of Congress to start forming meaningful measures of our country's fiscal position and the dangers it holds for our children.

**Economic Fall Out From Postwar Generational Policy**

U.S. postwar generational policy is accurately characterized as "Take As You Go." Over the decades Republican and Democratic Congresses and Administrations have taken ever-larger amounts of resources from young workers and transferred them to old retirees. The resources taken from the young to give to the old were called, in the main, "taxes." And the young were effectively told, "Don't worry. We are calling these resources taxes, but when you are old, you will receive massive transfer payments that more than make up for what you are paying now."

The impact of this policy was predictable. Older generations consumed more, younger generations had no or little reason to consume less, and the national saving rate fell. Chart 2 below documents the post 1950 decline in our national saving rate, virtually all of which can be traced to increases in private consumption. And as chart 3 shows, those within the household sector who consumed the most were older generations. The chart, provided by Professor Ronald Lee of the University of California at Berkeley shows a dramatic increase over time in the absolute and relative consumption of the elderly.

Countries that save less invest less. And chart 2 shows not just a remarkable postwar decline in the U.S. net national saving rate. It also shows a remarkable postwar decline in our nation's net domestic investment rate. Given that investment is one of the key factors underlying real wage growth, it's not surprising that average real wages of U.S. workers have grown so little in recent decades. There are obviously other factors involved – relatively poor primary and secondary education, competition with foreign workers, and competition with smart machines/robots. But having a net domestic investment rate of 4 percent rather than 15 percent is a prescription for limited real wage growth.

**Conclusion -- The Emperor's New Clothes**

Make no mistake, the standard measure of fiscal excess and generational policy – the government's debt – is, economically speaking, content-free. Thus we find ourselves, quite frankly, in Hans Christian Anderson's story of the Emperor's New Clothes with his chief tailors comprising the CBO, OMB, GAO, the IMF, the World Bank, and the OECD.

In Anderson's story, convincing the King that he was, in fact, naked proved an impossible task. Indeed, at the end of the story when a young child shouts that the King, who is leading a parade to celebrate his new clothes, is naked, the crowd stops cheering and starts murmuring. But then, as the King ignores the child and continues his promenade, the crowd starts cheering once again.

Distinguished members of the Senate Budget Committee, you are, by analogy, the crowd in this story. You can continue to steer America's fiscal policy using a metric – the federal debt – that the economics profession, whether on the left, right, or in the center, is saying, loud and clear, is a number in search of a concept. Or you can organize passage of The Inform Act and also take the painful steps needed to eliminate our nation's massive fiscal gap.

At www.thepurpleplans.org, I've laid out a series of very simple fiscal and other reforms that can close our country's fiscal gap. This reform proposals have been endorsed by economists with, again, widely varying political beliefs. They are called purple plans because they are designed to appeal to red Republicans and blue Democrats.

As these plans make clear, we don't need to abandon any generation, we don't need to eliminate social insurance, and we don't need to discard the poor to turn things around. What we do need is to understand the fiscal hole we've placed ourselves and our children and start digging ourselves out in a sensible, efficient, and humane manner.

Chart 2

**U.S. Net National Saving and Net Domestic Investment Rates, 1950-2013**

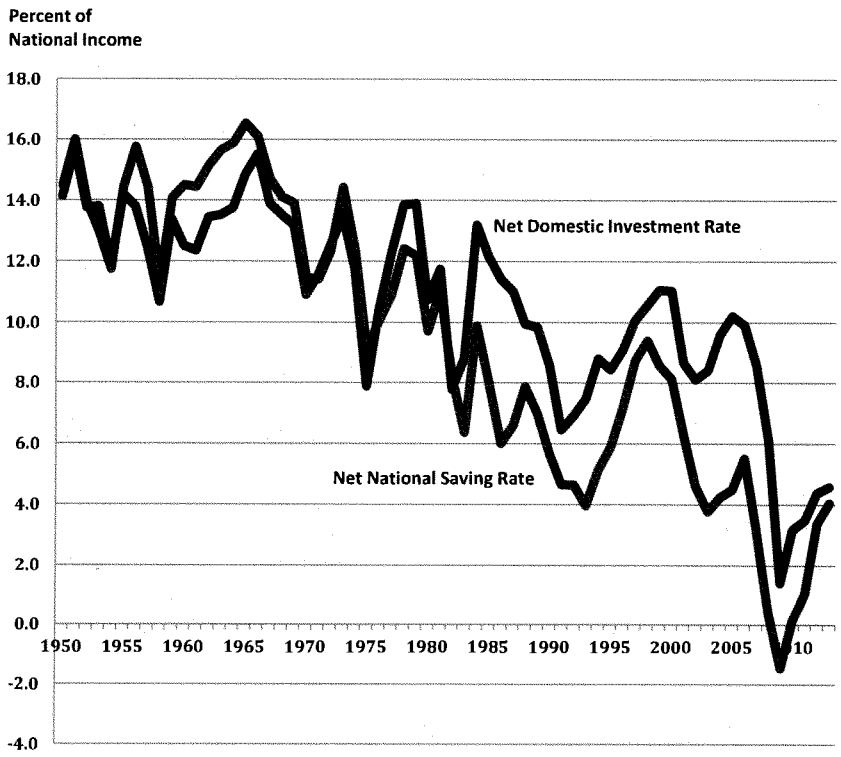
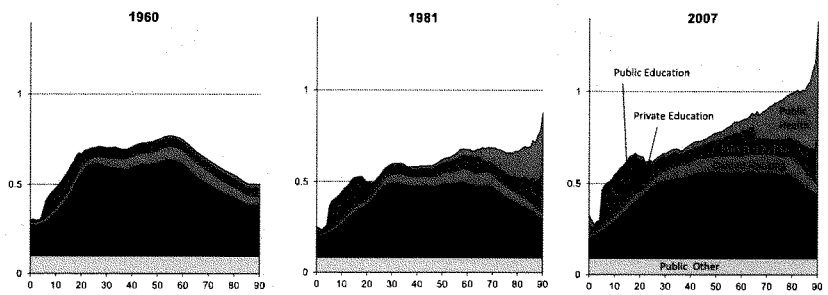


Chart 3

US consumption Per Capita by Age, 1960, 1981 and 2007

(Ratio to average labor income ages 30-49)




Source: US National Transfer Accounts, Lee and Donehower, 2011

Chairman ENZI. Thank you.
Ms. Pfitzenmaier?

**STATEMENT OF HEATHER PFITZENMAIER, DIRECTOR, YOUNG LEADERS PROGRAM, THE HERITAGE FOUNDATION**

Ms. PFITZENMAIER. Thank you Chairman Enzi, Ranking Member Sanders, and the distinguished members of the Budget Committee for the invitation to speak here today.

My name is Heather Pfitzenmaier, and I am the director of the Young Leaders Program at Heritage. Before I begin, the views in my testimony are my own and should not be construed as representing any official position of The Heritage Foundation.

Heritage is a 501(c)(3) research and educational institute, and our mission is to formulate and promote public policy based on key principles of limited government, individual freedom, traditional values, free enterprise, and a strong defense. The vision is to build an America where freedom, opportunity, prosperity, and civil society flourish.

In my role as director of the Young Leaders Program, I have the privilege of overseeing our internship program, campus outreach, and other programs which connect with young Americans every day. I have the opportunity to hear from these young Americans about their aspirations, challenges, and hopes for the future.

I am here today to be a voice for these young people and to say that I do not want my generation to be doomed as the debt-paying generation. If Congress does not act to reduce the spending, deficits, and debt, that is exactly what my generation and subsequent generations will be: saddled with debt.

Think about young people you know, like Kimberly. She is coming of age in a weak economy, where for many it has been hard to find a job. She already knows she will graduate from college with a huge personal debt. Now she must also think ahead to the future and the massive public debt that is coming to her and other young people. According to publicly available information, by 2028, when millennials will be in their mid-to late thirties, the public debt per capita is estimated to reach $66,000. It is jarring to think of having a mortgage this size but with no asset of a house.

If Congress does not act, my generation and the generations to come will face many unpleasant consequences. Some will be felt immediately, others much later in life.

Higher debt threatens opportunity and stifles growth. Not only will these student loans be more difficult to pay off for those who chose to go to college, but it will mean less money available for more education, for savings, for retirement, for health care. Maybe, like Jeff, they still live at home with their parents because they cannot yet afford to live on their own.

Countless other young people are underemployed, perhaps with a college degree and not working in their professional field, or even worse, not employed at all. Individuals cannot get those years back. Those earnings they could have made cannot be recouped. Those job opportunities and experiences are gone.

Excessive debt also hinders businesses trying to get a loan to start a business or expand and grow. Some young people want to launch a startup. Others, many of whom just started a family,

want to sell something on Etsy and work flexible hours that work for them.

Higher debt also increases the likelihood of inflation. Higher debt can lead to higher interest rates. What about the young person thinking through whether they can afford college? Or starting that business? Or buying a new home for their growing family? What is our outlook for the future?

Higher debt can lead to higher taxes, and higher taxes eventually means less money going into the pockets of young people when they need it and are growing their families and looking to the future. For many in my generation, it will mean less choice about the size of our families. Many will buy their first home later in life, others perhaps not able to afford one.

My generation does not want to be the first generation in living memory to have a poorer future than our parents did. One of the things that is so great about our country and Americans has been that each generation desires to leave our Nation and world a better place than they found it. At least that is how it worked in the Sexton and the Pfitzenmaier families.

How long can we pass higher and higher levels of debt along to the next generation? I am here to ask you to make the necessary changes and be part of the solution. I am fortunate to be here, to have the opportunity to speak to all of you. Many in my generation do not. Many are not even old enough to vote yet. Is it right to leave all this debt and its real consequences to a generation that has not had a role in making these decisions?

Individuals in their twenties and thirties should be launching our lives, building for our future. Instead, we and those younger than us are burdened by this ever-growing and looming debt and the impact it currently has and will have on our earning potential and lives.

This is no longer just a fiscal moment, as you have already heard. It is a moral one. Young professionals starting a family do not deserve to be bearing the burden of all of this debt. Students finishing high school and college do not deserve reduced economic mobility and opportunity. Our Nation deserves action. Americans deserve solutions. We all deserve an America where there is opportunity for all and favoritism to none.

Thank you.

[The prepared statement of Ms. Pfitzenmaier follows:]

**Testimony of Heather Pfitzenmaier**
**Before the Senate Budget Committee**
**February 25, 2015**

Thank you Chairman Enzi, Ranking Member Sanders, and the distinguished members of the Budget Committee for the invitation to speak here today.

My name is Heather Pfitzenmaier, and I am the Director of the Young Leaders Program at The Heritage Foundation. Before I begin, the views I express in this testimony are my own, and should not be construed as representing any official position of The Heritage Foundation. Heritage is a 501(c)(3) nonprofit research and educational institute. The mission of Heritage is to formulate and promote public policy based on individual freedom, limited government, free enterprise, traditional American values, and a strong national defense. The vision is to build an America where freedom, opportunity, prosperity, and civil society flourish.

In my role as Director of the Young Leaders Program, I have the privilege of overseeing our internship program, campus outreach, and other Heritage programs which connect with young Americans. I also am involved with and serve on the advisory boards of other youth organizations. So, in my work, I have the opportunity to hear from young Americans every day about their aspirations, challenges, and hopes for the future.

I am here to be a voice for young people and to say that I do not want my generation to be doomed as the debt-paying generation. If Congress does not act to reduce the spending, deficits, and debt, that is exactly what my generation and subsequent generations will be: saddled with debt.

Think about the young people you might know, like Kimberly. She is coming of age in a weak economy, where for many it has been very difficult to find a job. She already knows that she will graduate from college with a huge personal debt. Now, she must also think ahead to the future and the massive public debt that is coming to her and other young people. According to publicly available information, by 2028, when millennials will be in their mid-to late 30s, the public debt per capita is estimated to reach $66,000. It is jarring to imagine having a mortgage this size but without the asset of a house.

If Congress does not act, my generation and the generations to come will face many unpleasant consequences. Some will be felt immediately. Some will be felt much later in life. I am here to voice some of the concerns I hear about the debt and how it impacts young Americans' hopes for the future. I hear them from the nearly 200 interns from all across the nation who I oversee each year. I hear from students at the campuses I visit, conferences I attend annually, and groups I host at Heritage.

**Higher debt threatens opportunity and stifles growth**. Not only will student loans be more difficult to pay off for those who chose to go to college, but it will mean less money available for savings, for education, for retirement, and for health care. Young people have and may continue to face a weak economy. Overall, we fear slower and lower earnings over our lifetimes.
The result will be real consequences for our lives. We all know young people who are confronting these challenges already. Maybe, like Jeff, they still live with their parents, because cannot yet afford to live on their own. Countless young people are underemployed – perhaps with a college degree and not working in their professional field. Or even worse, they are not employed at all. Individuals cannot get those years back. The earnings they could have made cannot be recouped. These job opportunities and experience are gone.

**Excessive debt also hinders businesses trying to get a loan to start or expand and grow.** Young people come from all backgrounds, with different passions and goals. Some want to launch a start-up. Others, many of whom just started their families, want to sell something on Etsy, a great online platform for individuals to sell their homemade goods, and work flexible hours to be available for their families. These young professionals do not want to have government create barriers that hinder them from making a positive, productive impact for themselves, their families, and their communities.

**Higher debt increases the likelihood of inflation.** Higher debt can lead to higher interest rates. What about the young person thinking through whether they can afford college? Or starting their business? Or buying a home for their new and growing family? What is our outlook for the future?

**Higher debt can lead to higher taxes**. Higher taxes eventually mean less money going into the pockets of young people when they need it and are growing their families. If, as we fear, economic growth will be slower, incomes will be less. For many in my generation, it will mean we will less choice about the size of our families. We will buy our first home later in life – if we can ever afford one. All of these have a ripple effect on other industries.

My generation doesn't want to be the first generation in living memory to have a poorer future than our parents did. One of the things that is so great about our country and Americans, has been that each generation desires to leave our nation and world a better place than they found it. At least that is how it worked in the Sexton and the Pfitzenmaier families. My generation does not want to be the first generation unable to leave things better for our children and grandchildren. It will be because the Congress failed to act when it could to make sure we will not become the debt paying generation.

How long can we pass higher and higher levels of debt along to the next generation? I am here to ask you to make the necessary changes and be a part of the solution. I am fortunate to be able to be here, to have the opportunity to speak to all of you. Many in my generation do not – many are not even old enough to vote yet. They do not have the same opportunity to speak up. Is it right to leave all of this debt and its real consequences – to a generation that has not had a role in making these decisions? And many still cannot get involved to change the course.

Individuals in their 20's and 30's should be launching our lives, building our future. Instead, we and those younger than us are burdened by this ever-growing and looming debt and the impact it currently has and will have on our earning potential.

This is no longer just a fiscal moment. It is a moral one. Young professionals starting a family do not deserve to be bearing the burden of all this debt. Students finishing high school and college do not deserve reduced economic opportunity and mobility. Our nation deserves action. Americans deserve solutions. We all deserve an America where there is opportunity for all and favoritism to none.

Thank you.

Chairman ENZI. Thank you.
Mr. BARTLETT.

**STATEMENT OF BRUCE BARTLETT, FORMER DEPUTY ASSISTANT SECRETARY FOR ECONOMIC POLICY, U.S. DEPARTMENT OF THE TREASURY**

Mr. BARTLETT. Thank you, Mr. Chairman. I am just going to make a few sort of random points about the debt, simply because I seldom hear these mentioned in conversations, including those we have already heard from.

One is that we need to understand that the debt is a stock, and it is not a flow. The flow associated with the debt is interest on the debt. And so when we talk about, for example, the debt as a share of GDP, we are comparing apples and oranges. We should compare—I mean, Mr. Enzi, you told me you are an accountant, so we are comparing a balance sheet item to an income statement item. We ought to have an apples-to-apples comparison, so we should look at the debt as a share of our assets.

Now, we do not really know what the Federal Government's assets are. The financial statement of the United States Government takes a stab at that, but, of course, almost everything is carried at historical cost, so the numbers are worthless.

But the number that I think is important is interest as a share of GDP, and that number is 1.3 percent. It was as high as 3.2 percent just a few years ago. So by any meaningful standard, the burden of the debt is about a third of what it was just a few years ago. It has not been rising. It has been falling.

Also, I think that is important to understand, especially to members of this Committee, that budget conventions overstate the Government's interest cost because it treats the Federal Reserve as if it is part of the general public when, in fact, of course, it is part of the Federal Government. The Fed right at the moment owns about $2.5 trillion of Treasury securities that, for all intents and purposes, are the same as, for example, those held in the trust funds for the Social Security Administration. And although Treasury pays the Fed interest on that debt, last year paid $116 billion in interest, the Fed subtracts some percent for its costs, but then it gives it all back, or almost all of it. Ninety-nine billion dollars was simply a gift from the Federal Reserve to the Treasury of the interest that the Treasury had previously paid to the Fed.

Now, in my own personal opinion, we ought to adjust our financial account so that that money is subtracted from the net interest cost in order to make more accurate the true burden of interest in the budget, because I think that is the one number that really matters.

I would just like to make a point that Professor Kotlikoff made because it is not often mentioned, which is that tax cuts increase the burden of debt because it is the difference—the annual increment to the debt, the deficit, is the difference between income and outgo. And I presented a table in my testimony that I think is quite interesting because it is based on projections that the CBO made in January of 2001, before President Bush even took office, and looked at the projections of the debt at that time, and at that time the debt was about $6 trillion, and the CBO was projecting

a budget surplus of $6 trillion over the next 10 years. If we had simply done nothing, we would have paid off the entire national debt by now. But we did not do nothing. We started wars, we enacted huge tax cuts, we enacted new entitlement programs. And the result of all that is that we went from instead of having zero debt to having a $12 trillion debt. So we, in essence, added $12 trillion to the debt during that 10-year period.

I would like to make the point that capital investments are not netted out. We do not have an operating budget and a separate capital budget. I think that would be a good idea. All the States, we always talk—many people talk about how important it is that the States balance their budgets. We should do so, too. The States only balance their operating budgets. They do not balance their capital budgets. And I think it would be a good idea to shield capital investments in vital national infrastructure from across-the-board budget cuts. I think that is penny-wise, pound-foolish.

There has been a lot of talk about the burden of the debt on future generations. It is seldom noted that future generations inherit all the assets as well. It is true that they inherit the burden of paying interest on the debt, but they get the bonds. They receive the bonds themselves. If all of the national debt was owned by Americans, we would literally owe it to ourselves, and the money would just circulate around and go from one group of people to another. There would be no net burden in the aggregate.

We sometimes worry about the debt held by foreigners. They own about half of the debt these days. But the only reason countries like Greece and Argentina have ever gotten into trouble in this area is because their debt was not denominated in their own currency. One hundred percent of the United States' debt is denominated in dollars. We can always raise whatever revenue we need to pay those bonds. We do not have to raise foreign exchange. We do not have to get gold to pay those debts. And if worse comes to worse, we can just print the money. So there is never a danger that the United States Government will default.

I will simply stop there. You can read my statement. But I do think that the net of this conversation we are having here is to grossly overexaggerate whatever the real economic costs of the debt are. I mean, debt as a share of GDP was well over 100 percent, much higher than it is right now, when I was born. And if I were sitting at a panel like this one in 1951, I would be hearing how terrible the future would be. But, in fact, the future was quite good. The 1950s and 1960s were two of the greatest decades we have ever had despite this horrible burden of debt that we inherited from World War II, which was very, very large.

So I think it is not—it does not really make sense to take every single thing that is wrong with our economy, such as the lack of wages and income distribution and things like that, and just automatically attribute it to the debt. I think that is not—that does not really make sense. We need to do a deeper analysis and look more carefully at the situation.

Thank you.

[The prepared statement of Mr. Bartlett follows:]

**Statement of Bruce Bartlett**
**Before the Senate Budget Committee**
**February 25, 2015**

Thank you for the opportunity to testify this morning on "The Coming Crisis: America's Dangerous Debt."

I should state up front that I don't necessarily agree with the premise of this hearing. I don't think there is a debt crisis looming in the near or medium term on the basis of present or foreseeable policies, or that the national debt is per se dangerous.

Let me briefly make a few points about the debt that I seldom see in popular discussions of this topic.

1. ***The nominal debt is irrelevant***. By this I mean the dollar figure, which, as this is written, is $18,~~138,241,907.59~~141,409,083,212.36. That's a lot of money and it scares people. It makes them accept policies that may not only be unnecessary, but harmful. Cutting spending in a recession is clearly counterproductive and I think that the cuts that have been enacted over the last several years were unwise and slowed growth in the economy. The fact that the U.S. economy is doing marginally better than some in Europe is because they cut spending even more than we did.

2. ***The debt is a stock, not a flow***. To determine whether the debt is "excessive" we have to compare it to something that approximates ability to pay. Typically, we look at the debt as a share of the gross domestic product. But this is not a proper comparison; we are comparing apples and oranges. To get an apples-to-apples comparison, we should compare the debt to the federal government's assets. The comparable figure to GDP would be interest on the debt. Presently, net interest is 1.3 percent of GDP, well down from 3.2 percent in 1992. CBO currently estimates that this percentage will rise in coming years to 3 percent of GDP in 2025. This is due primarily to a projected rise in interest rates, rather than a rise in debt. This problem could be mitigated if the Treasury issued more long-term debt now while interest rates are low.

3. ***Budget conventions grossly overstate the interest cost***. The reason is that the budget treats the Federal Reserve as part of the public rather than part of the government. Presently, the Fed owns $2.5 trillion of Treasury securities, on which it receives interest from the Treasury.[1] But the Fed pays almost all of it back to the Treasury. In 2014, Treasury paid the Fed $116 billion in interest. After subtracting various costs, the Fed returned $99 billion to the Treasury.[2] This amount should be subtracted from the federal government's interest expense, just as we do with interest

[1] http://www.federalreserve.gov/releases/h41/current/h41.htm#h41tab1.
[2] http://www.federalreserve.gov/newsevents/press/other/20150109a.htm.

paid on trust funds. Instead, the Fed's payment to the Treasury is treated as a miscellaneous receipt.[3]

4. ***Tax cuts increase the debt.*** This may seem like an obvious point, but some of my conservative friends often act as though this is not the case. According to the Congressional Budget Office, tax cuts enacted between 2001 and 2011 added close to $3 trillion to the national debt.[4]

**Changes in CBO's Baseline Projections, 2001-2011**

| **Change in Surplus** | **Billions of dollars** |
|---|---|
| Economic Growth and Tax Relief Reconciliation Act of 2001 | -1,256 |
| Jobs and Growth Tax Relief Reconciliation Act of 2002 | -328 |
| Working Families Tax Relief Act of 2004 | -121 |
| Economic Stimulus Act of 2008 | -106 |
| American Recovery and Reinvestment Act of 2009 (tax provisions) | -253 |
| Tax Act of 2010 | -354 |
| Other | -461 |
| Subtotal of legislated tax changes | -2,879 |
| Subtotal of economic and technical effect on revenues | -3,484 |
| Total revenue change | -6,363 |
| Discretionary spending | -2,947 |
| Mandatory spending | -1,403 |
| Net interest | -1,376 |
| Subtotal of legislated spending changes | -5,726 |
| Subtotal of economic and technical effect on spending | +87 |
| Total spending change | -5,638 |
| Projected surplus as of January 2001 | +5,891 |
| Actual deficit | -6,111 |
| Total fiscal change | -12,002 |

5. ***Capital investments are appropriately financed by borrowing.*** There is an unfortunate tendency to treat all government spending as if it is consumption. Economists will commonly subtract the deficit from national saving to determine net saving. But of course, the federal government makes unambiguous investments in physical, technological and human capital that provide benefits for future citizens as well as those today. It would be highly desirable to clearly separate capital expenditures from operating expenses in the budget.[5] It is penny-wise/pound-foolish to cut infrastructure investments. Those who note that the states have balanced budget requirements and favor one for the federal government never call attention to the fact that such requirements apply only to state operating budgets, not capital budgets.[6]

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[3] Bruce Bartlett, "Fiscal Effects of the Federal Reserve," *Tax Notes* (January 23, 2012): 471-2.
[4] http://www.cbo.gov/sites/default/files/06-07-ChangesSince2001Baseline.pdf.
[5] There was a commission to study this idea in 1999: http://clinton3.nara.gov/pcscb/report.html.
[6] Thomas A. Garrett, "State Balanced-Budget and Debt Rules," Federal Reserve Bank of St. Louis (2011).

6. ***Those that fear the burden of the debt on future generations always forget that future generations inherit the assets as well.*** In the case of the national debt, it is true that future generations will inherit the obligation to continue paying interest, but they also inherit the bonds on which that interest is paid. While relatively few individuals may own Treasury securities, vast amounts are owned indirectly by pension funds and insurance companies for which they are a vital asset with which they will pay benefits to future generations. If the national debt were entirely owned by Americans, we would literally owe it to ourselves; there would be no burden in the aggregate.

7. ***The burden of debt owned by foreigners is not a problem as long as it is denominated in dollars.*** In every single case where a nation has gotten into debt trouble, such as Greece or Argentina, it has been because they sold bonds denominated in currencies they cannot control. Their problem wasn't so much that they couldn't service the debt as that they lacked the means to make or refinance principal payments when due. This cannot happen to any country that only sells bonds denominated in its own currency. In the early days of the Republic borrowers needed gold to service foreign debts. This is the principal reason why the Founding Fathers were opposed to government borrowing. In recent history, the U.S. has borrowed in foreign currencies only once back in the Carter Administration.[7]

8. ***The debt limit is a dreadful way to try and constrain the growth of debt.*** It manifestly does not work and creates unnecessary risk in financial markets when it is not raised in a timely manner. It should be abolished.[8] Since Congress is unlikely to do this, I have long urged the president to utilize his power under section 4 of the 14th Amendment to the Constitution to invalidate the debt limit. The legislative history of this provision makes clear that its purpose was to prevent Congress from holding the debt hostage to a political agenda.[9]

9. ***Analogies between a family's debt and the federal government's are totally invalid.*** There are two key reasons. Humans die and their books must be balanced at death, with all debts paid, passed along or written off. But the federal government lives forever; there is never a point at which its books must be balanced as a matter of principle. Second, if families get into debt trouble they cannot legislate higher revenues for themselves; the federal government can. The ultimate guarantor of the debt is the federal government's taxing power and secondarily its power to print money. Absent a problem with the debt limit, which is a technical legal problem, not an economic one, the federal government cannot default; families can and do.

10. ***There is no relationship whatsoever between the deficit and inflation.*** Historically, inflation has been the number one reason to oppose deficit spending, which is the annual increment to the debt. The history of the last several decades is sufficient reason to dismiss this argument. Indeed,

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[7] B. Dianne Pauls, "U.S. Exchange Rate Policy: Bretton Woods to Present," *Federal Reserve Bulletin* (November 1990): 902.
[8] I testified to this effect before the Senate Finance Committee on February 14, 2002.
[9] Bruce Bartlett, "The Dangers of Debt Limit Brinksmanship," *Tax Notes* (September 30, 2013).

the biggest problem facing the world economy today is deflation, most obviously in commodity markets, but in consumer prices as well. Recent research suggests that an aging society will tend to be deflationary, which may be a cause of secular stagnation.[10] Forecasters expect continued low inflation for the foreseeable future.[11]

11. ***The supply of private saving is vital to determining whether the debt is sapping economic growth.*** As I noted earlier, many economists assume that the deficit is negative saving and insofar as net national saving is a key determinant of growth, they believe deficits could crowd private borrowers out of financial markets and reduce investment, which would reduce growth.[12] This may have been the case in the 1970s, but today the economy is awash with saving, as shown by the low level of interest rates. Also, saving can be imported if domestic saving is insufficient to finance domestic investment. Historically, U.S. foreign investment has approximately matched foreign investment in the U.S., including Treasury securities, and the U.S. has long gotten a higher return on its foreign investments than foreigners have gotten on their investments in the U.S.

12. ***To a large extent, the burden of the debt is a function of the efficiency of the tax system.*** Since the true burden of the debt is the interest cost, it stands to reason that the revenue needed to pay it is critical to determining how burdensome that is. All tax systems impose what economists call a "deadweight" cost over and above the tax itself. If this deadweight cost is reduced by a tax reform that improves tax efficiency then the burden of the debt is reduced.[13] Of course, to the extent that tax policy can improve economic growth that will also reduce the burden of the debt.[14]

13. ***There is no 90 percent of GDP threshold for debt that must be avoided at all cost.*** This was the popular interpretation of a famous paper by the economists Carmen Reinhart and Kenneth Rogoff.[15] However, recent research and correction for coding errors in the Reinhart-Rogoff paper now show no threshold effect.[16] This is not to say that debt never reduces growth, only that it depends on circumstances, such as the trajectory of debt and other factors.

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[10] P. Gajewski, "Is Ageing Deflationary? Some Evidence from OECD Countries," *Applied Economics Letters*, forthcoming; Mitsuru Katagiri, Hideki Konishi and Kozo Ueda, "Ageing and Deflation from a Fiscal Perspective," Federal Reserve Bank of Dallas (November 2014).

[11] "Low Inflation: More in the Pipeline," Goldman Sachs (February 20, 2015).

[12] Jonathan Huntley, "The Long-Run Effects of Federal Budget Deficits on National Saving and Private Domestic Investment," Congressional Budget Office (February 2014).

[13] Hans A. Holter, Dirk Krueger and Serhiy Stepanchuk, "How Does Tax Progressivity and Household Heterogeneity Affect Laffer Curves?" National Bureau of Economic Research Working Paper No. 20688 (November 2014).

[14] "Economic Growth and Tax Policy," Joint Committee on Taxation (February 20, 2015).

[15] Carmen M. Reinhart and Kenneth S. Rogoff, "Growth in a Time of Debt," *American Economic Review* (May 2010): 573-78.

[16] Thomas Herndon, Michael Ash and Robert Pollin, "Does High Public Debt Consistently Stifle Economic Growth? A Critique of Reinhart and Rogoff," *Cambridge Journal of Economics* (March 2014): 257-79; Balázs Égert, "The 90% Public Debt Threshold: The Rise and Fall of a Stylized Fact," Organization for Economic Cooperation and

14. ***To the extent that we have a debt problem, the principal cause is unfunded wars, not benefits for the poor, elderly and disabled.*** One can easily argue that the national debt is simply the cost of past wars adjusted for the associated interest expense plus postwar costs such as for veterans' benefits.[17] Thus far, the wars in Iraq, Afghanistan and other post-9/11 conflicts have added $1.6 trillion to the national debt.[18] Future costs for these operations are estimated at $4 trillion to $6 trillion.[19] Polls show that Americans blame wars more for our debt problems than domestic spending.[20] In my opinion, it is irresponsible to start wars without raising taxes so that all Americans are invested in the fighting.[21]

15. ***Generational accounting exaggerates the burden of debt.*** Intergenerational accounting attempts to assess financial burdens through time, especially with a view to claiming that financial decisions taken in one generation can impose burdens on another. But this argument refuses to count as real assets the infrastructure and other national assets that the current generation will leave for future generations, and it does not understand that federal government debt never needs to be retired. In real terms, there obviously are no intergenerational transfers, except for the knowledge, the physical assets and the larger environment, which the present leaves to the future. The real goods produced in 2050 will be distributed to those alive in 2050, regardless of the public debt in existence at that time. Meanwhile, the U.S. government can always meet its payments when they come due.[22]

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Development (June 2013); Andrea Pescatori, Damiano Sandi and John Simon, "Debt and Growth: Is There a Magic Threshold?" International Monetary Fund (February 2014); Jurgen Amann and Paul Middleditch, "Revisiting Reinhart & Rogoff After the Crisis: A Time Series Perspective," University of Manchester (January 2015).

[17] Gawon Yoon, "War and Peace: Explosive U.S. Public Debt, 1791-2009," *Economics Letters* (April 2012): 1-3.

[18] Amy Belasco, "The Cost of Iraq, Afghanistan, and Other Global War on Terror Operations since 9/11," Congressional Research Service (December 8, 2014).

[19] Linda J. Bilmes, "The Financial Legacy of Iraq and Afghanistan: How Wartime Spending Decisions Will Constrain Future National Security Budgets," Kennedy School, Harvard University (March 2013).

[20] "More Blame Wars than Domestic Spending or Tax Cuts for Nation's Debt," Pew Research (June 7, 2011).

[21] Historically, taxes have always been raised to pay for wars. Only since 2003 has this norm been ignored. See Robert Hormats, *The Price of Liberty: Paying for America's Wars* (NY: Times Books, 2007).

[22] Kathy Ruffing, Paul N. Van de Water and Richard Kogan, "'Generational Accounting' Is Complex, Confusing and Uninformative," Center on Budget and Policy Priorities (February 6, 2014); Peter Diamond, "Generational Accounts and Generational Balance: An Assessment," *National Tax Journal* (December 1996): 597-607; "Who Pays What and When? An Assessment of Generational Accounting," Congressional Budget Office (November 1995).

Chairman ENZI. Thank you. And as one of the two accountants on this panel, I want to thank both of you for your comments about some additional budgeting that we need to do. I have tried to get a capital budget since I got here and some more honest numbers and the fiscal gap accounting. Wow. I am not sure what complications that would provide because it would be better numbers, and I am not sure that we are prepared for better numbers yet.

Dr. Kotlikoff, I have heard it is argued that the U.S. need not worry about its fiscal imbalances and level of public debt since we can just print more money and issue more debt. Somehow that does not sound right to me. As the other economist, what do you think? And, also, if our debt continued to rise rapidly, as some appear to want, what effect would this have on private investment and savings?

Mr. KOTLIKOFF. I am a little perplexed by some of what Bruce has said here. If it was just so simple we could print money to pay for everything, why should we have any taxes whatsoever? Why don't we just pay for everything, pay off the official debt, $13 trillion that is in the hands of the public, print $13 trillion today, pay for all the Social Security benefits and Medicare benefits, everything else, discretionary spending, just by printing money and do it forever? Now, what would that mean?

Well, it would mean hyperinflation. We have tried this experiment in other parts of the world. Argentina is trying it today. Germany tried it. There were 20 hyperinflations in the last century. They were disastrous for the country.

Our obligations are almost entirely real. The Medicare benefits are going to be real. So if inflation takes off, they are going to have to be increased to pay the doctors' real salaries. The same thing with the military. So you really cannot make much money by printing money in real terms. I think it is just a ridiculous notion. It is—I am aghast. I do not think any of the 1,200 economists who have endorsed the fiscal gap accounting would find that an intelligent response to this $210 trillion fiscal gap.

Chairman ENZI. Thank you. I want to ask you another question, though, because you made a strong case for adopting a different way to measure our current fiscal position. You advocate going to a fiscal imbalance measure that uses an infinite horizon calculation. How would you proposed to implement the changes in fiscal accounting? And what difference would it make to our policy debates?

Mr. KOTLIKOFF. Well, it would put everything on the books. It would stop this Enron-type accounting where you put certain things—where Congress gets to choose what to put on the books and what not.

Let me try and illustrate this concretely. You folks are all referencing the debt, the official debt, and, frankly, I have no idea what the word "debt" means, because I can make it whatever I want to make it just by changing language. So let me just give you an illustration.

Suppose you wanted to get rid of the official debt today. Suppose you offered to everybody who holds Treasury bonds and bills the opportunity to swap those for future higher Social Security benefits. They could just turn those in for higher Social Security benefit

commitments by the Government, and maybe you made that an attractive swap. Well, you would have no debt on the books tomorrow. And, therefore, would we have no problem? Would we have no fiscal issues? We could have a world where there is a balanced budget all the time, where we use words so that there is never any debt showing up on the books. But we can still drive our kids broke.

And here is how it works. You take young people. Let us suppose you folks on the right here are young, and you are old. You take young people, and you take money from them. You call it taxes. Give it to the old people. They get to consume more. You tell the young people, "Don't worry. When you are old, we will give you twice what you paid us. That is more than interest on what you paid us."

You become old. You are sitting over here. We come to the next set of young people. We have to take more from them. Taxes are equaling expenditures. There is no deficit. Take more from them, give it to them, tell those young people, "Don't worry. We are going to give you twice as much as you gave us."

We keep doing this. What is the problem with this? Well, the problem with this is that we come to a point where those young people that are sitting there do not have anything to give. You take everything that they have earned, and you give it to the old people, and that is the end of the game. That is game over. That is what we have been running in this country. We have been hiding the—we have been taking most of the money from the young and giving it to the old and giving promises to the young in the form of commitments that are off the books.

My mom is 95. She gets checks every so often from the—well, every month from Social Security and every so often from the Treasury for Treasury bonds. They look the same. But the Treasury bond checks, the only thing that is different is the amount on the check. But the present value of the money that is coming in Treasury bonds is put onto the books. The present value of her Social Security benefits, which are safer because they are indexed against inflation, and they also have not the full faith and credit banking, not those words backing those checks, but the AARP backing those checks, the political power of 50 million people backing her payments. So that is a much stronger liability. It is not on the books.

So you folks are having conversations about numbers that do not matter, that are not real numbers. The entire economics profession, with the exception of people on the extreme wings here—Paul Krugman and Art Laffer are not on the list of 1,200 economists, neither is Bruce Baker, who have endorsed the INFORM Act. But you have people on the far right and the far left, mostly are Democrats—the majority of the economists there I think have voted Democratic, and they are saying that we have to measure what we really owe, which is the fiscal gap. That is expenditures minus the taxes all valued in the present. And it is saying that we have to do this immediately. And in terms of the cost of doing this, it takes me about 5 minutes to take the CBO numbers in Excel and produce the fiscal gap. I have to extend those into the future. That is easy to do. And the reason we need the CBO to start focusing

on that is that that will focus your attention on the fiscal gap, and we will start budgeting on the basis of the fiscal gap.

In terms of capital budgeting, the fiscal gap does not say you cannot make investments that will pay for themselves. If you think that educational investments, increasing the expenditures will produce in the future more tax revenues and more than pay for themselves or highway investments or any type of R&D, the fiscal gap analysis will not say that is a bad thing. It will say that is a good thing. But it is a conversation that makes sense.

Chairman ENZI. Thank you. My time has expired, and I will have questions for the other two of you. Senator Sanders.

Senator SANDERS. Thank you, Mr. Chairman.

Dr. Kotlikoff believes that we are taking from the young to give to the old. I think the history of the last number of decades is that we have taken from the middle class and the working families of this country and given to the super rich. But I wanted to start off with a question for Dr. Bartlett, and I must confess that this is unusual for me because I am introducing somebody who worked for Ronald Reagan, who worked for the first President Bush, who worked for Congressman Jack Kemp, and worked for Ron Paul. He is my witness, not yours, so this is a little bit surprising. But I want to ask you, you used to be—you worked very hard with Republicans to advance supply-side economic policies, many of the same policies that my colleagues here today advocate. Today that is not your view. It is my understanding that you believe that the lack of aggregate demand, not the debt, is the biggest challenge that the economy faces, and you have supported policies to significantly increase spending on our Nation's infrastructure, among other things.

It is my understanding that you also believe that we should substantially increase revenue mainly by closing tax loopholes that benefit the wealthy.

Why years ago were you an advocate of supply-side economics? Why have you changed your views today?

Mr. BARTLETT. Well, first of all, Senator, thank you for the honorary Ph.D., but I do not have one. Thanks—unless it is from the School of Hard Knocks.

But everything you said is exactly correct, and, in fact, I worked with Larry Kotlikoff in years past, with conservative organizations, and I have not actually changed my fundamental philosophy, despite what a lot of people think. It is just what has happened is that circumstances have changed. I still think that the Reagan tax cut, which evolved from something called the "Kemp-Roth tax bill"—I drafted that legislation when I worked for Jack Kemp. I still think that was very good policy in 1981. I think it helped the economy. But I do not think that the nature of our economic problem today will be helped by tax cuts.

I think our basic problem has to do with the problem of very low interest rates. The "zero bound," as economists call it, makes it very hard for monetary policy to be functional. I think, you know, several years ago, when the Federal Reserve greatly increased the money supply by well over $2 trillion, every single conservative economist I know of was predicting hyperinflation. They were all saying, "Buy gold. We are going to go bankrupt." But none of that

happened because they were not looking at the particular economic circumstances that are quite different today from any time in our history except the Great Depression.

Now, if you go back to that era—

Senator SANDERS. Let me interrupt you, if I can, because I have a limited amount of time.

Mr. BARTLETT. Sure. I am sorry.

Senator SANDERS. Does it concern you that when we talk about deficits and national debts, my Republican colleagues are not forthcoming in asking large corporations that pay nothing in Federal income taxes now to start paying their fair share of taxes or that hedge fund managers have an effective tax rate lower than truck drivers and nurses? Is that an issue of concern?

Mr. BARTLETT. Yes. I think the carried interest loophole is the most egregious—perhaps the most egregious loophole in the entire Code, utterly unjustified, a huge giveaway to hedge funds. The problem of large multinational corporations storing—I do not know what the number is—perhaps $2 trillion of earnings in other jurisdictions, where in many cases it is not taxed at all. It is not a question of double taxation because they get a credit for any taxes they pay in foreign jurisdictions. But they are able to move this money around in such a way that nobody pays any taxes on it. And it does not even benefit the shareholders.

Senator SANDERS. Let me ask you this: Am I correct that you also understand that in an economy where 70 percent of our GDP is based on consumer demand, that when we have millions and millions of people who have literally no disposable income, it is going to be hard to grow the economy in the way we would like? Is that true?

Mr. BARTLETT. Yes, I agree completely. I think the problem of inequality that you pointed to is a problem. A number of organizations that are—for example, the Standard & Poor's Company put out a report just a few months ago worrying about the economic effects of growing income inequality because it said that if the people who spend do not have money to spend and the people who are getting the income are people who tend to save most of it, you are going to have too little spending and an excessive amount of saving for what the economy needs. And as you know, we have extremely low interest rates. That is evidence that we have more saving than we need, and, therefore, I think that if it were up to me, I think we desperately need a massive infrastructure program that would put people to work, that would get money mobilized, that would make Fed policy more effective.

I really think it is a tragedy that we cannot even get the Highway Trust Fund taken care of properly.

Senator SANDERS. Let me just—last question, Mr. Chairman. And I am going to mispronounce your name. Ms Pfitzenmaier?

Ms. PFITZENMAIER. Yes.

Senator SANDERS. Okay. You talk about the burden on younger people and the shift—the burden on younger people while protecting the elderly. Does it concern you that we have seen a massive shift in income and wealth inequality in this country so that we have the highest proportion of inequality in the world? Is that a concern of yours?

Ms. PFITZENMAIER. I think all Americans are concerned with making sure that our neighbors and everyone in our communities—I heard Detroit mentioned. I actually grew up about a half-hour outside Detroit. And I think the question is looking at things like mobility. How are those opportunities going to get those people who are in need to be able to climb up the ladder?

My colleague at Heritage, David Azerrad, has written a wonderful piece that I would happy to submit for the record to really look at that.

I look a lot on school choice, giving those kids—

Senator SANDERS. No, I just asked you a question. There has been a transfer of wealth, trillions of dollars, from the middle class to the top one-tenth of 1 percent. Is that an issue of concern?

Ms. PFITZENMAIER. I think we need to look at all different things of concern, and I am not a budget expert on this, but I think absolutely we need to look at really are there those opportunities to move up and help every American from every corner, from Detroit to California.

Senator SANDERS. Thank you.

Chairman ENZI. Senator Grassley.

Senator GRASSLEY. Yes, thank you all very much for participating. I am going to start with Dr. Kotlikoff.

I appreciate the work that you have done on studying generational debt. When OMB Director Donovan testified before our Committee a few weeks ago, I asked him about the debt burden of future generations and the impact President Obama's budget will have on future generations. The Congressional Budget Office has said that in future years a growing portion of people's savings would go towards buying Government debt rather than towards investing in productive capital goods. That crowding out of investment would reduce the size of the Nation's productive capital resources that, as you know, produce economic benefits over time. The smaller capital stock would result in lower wages and incomes, making future generations worse off.

My first question: To what extent will future generations be worse off by taking no action to reduce the deficit and debt in the near term? I assume that you feel that reducing the debt burden of future generations would be more prudent than 10 more years of deficit spending and growing debt, as the President's budget proposes.

Mr. KOTLIKOFF. Senator Grassley, thank you for the question. Again, the debt is not something that economics defines. Our mathematics can make the debt, the official debt, be anything we want with the words we want to use to label receipts and payments. So we are kind of having an "Emperor's New Clothes" discussion here. Every time you folks talk about the debt, I say I do not have any idea what you mean, because I can make the debt whatever number you want just by going back in time historically and relabeling things, calling things different things.

So the only real thing we can look at that makes sense, that is independent of what labels we chose, is the fiscal gap. The fiscal gap in the U.S., we do not have a long time series, but in 2003 it was $60 trillion. Today it is $210 trillion. Those are the numbers you need to be focusing on. That is what our profession—that is

what the people with the Ph.D.s actually say to look at. That is what George Shultz, 17 Nobel Prize winners—can you imagine what it takes to get 17 Nobel Prize winners from both political parties in terms of their orientation—but let me get back to your question—

Senator GRASSLEY. Well, let me take your approach, however you want to define it. My question is about making future generations worse off.

Mr. KOTLIKOFF. We are in a fiscal war against our children, and this does not undercut the issue that you are concerned about, Senator Sanders, about within a generation are we being too generous to the rich versus the poor. I have the same concerns, absolutely the same concerns on that score, the degree of intragenerational progressivity, intragenerational accounting. But we are absolutely at war with our kids. We are leaving them a bill that is going to entail at least a 58 percent higher set of taxes, if we do this all through taxes, all the correction through taxes, through the rest of their life. Every Federal tax, FICA, Federal income taxes, corporate taxes, have to be 58 percent higher to come up with $210 trillion in present value. If you wait longer, then you see in Table 2 that—or Table 1 that delaying requires even higher adjustments later on. The longer we wait, the bigger the burden is on Heather and her generation.

So, absolutely, we have a generational moral question here, and in terms of the impact—

Senator GRASSLEY. I think you have answered my question.

Mr. KOTLIKOFF. Okay.

Senator GRASSLEY. And I would like to go to Ms. Pfitzenmaier, and I would like to make a suggestion. I think that the points you make for young people are very good points, and I wish that in the 99 counties I go to every year in Iowa, I wish the young people would come and make as much concern about the debt as older people make. I think it would make a very important point. So if you can spend your time getting young people to talk to Members of Congress about how they resent the debt that we are leaving to them, I think your time would be better used. And that does not denigrate what you are doing right now.

As an advocate for future generations, how will this forecasted growth in debt affect the economic well-being of future generations?

Ms. PFITZENMAIER. Thank you for the question, Senator, and encouragement. One of the favorite parts of my job is getting the opportunity to travel around the country and speak with students and talk to them about their concerns. I know I have a short time, so I think covered a lot of that in my remarks as well as the testimony, but I think it all comes down to just the potential for lower quality of life. And that is what is really on the minds of young people, and that is what I hope that we can resolve when we look at these issues, is making sure that our generation can be better off than the one before, and then we can leave a better future for our children and our grandchildren.

Senator GRASSLEY. Thank you.

Chairman ENZI. Senator Stabenow.

Senator STABENOW. Well, thank you very much, Mr. Chairman. I appreciate your having a University of Michigan graduate on the panel, so, Ms. Pfitzenmaier, thank you.

Let me ask you—you talked about a young woman who had massive student loan debt. Do you think we should do something about that?

Ms. PFITZENMAIER. Well, thank you, Senator, and thanks for the plug for our Wolverines. I absolutely think that student loan debt and the whole higher education is another issue that is on the forefront of a lot of young people. I am not an expert on that. Lindsey Burke at Heritage is. But I know she has done wonderful work looking at the accreditation process, looking at some of these open online courses that can come, because I think that is absolutely a big source, and the ability—I know my parents were able to work and pay for their college, and I think that that is not really the ability for many young people today. So I think that is absolutely a topic to look at, and I am glad to hear that it is something you are passionate about.

Senator STABENOW. I am passionate about it. I would suggest that because we have a value of supporting education as a country, it does involve the public sector. We do not bring those costs down unless we as a country decide to also invest.

Mr. Bartlett, you talked about assets as well as liabilities. I appreciate that very much. I believe that educated people are a great asset for us, and that does involve our coming together on public investments, like other countries are doing as well, education innovation.

Mr. Bartlett, I very much appreciate the fact that you are looking from a practical standpoint about what works and what doesn't work, where we are today. And I think we are missing that in so many of these ideological discussions about debt. I come at this as a person who is in debt with a mortgage—a couple of them—who has put children through college who have had student loan debts, who has a car loan. We all go into debt. Businesses go into debt. But hopefully if you are smart about it, you do not go into too much debt. So it is based on our values. We want a roof over our heads for our families. We want to be able to drive a car. We care about our children; we want them to go to college. So we all—I mean, this whole notion that somehow—you know, this is all about values and decisions about how much, what we do, what is important. That is what this is about.

What I get frustrated about is that we see things that have worked during the Clinton years, asking folks to pay a little bit more, we balanced the budget, 222 million jobs created. There were some cuts that were made, but it was kind of done in a way that was balanced. We go into the next 10 years, and, Mr. Bartlett, you were talking about $12 trillion in debt. We would be out of debt right now, $12 trillion, because different priorities. We heard, unfortunately, during the second President Bush's years that deficits did not matter when we were going to war; deficits did not matter when we were doing not one, but two rounds of high-end tax cuts for the wealthiest Americans, increasing the gap between working Americans and those at the top.

So folks use deficits and debt for all kinds of things. I agree that, you know, it means all kinds of things. In the end, it really is about our values as a country in this great country and how we are going to all be in it together.

I also want to just say—and I am talking more than asking a question, but when we talk about Detroit, I just want to say on behalf of the people of Detroit and Michigan, this is not about tax rates in Detroit. This is about jobs; it is about infrastructure, about investments and quality of life. What people in Detroit want to know is that there are public lights that work and roads that work and schools that work and safe neighborhoods so that police and fire come when you call. And that does involve accountability on public money, but it does involve people contributing to public services. It is not just about tax rates. If it was about tax rates, Detroit would have been able to fix it. It is about much more than that in terms of our investing in people and the quality of our life.

So I am just about out of time here, but I just want to say that, whether it is—I know, Dr. Kotlikoff, one of the things that you suggest is eliminating the corporate income tax altogether and instead helping to pay for that by an additional tax on workers' wages. I am sorry. I do not get that.

Mr. KOTLIKOFF. Can I just correct that?

Senator STABENOW. Yes.

Mr. KOTLIKOFF. That is not at all what I proposed. What I proposed was that we eliminate the corporate tax and that we impute the corporate income of the shareholders, no matter what corporations they hold, whether U.S. corporations or foreign corporations, onto their personal income taxes, so there is no way in which I have suggested that we put that burden onto workers. What I have said is quite the opposite, that doing this kind of integration would lead companies to invest a whole lot more in the U.S. to improve jobs in Detroit and other places and raise the wages of workers. What I said was that this is in this paper—and, please, it is on my website. Please take a look at it. I have said nothing like that. You have to—I know you think that—

Senator STABENOW. Well, if I was wrong, I apologize. That was the information that was given to me.

Mr. KOTLIKOFF. I mean, I am over here maybe on this side of the table because I was invited by the folks on this side of the table. But I am not political. I am an economist. Okay?

Senator STABENOW. I very much appreciate that, and I am out of time. I do not mean to be rude, but I understand that. I would just argue this is more than about numbers, and right now what I am most concerned about—we have eliminated two-thirds of our annual deficit in the last few years. What I am most concerned about is the middle-class jobs deficit and education deficit and infrastructure deficit in our country. The annual budget deficit has gone down by two-thirds, and the deficits in the other areas that relate to the quality of our country, the strength of our country, have gone up. And that involves all of us together doing our fair share.

Thank you, Mr. Chairman.

Chairman ENZI. Senator Perdue.

Senator PERDUE. Thank you, Mr. Chairman.

You know, Ms. Pfitzenmaier, I agree with you, but I am on the other side of that generational gap. I do not want to be the member of the first generation that has to tell your generation that my generation is leaving your generation an America that is worse off. And yet that is what all the numbers say today, in my opinion.

The problem is a lot worse than you said, though, and, Dr. Kotlikoff, I agree with you. We can make the number—you can pick a time period and get a number. It is $150, $200 million. Pick a number. But you get it back to households. The responsibility to pay this back over time is about $2 million per household. It is not $60,000. It is about $2 million a household. We all have car payments. We all have mortgages. That is unmanageable.

And, Dr. Kotlikoff, I have a question I want to get to, but I honestly think this is the biggest crisis we face. It threatens our national security. It threatens the ability to talk about this gap. The gap we could talk about.

And, Mr. Chairman, I am sorry. The conversation in this Committee that I have watched the last three times, that conversation does not serve the American people. This partisanship that is in here, this should be like Foreign Relations, should be like Armed Services, should be like the Intelligence Committee, where we are talking in a bipartisan way to try to get at the solution to this thing. How we got here, there are no innocent parties up here. I have said this for 2 years. I have not been in politics. I am an outsider looking at this thing, and I can tell you what. People out there hear what we say in here, and it does not make any sense to them. And it does not make any sense to me. I could argue all day long that the crisis in 2009 started in 1998 when we changed the homeownership rules about mortgage qualification.

But I want to get to a question today that relates to what do we do to get out of this. I think we all realize that the problem that we have is today we are facing a problem by April 15th, we have to put a budget together. OMB, the President, wants $4 trillion. Right now in that budget there is something like $229 billion in interest payments. There is another $95 billion in accrued interest that goes to Social Security in terms of the other $4 trillion of debt. So we have $18 trillion that we talk about today.

In just simple math, if interest rates were at their 30-year historical average, somewhere around 6 percent, we would already be having a request in here on that budget for $1 trillion of interest. Personally, I can debate all day long about whether it is $200 trillion or not. But the one thing that we cannot argue is that next year we are going to have to make X number of dollars of interest payments, and if interest rates get back to a 30-year average of 6 percent, I just do not see, frankly, how we can pay that.

The question I have, Dr. Kotlikoff, is: Have we already passed this tipping point years ago? This is not a partisan question. It is a question of how—what do we do now to get out of here? And I want a follow-up question behind that.

Mr. KOTLIKOFF. Well, we are in very deep water. I have proposed—you asked what we can do. I have proposed at www.thepurpleplans.org reforms of the tax system, reform of the Social Security system, reform of the health care system, reform of the banking system, reform of the energy treatment, energy policy,

which many, many economists, including many Nobel Laureates, have endorsed these bills, these proposals. Each one of them is a postcard in length, so I would encourage you to take a look at www.thepurpleplans.org. It is purple because it is a combination of red and blue. It is supposed to interest both parties.

Those proposals could dramatically reduce, if not eliminate, the fiscal gap, and they really, I think, meet the concerns of the Republicans and the Democrats. These are what economists would say will get us out of this hole and help our kids and also produce more equality, I believe, for—within a generation, more equity, more progressivity, because we have such a complicated fiscal system. We have something like 25 major fiscal programs from the earned income tax to the alternative minimum tax, that getting a picture of the overall progressivity of the system is quite difficult. But I think that, on balance, these things would improve progressivity.

Senator PERDUE. I am sorry. I have one more question, but my time is almost up—

Chairman ENZI. Microphone.

Senator PERDUE. I am sorry. It should be on now. Sorry.

You mentioned to solve this problem, you can increase taxes 58 percent, you could cut spending 37 percent—

Mr. KOTLIKOFF. 38.

Senator PERDUE. 38 percent. But we did not talk about growing the economy, and the numbers we are being given by OMB, if we grow the economy one GDP point, 100 basis points in GDP, that is $4 trillion over 10 years.

Mr. KOTLIKOFF. Right.

Senator PERDUE. The question I have is, you know, this gridlock that we have watched in Washington for the last 15 years under several administrations, 11 different Congresses, we are not getting anywhere. That gridlock is not going—I just do not see how we are going to solve this without growing the economy. We talk about the earning gap, and I agree there is an earning gap. But we can talk about how 30 percent of the people who are not working today are contributing to that. We have created an environment out there where we just do not have the economy working. In the last 6 years alone, 4 million women have fallen into poverty, and the middle class is getting whipsawed by the economic policies. Obamacare alone has got two-thirds of small businesses have either stopped hiring or cut back employment.

So the question is: Can we get the debate about how to get the economy going into this conversation about dealing with this budget issue?

Mr. KOTLIKOFF. Okay. So one of the problems, Senator, is that we have less investment going on. If you look at this chart of the national saving rate and the domestic investment rate, you see that all this financing of higher consumption through these pay-as-you-go Ponzi scheme policies we have been running, some of which are very important, but, you know, Medicare Part D is an example. President Bush imposed a $15 trillion addition to the fiscal gap in that measure. Now, do we need health insurance for drugs for the elderly? Absolutely. But should all the elderly have been left off the hook in paying for it? Absolutely not, especially the rich elderly.

So we do need to have Government involvement in a lot of areas, including social insurance. The purple plans say this, but they also say you need to make sure we do not kill off our kids in making them pay for all our bills.

And so one way to get things turned around is to get investment up, and that means to get saving up, and that means to get consumption down actually as a share of national income, and, absolutely, getting the burden off of our small businesses.

So what about rationalizing our health care system? We now have Medicare and Medicaid, Obamacare, employer-based health care. The Government is involved in all four of these programs. We have got four different programs trying to provide basic health insurance to everybody. The Purple Health Plan provides a voucher plan, individually risk adjusted so it is actually highly progressive, that would provide a basic insurance plan for everybody in the country. I have talked o Congressman Ryan and people on the left as well. I think that is the way to go, and most economists do. This would eliminate all that paperwork that you are concerned about that employers are now facing.

Chairman ENZI. Senator Whitehouse.

Senator WHITEHOUSE. Thank you very much, Chairman, and I can say that there is nothing that I would be more pleased with than a nonpartisan conversation about the debt and the deficit. But when we open up with blaming the Obama administration for debt levels that relate back to a war he did not start, tax cuts he actually tried to overrule, and an economic downturn that caused him to take office at a time when the economy was losing 800,000 jobs a month, that is not exactly a signal that we are involved in that nonpartisan discussion.

It is also, I think, significant that debt should be the real target of our conversation. If the debt is just a stalking horse for an attack on social programs—on Medicare, on Social Security, on other things—and if it is defined, as it has been defined in this very hearing, as an overspending problem, and my colleagues refuse to look at the revenue side of the equation, again, hard to believe that is not a partisan discussion. I mean, this is a longstanding divide. The Democrats have stood up for Social Security and Medicare for generations, and Republicans have attacked them for generations. If you want to relitigate that through the debt discussion, we can do that. But I do not think that is very helpful. And it is particularly not helpful when there is more money going out the back door of the Treasury through tax credits and favors and deductions and so forth than there is actually being spent through the discretionary accounts. And ignoring that I think is mathematically not sensible and morally not fair, particularly when you have favored groups that are getting very special attention here.

I know that the oil companies have huge clout around here. They do not need subsidies. They do not need subsidies. They are making more money than any corporations in the history of the universe, and yet it is almost as an act of political fealty, "Yes, we are going to show up and do what you want, guys. We love you. Here is some more money." If that is more important than the debt, then we are not having a serious discussion about the debt.

Hedge fund managers get a tax benefit that the witnesses have already condemned through the carried interest exception, and as a result, in the recent years they have had tax rates that are lower than the tax rates for Rhode Islanders who were hospital orderlies, who were brick masons, and who were truck drivers, if you go back over the 3 years.

When we try to change that, we have a war on our hands: "No, that is an unmentionable. We cannot possibly not help our hedge fund buddies." While that is happening, while that is the conversation, we are not having a nonpartisan, legitimate discussion about the debt.

And we know a lot of American companies love to offshore. That is a huge loss to our economy in a lot of ways. But Senator Levin fought very hard to try to get these offshoring restrictions put in, to try to protect against that offshoring. Every single time he had a war from the other side of the aisle on that.

So please do not paint me into the corner of being an obstructionist or partisan about doing something about the debt when you have taken the biggest part of the problem and ruled it off limits. That just is not fair. And the math is not proper. Just none of that makes sense in any way.

The third point that I will close with is we are making some progress on the spending side. The debt is—the deficit is coming down. And what most people have said in this hearing room, when they have talked about the long-term out-year projections, is that the biggest and scariest piece of it is health care. That has been a bipartisan opinion that we have heard over and over again. And there are ways to address our health care problem that we should be seriously attending to, because we have a health care system that costs about 50 percent more than all of our industrialized competitors and produces health care outcomes, at least as measured in life expectancy, that are equivalent to Greece and Croatia. I mean, there is a great area for us to be working together, and I hope that is an area that we can focus on rather than have these exercises in kicking social programs and kicking the President all under the guise of a conversation about the debt. It is a serious problem. It deserves better, in my view.

Chairman ENZI. Senator Sessions.

Senator SESSIONS. Thank you, Mr. Chairman. Thank you for your expertise and leadership in this Committee.

Senator WHITEHOUSE. Mr. Chairman, I am sorry. May I ask unanimous consent to have a document put into the record that supports what I was saying? I apologize for interrupting the Senator.

Chairman ENZI. Without objection.

Senator SESSIONS. I do not know, Mr. Bartlett, if you were part of the group that said deficits do not matter. I never felt real comfortable with that idea.

Mr. BARTLETT. I worked for the first President Bush.

Senator SESSIONS. Deficits do matter.

Well, I guess I will just say on a political basis, I do believe the President of the United States has failed to look the American people in the eye and tell them we are on an unsustainable financial path. I think a President of the United States has a lot of duties,

and one of them is not to misrepresent the danger that we face. So I think he deserves to be criticized for that. And to suggest that the reduction in deficits that we have seen somehow fixes the problem is really dangerous and really misleading and takes the heat off us to try to fix things. And without Presidential leadership, it is hard. But I think Congress forced the Budget Control Act and made some progress, as others have said, and there are more things that we need to do.

Dr. Kotlikoff, the way I understand your position and what you are trying to have us hear is that a better way to look at where we are financially rather than debt is the fiscal gap, and the fiscal gap is relatively easily ascertainable and that we should judge ourselves on whether or not we are reducing the fiscal gap or not. Is that what you are saying?

Mr. KOTLIKOFF. Absolutely, exactly what I am saying. And it goes beyond that. It is that the debt is not a well-defined economic measure. It is not defined by our math. Our equations do not say how to label the terms in our equations. They do not say what words to use to discuss our equations. So the debt is actually not well defined mathematically. Just like time and distance is not a well-defined mathematical thing in physics. It is a concept. It is how you are moving through space, at what speed, will determine what you say the time is right now and what the distance of this table is.

So there are a zillion different measures of time and distance. They are equally useless in physics in terms of understanding anything.

The fiscal gap, the infinite horizon fiscal gap, is the only measure that is label free. So no matter what convention you use in terms of your labeling, as long as it is internally consistent, you will get the same fiscal gap. This is why the entire profession has endorsed fiscal gap accounting. They are, in effect, saying that you guys are looking at the wrong numbers on a routine basis. And so that is—you know, I think that you have to start thinking about the fiscal gap. You have to pass the INFORM Act. You have to start—I know you are focused so much on these partisan fights, but there is a way around this to get to a safe place for our kids and for the poor versus the rich within a generation, and that is these purple plans, because they are big ideas. We need big solutions now. We need big bipartisan solutions. And I think if you just start looking at those and discussing those plans, which have been endorsed by a slew of economists, I think you will stop the bickering over small stuff and get to the big picture. And it does not undermine the social insurance programs that we have. It is saying let us do the social insurance programs efficiently so we do not leave Heather in bankruptcy.

Senator SESSIONS. Thank you for sharing actual ideas about how to fix the problem, number one. I just think it is absolutely true that we have enjoyed more benefits today by creating debt, which is requiring our next generation to pay for the extra benefits we choose today. So, Ms. Pfitzenmaier, I think you are on the right track. And I agree with Senator Grassley. We do need to get our young people to better understand that, and I am sure we would be effective with it.

But we see the deficits increasing relentlessly in the years to come. The Congressional Budget Office has told us we are on an unsustainable path. Those words have grave meaning to them. It creates the likelihood of a fiscal crisis, or if we have a financial crisis, it creates, does it not, Dr. Kotlikoff, greater difficulties in working our way out of it and creating more danger? So the greater debt we have—I saw an article recently in a financial magazine trying to counsel people on their investments saying we have recessions every 10 years, about two every 10 years, more than one a decade. So we have another recession, and we are carrying this much debt. Does it not make it more difficult for us to work our way out of a future crisis if we have an unsustainable and growing debt?

Mr. KOTLIKOFF. Yes, and I am very concerned about the monetary policy, because if we have seen what the Federal Reserve has been doing for the last 8 years, it has been printing money like crazy. Now, they call this "quantitative easing," but it is really easing the burden on Congress to pay for its bills, for what the Government spends. There has been an increase of something like a factor of five in our base money creation. If that money gets out into the bloodstream of the economy, if the banks start lending it out—they are holding a lot of excess reserves—we could see inflation take off, and that could put the economy into recession and cause more problems.,

So we have to start understanding where we are going, and, you know, Ben Bernanke says it is in order to lower interest rates. You know, that is a lot of, to me, frankly, B.S. for what is really going on, which is just printing money to pay for bills. And that is not going to be a solution into the future. And increasing the money supply by a factor of five is one of the most irresponsible things you could do as a Fed Chairman.

Senator SESSIONS. Thank you.

Chairman ENZI. Senator Warner.

Senator WARNER. Well, thank you, Mr. Chairman. I want to thank the panel for being here. I apologize about the fact that we all feel fairly strongly on some of these issues, and I appreciate, Dr. Kotlikoff, you put out some ideas. And, Mr. Bartlett, I think you have raised some very valid points as well, particularly in relation to the circular flow on things like the Fed interest rates.

I do need to, I think, point out what I—and I have been, perhaps as anybody on this panel, more engaged in efforts of trying to bring the Simpson-Bowles—not a perfect plan, but a plan that led us with shared responsibility out of some of these challenges.

I do, though, need to, I think, correct some of the record. You just cannot get away from the facts that the deficit has been cut by two-thirds under this President. You cannot get away from the fact that the President, much to the chagrin of the Ranking Member and others, suggested changes to our entitlement system that I supported, things like chained CPI. But there was not a willingness from our friends on the other side, at least from a leadership level, to meet halfway.

So there clearly is blame on both sides here, and anyone who tries to assess this was started on one side or the other is just not, I do not believe, accurate.

I do think the thing in the—and the Chairman raised this point. I think we do need to recognize the issue is now growing the debt, but the deficit is actually within historic means a relatively manageable basis. But because of irresponsible actions of the preceding 40 years, the total aggregate debt is not sustainable. We can pick our accounting methods or our time frames, but we all live with the referee, the CBO, 10-year windows. Probably not the most appropriate way, but that is what we have got to play with.

And the CBO right now has just plain data that says a 100-basis-point increase in interest rates adds $120 billion on an annual payment off the top to the debt payments. That is bigger than our whole debate now about the Department of Homeland Security. That takes precedence over everything else.

The current CBO projection says that at the end of 10, debt payments alone will totally exceed defense, a national priority, or totally exceed our domestic discretionary. Right now domestic discretionary is already at historic lows. I for one, as one who has spent more time in the private sector than the public sector, believe strongly in the free enterprise system. But I do believe there is incredibly valuable commitments made by the public sector, in education, in infrastructure, in research. And as a venture capitalist, I would not invest in an enterprise right now that is spending less than 10 percent of its revenues on investments in those three categories. That is a bad business plan for America.

And if you look at the actions since the crisis, the ratio of cuts to revenue is 4:1. Simpson-Bowles had a 60:40 ratio.

So I guess what I would—and I apologize. Again, I may make it to a question or I may not, but I just think it is important to put some of these facts out on the table. You know, historic revenues, we are running at 17.5 percent of GDP. That is close to the 17.4 percent 50-year average. Anybody who says we ought to go back to the 50-year average cannot read a balance sheet. And I know the Chairman is an accountant and understands that, because we never balanced the budget when it was at 17.4. You got to get revenues—you got to get spending down, but you got to get revenues between basically 18.5 and 19.5.

Now, how we can get it, whether it is a purple plan or whether it is tax reform, but there is no way you can run this enterprise or anything close to it on the revenue stream we have got right now.

And I think Mr. Bartlett's point that in many ways the deficit—we spent a rather tiresome New Year's Eve a few years back all together where I am sure we probably did not want to spend it together where we avoided perhaps fiscal apocalypse for $600 billion in one-time revenues or 10-year revenues. We have got to do more on the entitlement side. I will take those hits and have laid out plans that have gotten me a lot of criticism from my colleagues on this side of the aisle. But you cannot get there without revenues.

You know, we are actually in a worse position than currently because we have spent that $600 billion on revenues; yet because we have gotten $420 billion in extraordinary one-time revenues from the profits from the Fed—and the way OMB books—you have got to go back to your accounting methodology The way OMB books return of the Fannie and Freddie profits, that is another 220. So we

have got one-time revenues in excess of what we almost brought the Government to the brink of an abyss. And those are not going to be coming on a going-forward basis.

So, Mr. Chairman and Ranking Member, Senator Sanders, you know, the debt has to be dealt with because it is unsustainable. But I would just ask in the spirit of what our panel has suggested that we both have to come out of foxholes. We have seen improvements in health care. We do have to recognize entitlements, and the mandatory has to be part of this. But any notion that we can get there with anything close to what the American public is expecting from the Federal Government without revenues in the mix is just not possible.

My apologies to the panel for not getting to a question.

Mr. BARTLETT. Senator, could I make a brief point about that?

Senator WARNER. Yes, please.

Mr. BARTLETT. I do agree with you about revenues, and one point that may be in the interest of bipartisanship, we used to have a principle that partisanship stopped at the water's edge. And as I pointed out, one could argue that our national debt is essentially the accumulated legacy of the costs of all previous wars.

Now, in World War II we raised taxes very substantially. Before the war, only 3 percent of American people paid any income taxes at all. By the end of the war, it was up to 30 percent. We increased taxes very substantially during the Korean War. During the Vietnam War, we had a 10-percent surtax that applied to all income, so if you owed $1,000 of taxes, the next year you owed $1,100. And Richard Nixon extended that tax.

I was working for President George H.W. Bush when, in 1990, in an act of what I think was great bravery, he raised taxes because he knew we needed the revenue to pay for the first Iraq War. Now, over the last 10 years or 12 years, whatever, for some reason we have decided that we are not going to pay for wars. And a great many of our fiscal problems result from the fact that we launched the Iraq and Afghanistan operations without asking the American people to pay, to share in the sacrifice of our soldiers. And I think it was irresponsible not to put on some kind of tax specifically dedicated to that war. And the reason I bring it up is because we are talking about another military operation, and maybe we can agree this time to put on some tax to pay for this new operation so that everybody is in this together, me and everybody else.

Senator WARNER. Mr. Bartlett—and Mr. Chairman, I will only take 10 more seconds with your—10 more seconds. I do believe absolutely what this country desperately needs is all in this together, whether it is for payment for the cost of defending our country or a debt surcharge, because I do believe Heather's comments are absolutely appropriate. It is unfair. We are making a massive wealth transfer from your generation to increasingly my generation. Poverty, because of good work of people like Senator Sanders, has dramatically decreased among seniors over the last 50 years because of commitments we have made. Poverty is at 9 percent. Unfortunately, poverty among children today is 24 percent. That is not a progressive system for our country, and I think this all-in-it-together concept is one that needs further exploration.

Thank you for the extra time, Mr. Chairman.

Chairman ENZI. Senator King.

Senator KING. Thank you, Mr. Chair, and thank you for calling what I think is a very important hearing on a topic which we need to discuss at further depth.

Tom Brokaw wrote a book a couple of years ago called "The Greatest Generation," and it was the generation of the Depression and World War II. And I want to take off on what you just said, Mr. Bartlett. That generation fought World War II, paid for World War II. If you look at the charts of debt, there is a great burst of debt right in the late 1940s, early 1950s. They paid it off. They built the Interstate Highway System. They taxed themselves to pay for it. They paid for the Korean War, as you pointed out. And now we cannot keep the potholes filled. They built the Interstate Highway System, and we cannot keep the potholes filled.

I think if Tom Brokaw wrote a book about our generation, it would be called "The Great Skedaddle" after the first Battle of Bull Run, where our generation has skedaddled from its responsibilities to pay its bills. It is pretty straightforward. And we talk about an unsustainable path. We have been on an unsustainable path for about 40 years. Sometime in the 1960s, we decided we did not have to pay our bills as a generation, and what we are doing is simply passing them on to our children.

I had a very formative experience with a hardware store clerk in Brunswick, Maine. When I asked him in 2003 or so, "What do you think of the Bush tax cuts?" he said, "There have not been any Bush tax cuts." I said, "Of course there have." He said, "No, there were no tax cuts." I said, "What do you mean there were no tax cuts? Don't you watch the news?" He said, "Listen, if you cut taxes when you are in a deficit situation and borrow to make up the difference, all you are really doing is shifting that tax to the next generation."

I thought that was a very interesting insight. Those kids are going to have to pay for that. Our children are going to have to pay for that.

Doctor, I understand you talk about debt and the fiscal difference. I call it "unfunded liabilities." You are putting together the unfunded liabilities of Social Security. I agree, that is an appropriate way to look at it.

We all agree around this table that we have got a problem. The question is: How do we deal with it? And do we start to deal with it in a serious way? And it seems to me there are only three ways to deal with it: one is revenues, two is cuts, and three is economic growth. And that is where Senator Sanders comes in, because I think inequality is costing us economic growth. You talked about one point of GDP. If 70 percent of the U.S. economy is driven by consumer spending and consumers, the vast middle class, do not have money to spend, by definition you are going to have slower economic growth. So inequality is an issue.

But we have got to look at all three, and we have also got to look at the demographics of where we are now as a society. We cannot, as Senator Warner said, we cannot support the commitments we have made to seniors given the retirements of the baby boomers at the current level of revenues unless we are just going to wipe everything else out.

And then the final point, I think, Mr. Chairman, that I know you are worried about is interest, and the point has been made several times here. Interest rates are going to kill us. We are in a fantasy land of interest rates right now, of 1.5 to 2 percent. Interest rates, as has been pointed out, go back to historical norms of 5 or 6 percent. That would virtually equal what we are now arguing about is the entire discretionary budget of the United States Government. And it is going to crowd out everything that both sides of the aisle value, whether it is battleships or Head Start slots or student loans.

And so we have really got to be thinking about that, and I think we have got to be thinking about—yes, we need to think about the unfunded liability. Let us put that aside for a minute and talk about the $18 trillion debt. And I think we have got to be thinking about how to bring that down. Yes, the deficit is lower. The deficit is lower. But it is still a deficit. We are still digging the hole deeper to the tune of half a trillion dollars a year.

You found a question in there. I compliment you.

Mr. KOTLIKOFF. Could I interject just a second here? I am trying to get across that we do not have a well-defined measure of the debt, so you guys keep talking—gentlemen and Senators keep talking about the deficit. The true deficit is $5 trillion between last year and this year, because the fiscal gap in the chart you will see went from $205 trillion to $210 trillion. So—

Senator KING. I understand that. I am trying to distinguish—you are lumping together what I call "unfunded liabilities" with the public debt.

Mr. KOTLIKOFF. Economic theory does not know what the public debt is. It is just a matter of word games. You guys are engaged in a word game and have been for decades. That is why—you know, again, my mom's Social Security check is a debt. It is not on the books.

Senator KING. I agree.

Mr. KOTLIKOFF. So what you call interest is a matter of your language. What you call the deficit this year is a matter of your language.

Senator Warner said that we can all choose our accounting method. Economists, 1,200 strong, 17 Nobel Prize winners, are saying you cannot all choose your accounting method. There is only one accounting method you can use. It is the infinite rise in the fiscal gap method, because that is what the theory says. That is the only method that is independent of your choice of words.

Senator Kaine along with Senator Thune have cosponsored the INFORM Act. Pass it. It requires you to do fiscal gap accounting, put everything on the books, and it does not undermine the investments that you need to make to improve in R&D and education that will cost money but also get back hopefully taxes which will exceed what it costs in present value. So it is a framework for capital budgeting as well.

Senator KING. I agree, and I agree we need to have the clearest picture we can have. I do not mean to imply that we do not. But the question still is: What do we do? And, Mr. Chair, I think we ought to have a capital budget. There are things we should be borrowing for. The problem is now we are borrowing to pay park rang-

ers, and that does not make sense. So that should be part of our discussion.

Senator KING. I agree.

Mr. KOTLIKOFF. And do not take my forcefulness as really fundamentally disagreeing with you or your values, because we agree 100 percent on those things.

Senator KING. Well, I just think we have got to do something about this, and we have got to do it in a comprehensive way, and we have got to start—every year we wait to do it, it is going to get harder. And, fundamentally, to me, it is our generation being unwilling to pay our own bills. And we are borrowing from our kids, and at some point they are not going to be able to carry this burden. And it also saps any flexibility we have to deal with a legitimate crisis.

Mr. KOTLIKOFF. Right.

Senator KING. If we are running huge deficits at a time of relative non-crisis and then when we have a legitimate crisis, we do not have any well to go to. So I commend all of you for bringing this to our attention. I do think it is something that we have to work on. But it is not going to be able to be solved painlessly on either.

Thank you, Mr. Chair.

Chairman ENZI. Senator Wyden.

Senator WYDEN. Thank you very much, Chairman Enzi and Senator Sanders. I think this has been an important hearing, and I wish I could have been here for more. But as you know, there are a few things going on at the Finance Committee right now that are time-sensitive.

I want to get into the question of health care costs for a moment. I understand there has been some discussion, but what is striking is some of the tangible progress that has been made in reducing the growth of health care costs. And I was particularly struck by the Congressional Budget Office analysis. That is a substantial bit of progress in terms of moderating health care costs. And having heard you on this subject before, Dr. Kotlikoff, I know you agree, and I am happy to have all of you here today.

What I wanted to get into is the question of dealing with the structural challenge in terms of health care, because I think it is well understood that 10,000 people are going to turn 65 every day for years and years to come. And, in effect, so much of the debate seems to be, well, for the structural challenge you really have two choices: you can cut people's benefits, or you can just kind of do business as usual. And I feel very strongly that there is a third path, that there is a path to better care and lower costs.

Senator Sanders, my colleague here, his House compatriot, Peter Welch, is part of a bipartisan effort with myself and Senator Isakson and Erik Paulsen to focus on the challenge that, frankly, both political parties have missed in the past, and that is chronic disease.

Medicare today is no longer primarily about broken ankles. You know, back when I was co-director of the Gray Panthers, that is what we often talked about. But there would not be any political debate today that Medicare was about broken ankles. Medicare today is about cancer, it is about diabetes, it is about heart disease,

it is about stroke. That consumes 90 percent of the Medicare budget, and yet my view is that both political parties have not adequately addressed this issue.

So perhaps we might start with you, Dr. Kotlikoff, but any of you who would like to get into this. It seems to me that the centerpiece of what is done particularly in Medicare is to refocus so as to put the primary attention of the program on those with chronic disease, those with very often multiple chronic conditions, who are the most costly individuals, and that will make sense for Medicare. As we get into the issues, as we have sought to do in this bipartisan bill, we must also consider the population that is under 65, because there will be a greater focus on prevention.

So let me just go right down the table roster and start with you, Dr. Kotlikoff, what you think of that analysis.

Mr. KOTLIKOFF. Well, I think that certainly the Government has a big role in research and development in the area of health care, and it may be that we are underfunding NIH in these areas and that we need to—

Senator WYDEN. I am talking about coordinating care. I mean, for example, the bulk of the program today, where there is not Medicare Advantage and, you know, fee-for-service medicine, you cannot get a collective payment if a doctor, a physician assistant, or maybe a pharmacist want to team up. And it just seems to me we have got to coordinate these services to get better care and lower costs.

Mr. KOTLIKOFF. Senator, my reform proposal—I wrote a book called "The Healthcare Fix"—is one of the purple plans, it is called "The Purple Health Plan." It has been endorsed by, I think, five Nobel Laureates. It is right there on the website, the purpleplans.org. It would say we should give everybody a voucher that is based on their pre-existing condition, whether they have cancer or diabetes, and that everybody would take that voucher to an insurance company to buy a single basic plan that would cover the things that were set by a panel that would be covered subject to a global budget so that the costs of all the vouchers would never exceed 10 percent of GDP.

Now, if you go to that kind of a system, you start giving the insurance companies—you make the basic health insurance plan a commodity, just like apples. And then you get them competing to provide that, and so they are going to go to the most efficient delivery system. So you are going to have Kaiser Permanente, for example, trying to figure out what is the most—how can we internally coordinate care for people with these chronic diseases so as to minimize costs? Because we are just getting their voucher—that is all it is—and we are not allowed to turn anybody down, but we are happy to have somebody who is diabetic because they are going to have a bigger voucher because they have—we are going to base it on medical records. There are electronic medical records proposed in this proposal. This is going to mean that they are going to come to us with a bigger voucher, so they are a good customer, too. And we solve—so we need to, I think, rely on the private sector to do this coordination of care, and they have to have the incentive. And the way to do that I think is to make the health insurance industry hyper-competitive and turn basic health insurance into a com-

modity, a simple commodity like apples. And beyond that, people could buy supplemental policies if they want to have insurance to get an angioplasty at 98, they would buy—

Senator WYDEN. Why don't we do this—because I am over my time. Let us go to Mr. Bartlett. I think we in the Congress have not had a very good history with vouchers or saying that health care is like apples, because it is a very different set of considerations. I think there ought to be a role for the private sector, but I think the idea of just handing somebody a voucher and saying health care is like an apple, that is not what our bipartisan group is all about. We are about choice, but not vouchers.

Mr. Bartlett?

Mr. BARTLETT. I am disinclined to think that getting the private sector more involved in health is going to help our problems because we are already spending something like $300 billion a year of unnecessary administrative overhead because of the complexity of our health system. And I think it is quite—the most relevant statistics that I am familiar with about health is the fact that the next country most like ourselves, the OECD, with the heaviest health spending spends half of GDP of what we spend. If we spent no more—we could have the health system that the British have—which is actually on balance a better system than we have. They have better health outcomes over a lifetime. We could have that, and if we spent the same amount they spend, which is a little over 10 percent of GDP, we would have the equivalent of the payroll tax to give away for nothing. All Americans would be better off by the amount of money they now pay for the payroll tax that they could spend on anything. Their standard of living would be massively higher, and their health would be no worse than it is in Britain, which is better than ours.

So I think we missed a chance in 2009 to examine foreign operations and see what we could have learned from their experience instead of just reinventing the wheel, as we always do.

Senator WYDEN. You are spot on, as you often are, on this question of driving down administrative costs. I mean, driving down administrative costs is the heart of this. And, of course, that is one of the most appealing features of Medicare, is that Medicare, of course, has done it. The question is: Can we now get Medicare to focus on the future, which is really chronic disease? And I know my time is up, and I thank you and look forward to working with you, Mr. Chairman, and Senator Sanders on these issues.

Mr. KOTLIKOFF. Senator Wyden, can I make a quick correction?

Chairman ENZI. We are running way behind.

Mr. KOTLIKOFF. Sorry.

Chairman ENZI. Senator Kaine has been here from the beginning, and as I understand it, he is the cosponsor of your plan.

Mr. KOTLIKOFF. Absolutely.

Senator KAINE. Indeed, I am a big supporter of the INFORM Act, a big supporter, and I appreciate the testimony of all of you.

I want to ask you each just one question, and it deals with the title of the hearing, "America's Dangerous Debt." How much debt is dangerous, is what I want you guys to tell me.

Here is my observation. I was a mayor, and I was a Governor, and we had a philosophy in my city hall and we had a philosophy

in my State for managing debt. And I have worked with some pretty dysfunctional folks, I do not mind telling you. My city council, five of my colleagues in 8 years were criminally prosecuted and four of them went to jail. Very dysfunctional, and very bipartisan, but we had a philosophy—

Senator SANDERS. The Democrats and Republicans going—

[Laughter.]

Senator KAINE. It was a bipartisan tradition. We had a philosophy about how to manage debt. It was, you know, debt service as a percentage of the city budget. We were always issuing debt and retiring debt, total outstanding debt, had some ratio relation to, you know, city assets.

At the State level, the same thing. I had two Republican Houses who fought with me on everything, but we had a bipartisan compromise whether the Democrats or Republicans were Governor, whether the Democrats or Republicans were in majority in the legislative branches, about a debt management philosophy. Debt service payment as a percentage of State outlays and total debt as a percentage of, in this case, State GDP.

The thing that surprised me here, coming here, is—I mean, I know, you know, the way you bring down debt is the three things that Senator King mentioned: more taxes or cut spending or grow. But there is no consensus here about what level of debt is appropriate. We are going to have debt. What level of debt is dangerous?

I tend to agree with Dr. Bartlett that nominal debt is irrelevant, just the number. We never used the number as the danger zone in city hall. We never used the number as the danger zone in a State budget. It was always a ratio. It was a ratio of total debt to assets or a ratio of debt service payments to total State budget.

So I am assuming that the measure of what is appropriate debt—and we are going to have appropriate debt—and what is dangerous debt is some ratio rather than just a finite number. And I just would like to ask each of you—I mean, I have been kind of trying to determine what your answers will be based on your testimony. But I would just like to ask each of you, forget about how we solve it, that is on us to do, but what would your professional advice be as to an appropriate Federal debt management metric? What should we, you know, paint as our bull's eye and try to manage to?

Mr. KOTLIKOFF. Senator, if you are asking me, the answer is that the fiscal gap has to be zero. It cannot be 10.5 percent of the present value of GDP. Another way of saying that is that it is 10.5 percent of GDP that we need additionally to collect, either in the form of lower spending or higher taxes through ever. So the fiscal gap has to be zero; otherwise, you have got an economy that is trying to consumer more than it actually has in resources in terms of labor and income coming into the future and also current net wealth. And our country is trying to consumer more than it can. You see this in the national saving rate diagram—

Senator KAINE. Can I—I mean, I hear your answer, and I want to make sure the other two answer within my time. But you would say forget debt, forget—

Mr. KOTLIKOFF. It is not a well-defined—

Senator KAINE. —debt service payment. You would say we should not even be having a hearing about dangerous debt; we should be having a hearing about the fiscal gap.

Mr. KOTLIKOFF. Because I have no idea, as an economic scientist, what the word "debt" means. It is not define.

Senator KAINE. All right. Let me go to you, ma'am.

Ms. PFITZENMAIER. Well, since I am not here as an economic scientist, I do not think I can really put a measure, but I think it is something that I am glad we are having this discussion about, because I think it can really affect the quality of life of all Americans, as I mentioned in my remarks.

Senator KAINE. Mr. Bartlett?

Mr. BARTLETT. Well, let me make a bit of a technical point, since I worked at the Treasury and I kind of think of debt in the way the Treasury thinks about it. I think the structure of the debt makes a huge difference. Whatever the amount is, I mean, we all know that we can adjust our backpacks in such a way to make the same weight more easily carryable. And, you know, looking at the debt right now, we are paying literally two basis points on Treasury bills, and 88 basis points on 3-year, 1.81 percent on 10-year, and 2.39 on 30-year. So a penny-wise, pound-foolish kind of approach to the debt would say, well, let us just sell everything in T-bills and, you know, not worry about the future. But it seems to me that if you take the attitude that interest rates eventually are going to rise to a more normal level, you know, years from now we may look back and say, God, we should have been selling every single bit of 30-year bonds at 2.39 that we possibly could. I mean, you are old enough to remember the era of double-digit Treasury interest rates, as I am, and I think that we—it might be in the interest of the Treasury to sell more long-term bonds now, even though it will in the short run add to the Treasury's interest cost, because down the road within that 30-year time period that those bonds are going to be out there, rates are undoubtedly going to be much higher, and we will come out ahead in the long run. And it would help to use Professor Kotlikoff's type of analysis where you are looking over the long term to make these kinds of judgments.

Senator KAINE. It is probably not a fair question to ask you without giving you the heads up, but the difference up here is not just because of partisanship. The difference is in the profession there is not an agreed-upon metric about debt.

Mr. KOTLIKOFF. Senator, there—

Senator KAINE. I mean, you say debt is a meaningless concept. You say nominal debt is—

Mr. KOTLIKOFF. No, no, Senator, can I—

Senator KAINE. So I just think that the—you know, we can talk about legislation to pass; we can talk about selling T-bills; we can talk about all kinds of things. But if we are having a hearing about what debt is dangerous and nobody has a metric by which to measure it—

Mr. KOTLIKOFF. No, Senator, let me just—

Senator KAINE. —that is one of the reasons why these discussions are so difficult.

Mr. KOTLIKOFF. Let me—

Senator KAINE. Thank you all—

Mr. KOTLIKOFF. Can I just interject on that point? The profession has been very clear—at theinformact.org—you cannot come up with 1,200 better economists, okay? These are all Ph.D.s from the top universities and other small places, but we have 17 Nobel Prize winners. There is no question in our math. There is no question among the economists as a profession what it is we need to measure. It is the fiscal gap.

It is true that Bruce Bartlett does not sign onto it, or Paul Krugman or Art Laffer. That does not mean that the profession is not clear as to what to do or that the math is not clear. It is absolutely clear.

Chairman ENZI. Thank you. And all of you can submit extra comments if you want to. I would like to thank all the witnesses for agreeing to testify this morning. We appreciate your time with us and your thoughts as we work on this critical issue. And we have asked that you be willing to answer any questions that come in writing. There are some people who were not able to be here, some that were here that were limited on the number of questions that they could ask. I had some more questions. So questions should be turned in for the record no later than 6:00 p.m. today to the Committee clerk in Dirksen 624, and we would hope that you would respond to any of those questions within 7 days.

Chairman ENZI. With no further business to come before the Committee, we stand adjourned.

[Whereupon, at 12:27 p.m., the Committee was adjourned.]

Responses to Questions for the Record

Submitted by Senator Mike Enzi

By Laurence Kotlikoff

March 9, 2015

**Question 1 -- Do the infinite horizon and CBO's measures of the fiscal gap make our country more vulnerable to fiscal crises? Do they increase the likelihood of fiscal dominance in monetary policy? How would a fiscal crisis affect the U.S. Economy?**

I have no idea what the CBO believes it is measuring when it comes to official debt projections. The Director and other economists at the CBO are sufficiently well trained or should be to understand that the official debt is a measure of nothing more than our word choice. Consequently, I can only say what any trained economist would say -- the CBO's debt projection tells us nothing about the economy.

The infinite horizon fiscal gap is, on the other hand, well defined. Its magnitude -- $210 trillion -- tells us the U.S. is broke, not down the road, but today. Once the financial markets understand the degree of our country's insolvency and put two and two together, namely that our government has been printing money like crazy to pay its bills, they will likely sell their long-term bonds, leading to major interest rate increases. This, in turn, will increase the velocity of money -- the speed at which money circulates in the economy. The result will be that the massive increase since 2007 in the amount of money will be accompanied by faster money, both of which will put upward pressure on prices. Sharp increases in interest rates due to actual or expected inflation can put the economy into recession. It can also trigger another financial crisis since banks continue to borrow short and invest long.

The insolvency of the country has already led to massive money creation -- roughly $4 trillion since 2007. Given the size of the fiscal gap, the Federal Reserve will be under ever greater pressure to print money to pay the government's bills.

**Question 2 -- Will rising fiscal gaps discourage investment and mean less output?**

Yes. As my testimony makes clear, the fiscal gap has been associated with an enormous redistribution from young savers to old spenders. The net national saving rate, which was roughly 15 percent in the 1950s now stands at roughly 4 percent. And since most of net domestic investment is financed by net national saving, the net

domestic investment rate has also dropped dramatically. It too was averaging 15 percent of so in the 1950s and is now down to roughly 4 percent. The redistribution has helped successive generations of older Americans consume at a higher rate. This is shown in the chart included in my written testimony of U.S. age-consumption profiles. The chart shows the massive increase in the relative consumption of the elderly through time. Closing the fiscal gap is a zero-sum game across generations. Hence, the longer we wait to close the gap, the more current older generations will be left off the hook in paying the government's bills. This will permit them to consume even more and further drive down our rates of national saving and investment. So leaving the fiscal gap to grow will, indeed, encourage consumption, disproportionally by the elderly and further lower our national saving, net domestic investment, GDP growth rate, and growth rate of real wages.

**Question 3 -- Will We Print Money to Close Our Fiscal Gap?**

Governments that can't pay their bills print money. Most of our fiscal gap reflects real spending commitments. So the U.S. government doesn't have that much wherewithal to use the printing press and its associated fallout, inflation, as a form of fiscal finance. Indeed, were we to inflate away the real value of the entire $13 trillion held by the public in official debt, we'd still face an enormous fiscal gap. But the fact that printing money isn't a real answer to our nation's fiscal insolvency won't prevent our government from trying to ease the fiscal pain by resorting to the printing press.

In fact, the Fed, which is part of our government, has spent the last eight years doing precisely this. To be precise, it has spent the last eight years printing over $3 trillion of new money according to the Monetary Base statistics reported by the St. Louis Fed. This has produced a five-fold increase in the size of the Monetary Base since 2007. If the M1 money multiplier (the ratio of the M1 money supply to the Monetary Base) and the velocity of money (the speed at which money circulates in the economy) had, today, the values that prevailed in 2007, prices would be almost five times higher than they were in 2007. They are now only 15 percent higher because the money multiplier and the velocity of money have plummeted. But there is nothing guaranteeing that the level of these variables don't revert to their 2007 values.

Some people think that because the price level hasn't risen by much that the government hasn't been printing money to pay its bills. Not true. When the Treasury borrows $3 trillion to cover its expenditures and the Fed buys the $3 trillion in bonds back from the public, this is no different from the government (the Treasury and the Fed taken together) having simply printed $3 trillion to cover its expenditures. Yes, the Fed formally holds the Treasury Bonds. But the Treasury's payments on the bonds are

handed back to the Treasury as Fed profits. So this is just camouflaging the fact that Uncle Sam is printing money to pay for his spending.

So the fact that M1 hasn't risen in proportion to the Monetary Base or that money's velocity has slowed and that prices haven't risen as rapidly as as M1 doesn't alter the fact that Uncle Sam has been engaged in Monetary Finance. If the government prints money and uses it to buy, say, chickens, that's fewer chickens available for the private sector to eat. Or it it prints money and gives it to person X who then buys more chickens, that's fewer chickens for everyone else to eat. What happens to the price level in this process is important and can, in fact, influence the government's fiscal position. But that reaction of the price level to the greater supply of Base money is secondary or endogenous to the use of the printing press to feed chickens to the government or to feed chickens to whomever the governments wants to provide dinner.

Other people think that the fact that the banking system has held much of the increase in the Monetary Base in the form of excess reserves means the government hasn't been engaged in monetary finance. Not the case. What the private sector does with additional money that it receives for its chickens doesn't alter the fact that Uncle Sam or his special friends are eating the chickens. Nor does the Fed's paying interest on excess reserves change the fact that the government is funding its real expenditures by printing money. Indeed, the payment of interest on excess reserves, to the extent that it is financed by more money printing, is just another case of the Fed helping its friends, in this case the banks, eat more chickens.

Some people look at the excess reserves as a form of borrowing by the Fed, which is used to buy assets. I.e., they view the Base Money that's held as excess reserves not as monetary finance, but simply as hedged operation in which the Fed borrows and then lends. To see why this view is off base, consider this scenario. A) The Treasury borrows $3 trillion and buys chickens for the military, most of which they freeze. B) The Fed buys up $3 trillion in Treasury bonds. C) The private sector holds the extra $3 trillion as currency. Now suppose the private sector is thinking of depositing the extra $3 trillion in the banks and the Fed prevents this by paying those holding the $3 trillion an amount, which they call interest, to keep the money in their pockets. At this point, Uncle Sam has the chickens, the private sector has extra cash, and the Fed is trying to influence what the private sector does with its money. If the Fed offers to pay banks interest on their excess reserves and the private sector deposits the $3 trillion in the banks, the Fed's balance sheet won't change. It will still carry the $3 trillion of newly created Base Money as a liability whether that Base Money is being held at the Fed as bank reserves or held by the public as cash in their pockets. Yes, when it's held as bank reserves rather than currency it has more of the appearance of a form of borrowing by the Fed. But if the banks withdraw their reserves the Fed doesn't have to do anything and hand them all to the public to hold in their pockets, the Fed doesn't

have to do anything. In particular, it doesn't have to hand over any chickens to the banks.

In sum, the fact that the Monetary Base appears on the Fed's balance sheet as a liability is fallacious accounting. It's been designed by clever accountants to suggest that the government is not simply printing its revenues, which it does and is. The right accounting for the Fed and Treasury is combined government accounting and the right combined government accounting is infinite horizon fiscal gap accounting. Under fiscal gap accounting the present value of future increases in the Monetary Base would show up as an asset as would the present value of future taxes.

Responses to Questions for the Record

Submitted by Senator Ron Johnson

By Laurence Kotlikoff

March 9, 2015

**Question 1: Will continued progress on lowering the growth in healthcare spending improve our country's massive fiscal problem.**

Absolutely.

The CBO took account of the recent slower growth in Medicare and Medicare expenditures in projecting those programs' future outlays. The fiscal gap, even with this improved outlook for health spending, is enormous.

Moreover, the recent progress in restraining Medicare and Medicaid spending growth may not continue. And expenditures on Obamacare and well as tax expenditures on employer-based health insurance can grow much more rapidly than is now assumed.

What's really needed to to keep all federal spending on healthcare fixed relative to GDP is the Purple Health Plan (see www.thepurpleplans.org). This plan provides for *full* payment of the premiums of all Americans for a basic health insurance plan that provides the same coverage to all Americans. The payment would come in the form of a voucher, but it would be a voucher that pays the entire cost of the basic insurance plan. Those who could afford it would be able to buy supplemental insurance to cover health risks not covered by the basic insurance plan.

**Question 2. Does focusing on the high cost of the most costly individuals make sense?**

Yes, but this will happen best under the Purple Health Plan. Under the Purple Health Plan I envision all Americans signing up with an HMO that would coordinate their service and cut the fat very deeply.

Responses to Questions for the Record

Submitted by Senator Kelly Ayotte

By Laurence Kotlikoff

March 9, 2015

**Question 1: Should we transfer money from the OASI fund to the DI fund?**

Social Security is 33 percent under-financed according to table Vi.F1 of the 2014 Social Security Trustees Report.

Please see http://www.ssa.gov/oact/tr/2014/VI_F_infinite.html. Social Security's present value fiscal gap equals $25 trillion. The 33 percent underfunding means that the OASDI system needs a 33 percent higher path of revenues starting immediately to cover projected benefits obligations. Transferring assets from one fund to another will do nothing to reduce the fiscal gap. Consequently, its use to avoid taking meaningful steps to address Social Security's financial insolvency will simply make the insolvency worse and harder to handle. Having Congress move money from the OASI fund to the DI fund is akin to a household borrowing on one credit card to pay off another. Social Security's financial crisis is not in the future. It's here and now. Major, not cosmetic surgery, as outlined at www.thepurpleplans.org, is the only way to go.

**Question 2: Is debt sustainable as long as deficits are below 3 percent of GDP?**

In my testimony I pointed out that the debt and its change over time, the deficit, are not well defined economic measures. Instead, they reflect the economically arbitrary choice of how to label government receipts and payments. Consequently, I honestly don't understand the question. The infinite horizon fiscal gap is the only label-free, economically meaningful measure of our country's fiscal position. Its use has been endorsed by over 1,200 economists, including 17 Nobel Laureates in Economics as you can see at www.theinformact.org. The increase in the fiscal gap from one year to the next is the *only* true measure of the deficit. That increase was $5 trillion between the end of 2013 and the end of 2014.

Responses to Questions for the Record

Submitted by Senator Ron Johnson

By Laurence Kotlikoff

March 9, 2015

**Question 1 -- Does the Public Understand that Social Security's Is Insolvent?**

No, the public doesn't understand. They haven't been told about table VI.F1 in the Trustees Report, which has been intentionally buried in an act of utter fiduciary malfeasance. It's not even clear whether the Trustees have even looked at this table, which was generated by the Office of the Actuary. Were they to do so, they'd learn that the system needs a 33 percent immediate and permanently payroll tax hike to pay its projected benefits. I.e., the system is 33 percent underfinanced. The trustees' benign summary of the system's financial status in the 2014 Trustees Report is focused exclusively on the 75-year fiscal gap, which no well trained economist would view as a measure of anything economic due to economics' labeling problem.

**Question 2 -- Will Delay in Fixing Social Security's Infinite Horizon Fiscal Gap Necessitate Massive Benefit Cuts**

Absolutely. The benefit cuts needed to eliminate the system's fiscal gap starting today, let alone down the road, are over 20 percent. Waiting to address the system's insolvency will make the request benefit cut or tax hike or combination that much worse.

**Heather Pfitzenmaier**
**Question for the Record**
**Before the Senate Budget Committee**
**March 4, 2015**

**Question from Senator Enzi**
As you travel around the country speaking to young people, what do they tell you about their views on whether they'll receive Social Security and Medicare benefits when they retire, and how do they speak about "debt" in relation to the federal government?

**Response for the Record**
When I travel around the country, I frequently hear concerns from young people about their futures. With respect to Social Security, many young people do not feel they will receive any Social Security benefits at all. From what they understand and perceive, young people believe this program is bankrupt and do not foresee Congress reforming and saving this program so it will be available when they retire. I hear less often about their views on Medicare, though frequently hear similar sentiments regarding whether the benefits will exist when they retire, and if so, what they would look like.

When young people speak about debt in relation to the federal government, they are frustrated. Young people feel they are paying into programs that they will receive few if any benefits from. Many have only voted once or twice, if that, and do not understand the decisions the federal government has made prioritizing programs and spending, especially when they are going to feel the impacts of these decisions.

**Bruce Bartlett**
**Responses to Questions for the Record**
**Submitted by Senator Mike Enzi**
**March 16, 2015**

**Question – You argued in your testimony that the federal government has never defaulted on its debt. While this is generally true, the U.S. Treasury experienced a bond default in the spring of 1979 that lasted about three weeks. In addition to this explicit default, the value of Treasury notes and bonds has been degraded many times though inflation and currency valuation changes. Given this historical record, please provide data supporting your argument that the Unites States has never failed to perform under its debt instrument contracts.**

In my testimony, I don't believe I said that the federal government has never defaulted on its debt, only that there is no reason in principle why it would ever need to, absent a technical problem with the debt limit. I was trying to make the point that there is no economic problem with servicing the debt as long as it remains denominated in U.S. dollars, but of course there may be technical or legal problems.

Since you mention the 1979 episode in which the Treasury technically defaulted due to some problems printing checks for interest, I would note that a study of this event showed a long-term increase in Treasury borrowing costs. [Terry L. Zivney and Richard D. Marcus, "The Day the United States Defaulted on Treasury Bills," *Financial Review*, 24:3 (August 1989): 475-89.] I hope you will keep this fact in mind when it again becomes time to raise the debt limit and Congress again waits until the last possible moment to act, with many members of Congress saying they don't care – and even welcome – a debt default.

Regarding your point about inflation constituting a de facto default, this view is not generally held since at least the 1930s when, in the gold clause cases, the Supreme Court ruled that as long as the debt is repaid in current dollars then the legal requirement is met.

I would point out, further, that an investor looking to lock in a real return need only buy Treasury Inflation Protected Securities. You will note that the interest rates on these securities are well below those on regular Treasury securities that are not indexed to inflation. The difference is, in effect, compensation to the lender for the risk of inflation.

**Bruce Bartlett**
**Responses to Questions for the Record**
**Submitted by Senator Ron Johnson**
**March 16, 2015**

**Question 1 – You testified that while future taxpayers will inherit federal debt obligations, they will inherit federal assets as well. Regarding a specific set of federal assets, are the Treasury securities that constitute the holdings of the Social Security and Medicare trust funds assets of the government as a whole that can be drawn down in the future to fund benefits?**

The securities held in trust are best thought of as de facto authority for the Treasury to use general revenues to pay Social Security and other benefits. They are neither a liability nor an asset. In principle, Congress could simply create out of nothing $100 trillion of Treasury securities and place them in the Social Security trust fund and it would have no economic effect whatsoever. It would simply extend the Treasury's ability to use general revenues to cover any shortfall between current payroll tax revenues and current Social Security benefits, in the event that the trust fund is exhausted before Congress acts in some other way to raise the payroll tax or reduce benefits in some way.

In other words, there is an essential difference between marketable Treasury securities and those that are nonmarketable, such as those in various trust funds. This is important not only for determining the burden of the debt, but also for legal reasons. It is sometimes suggested that even if the debt limit is not raised that the Treasury could still pay Social Security benefits by selling bonds in the trust fund. But Treasury cannot do this, legally. In practice, Treasury can only redeem bonds in the trust funds with its own cash, which it may lack in the event that the debt limits is not raised in a timely manner. I believe the Treasury is on record as saying that if it lacks the cash to pay Social Security benefits the day they are due, it cannot use trust fund securities to get around this constraint.

**Question 2 – You testified that "the principal cause" of our debt problem "is unfunded wars, not benefits." You also testified that "the wars in Iraq, Afghanistan and other post-9/11 conflicts have added $1.6 trillion to the national debt." Gross federal debt has increased between the end of FY2001 and FY2014 by about $12 trillion. In what way can a cost of $1.6 trillion, about 13% of that increase in debt, be considered the "principal cause" of the increase?**

I was referring to wars in general, not specifically to the wars in Iraq and Afghanistan. As I said in my written statement: "One can easily argue that the national debt is simply the cost of past

wars adjusted for the associated interest expense plus postwar costs such as for veterans' benefits."

In other words, we are still paying for the costs of World War II, the Korean War, Vietnam War and other wars because we never paid off the debts that were created during those wars and therefore continue to pay interest on the bonds that were sold to redeem the bonds issued during the wars, and because we are still paying veterans' benefits to those who served in those wars and will continue doing so for many years into the future.

**Bruce Bartlett**
**Responses to Questions for the Record**
**Submitted by Senator Ron Wyden**
**March 16, 2015**

**Question 1 – An Institute of Medicine (IOM) study estimates 30 cents out of every health care dollar spent pays for ineffective or redundant health care. The inefficiencies that lead to this unnecessary spending often centers on individuals with chronic diseases. Chronic disease patients often do not receive care consistent with recommended standards; in part due to lack of care coordination amongst the providers caring for them. This can lead to increased visits to emergency departments, rather than receiving care in the appropriate setting of a doctor's office, resulting in a higher cost of care.**

**Over the past several years, we have made great progress in reining in the growth of health care costs. Specifically, Medicare spending growth remains low at 3.1%, much smaller than the previous 10 year average of 7%. CBO has acknowledged our progress. CBO estimates made in 2010 of projected Medicare spending in 2020 have fallen by 14%, or $122 billion - all because we've slowed the growth of health care costs. This has had an indisputable benefit on our budget. We need to double down on this progress and focus on where the money is – the chronically ill. On average, Medicare spends just under $10,000 per beneficiary; however, for beneficiaries with six or more chronic conditions spending per beneficiary triples.**

**Do you agree that continued progress on lowering the growth of health care spending will reduce our deficits and ultimately our national debt? Do you agree that focusing our efforts on the most costly individuals, those with chronic diseases, is the area we need to focus on?**

I'm afraid that your questions are outside my area of expertise.

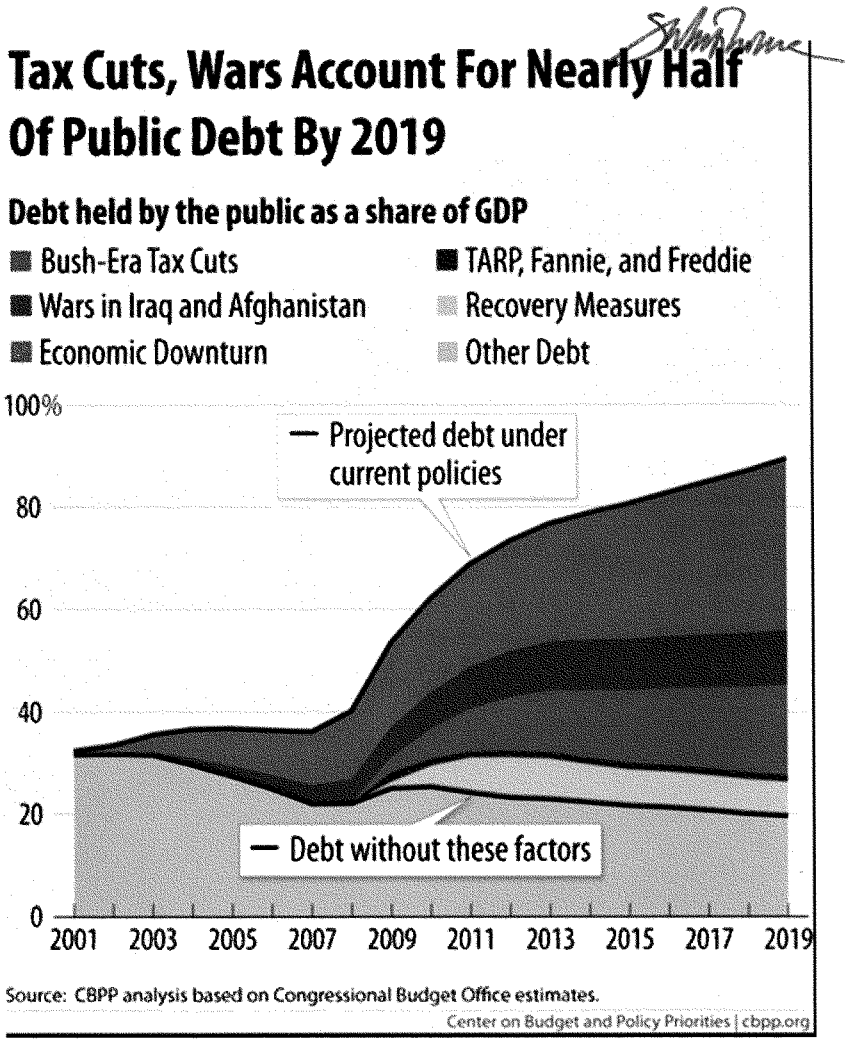
**Question 2 – Our health care system has flaws and obstacles in delivering high quality and efficient care. These shortcomings are exacerbated for the sickest patients because they interact with the health care system so much more than healthy patients. Specifically, these obstacles include navigating a health care system independently, without guidance. This encourages the utilization of medical services despite the quality of care delivered to the patient.**

**This year marks the 50th Anniversary of Medicare and Medicaid. As Congress celebrates this important anniversary, it is important to look at how they can be improved.**

**Historically, Medicare has paid providers for the number of services they preform rather than the quality of the services they provide. Speaking as economists, what type of incentives does this create?**

**In recent years, we've pushed Medicare to start paying for services based on value – linking payment directly to the quality of services delivered and the health of actual patient. Again, speaking as economists, what type of incentives does this create? Do you agree that our health care system needs to encourage the types of incentives that are created by rewarding value and not volume?**

I'm afraid that your questions are outside my area of expertise.


Tax Cuts, Wars Account For Nearly Half Of Public Debt By 2019
Debt held by the public as a share of GDP
Bush-Era Tax Cuts
TARP, Fannie, and Freddie
Wars in Iraq and Afghanistan
Recovery Measures
Economic Downturn
Other Debt
100%
80
60
40
20
0
Projected debt under current policies
Debt without these factors
2001
2003
2005
2007
2009
2011
2013
2015
2017
2019
Source: CBPP analysis based on Congressional Budget Office estimates.
Center on Budget and Policy Priorities | cbpp.org

# WASTEFUL DUPLICATION IN THE FEDERAL GOVERNMENT

**WEDNESDAY, MARCH 4, 2015**

UNITED STATES SENATE,
COMMITTEE ON THE BUDGET,
*Washington, D.C.*

The Committee met, pursuant to notice, at 10:30 a.m., in Room SD–608, Dirksen Senate Office Building, Hon. Michael B. Enzi, Chairman of the Committee, presiding.

Present: Senators Enzi, Sessions, Johnson, Ayotte, Corker, Perdue, Sanders, Warner, Kaine, and King.

Staff Present: Eric Ueland, Republican Staff Director; and Warren Gunnels, Minority Staff Director.

## OPENING STATEMENT OF CHAIRMAN ENZI

Chairman ENZI. Good morning, and welcome to everyone that is here. I will call this hearing to order.

This should be one of our more bipartisan hearings during the year. We have all had some involvement in causing the problem. I have been looking at this for a long time, and it appears as though everybody comes up with an idea for a project, and the easiest way to pass it is to call it a demonstration project and to have it instituted in five places across the country and, you know, to see if it will work and to see if it is so spectacular that the local communities will take it over. So far every one of them has been spectacular, and so far the local communities have not taken it over. But since it was so spectacular, we nationalize it and do it for everybody, and that involves a lot of employees, too. So anytime that there is duplication and we are interested in ending the program, the employees fight for their job and send us the examples of the 20 people across the country that absolutely were helped, and we reinstitute the program.

So what Government does too little of is to make any credible attempt to ensure that taxpayers are getting the best deal for their money. It spends too little time guaranteeing that the taxes they send to Washington are spent in the best and most efficient way. We spend too little time ensuring that when duplication is discovered, it is addressed. That is why I called this hearing today. One of the ways our chronic overspending problem could be improved is with a commitment to rooting out the needless duplicative spending in our Government.

We will hear this morning from the head of the Government Accountability Office. The GAO has outlined tens of billions of dollars in savings that can be achieved through various efficiency meas-

ures. Ensuring that spending programs do not duplicate each other protects the taxpayer; as well, reforming and consolidating programs can ensure that they focus on the real needs and be managed with an eye on real results.

The Federal Government has grown so large and complex that no one seems to know how many Federal programs exist. Even the executive branch cannot tell how many programs it administers. I am not kidding. Let me explain.

Several years ago, Congress passed a law requiring the administration to publish a list of all Federal programs on a central governmentwide website, along with related budget and performance information. Unfortunately, when the program lists were put online, GAO reviewed the information and discovered that the inventory, in their words, was "not a useful tool for decisionmaking."

Why was that? Well, each Federal agency uses a different definition of what constitutes a "program" in making its contribution to the inventory. GAO reported that because agencies used different approaches, similar programs across agencies would not be identifiable. So we do not know how many Federal programs there are. But even if the Government cannot answer that question, we can find strong evidence that the number is on the rise.

One way to assess program proliferation is through the Catalog of Federal Domestic Assistance, CFDA, a governmentwide compendium of Federal programs that provide assistance or benefits to the American public. We have a slide that shows how the number of programs in the catalog have grown over time.

In 1967, when the CFDA was first published, it contained 459 programs. What our chart shows is that the list grew to 1,390 by 1995; and by 2005, it had increased to 1,580; and today there are 2,292 programs outlined in the CFDA. That is a five-fold increase in the past half-century.

But this snapshot of numerous programs is just the beginning of the problem. The CFDA uses a narrow definition of "program" that excludes many activities and initiatives not specifically designated in law. This is important because now in this administration, new initiatives are spawned internally by Federal agencies and have been by other administrations, too. So not only are we spending much more money, not only are the number of programs that we directly appropriate for growing, now the executive branch is busy creating all sorts of new programs on their own through an increasingly byzantine web.

It stands to reason that as Federal spending and the number of Federal programs grow, both overlap and duplication become harder to avoid. Fortunately, Congress has required GAO to investigate and report on duplicative programs. Pursuant to law, GAO has published a series of four annual reports chronicling the spending with duplicative goals and activities both within agencies and across the Government.

The extent of spending program duplication is staggering. Take a look again at the video screens, colleagues. What has GAO found so far? Among their discoveries, GAO has outlined 209 STEM education programs across 13 Federal agencies. This number was reduced to 158 after GAO's initial findings were released.

GAO has also found nearly 700 renewable energy initiatives being administered by 23 agencies and their 130 sub-agencies.

GAO in these reports also identifies opportunities for agencies or Congress to reduce, eliminate, or better manage fragmentation, overlap, or duplication, and achieve cost savings. Such savings would benefit our constituents.

So what have we done with all of GAO's good work? GAO has maintained a running tally of its recommendations and how many have been addressed. So far it has made 440 separate recommendations, but, unfortunately, fewer than one-third of their recommendations have been fully implemented by Congress and the executive branch. That is highly disappointing. It is long past time to take these recommendations on spending seriously. Taking GAO's advice, we can begin almost anywhere, but regardless, we ought to begin.

For example, by using strategic sourcing, we can reduce duplicative IT investments by Federal agencies. The Federal Government spends about $80 billion annually on purchasing and upgrading software and hardware, so trimming even a few percent off of the cost would yield billions in savings. And by consolidating Federal data centers, we can save $3 billion over 10 years.

Fortunately, there is the possibility of progress this Congress. Our committees in the House and Senate should be empowered to focus on consolidating duplicative programs, and our budget should facilitate that.

As well, our colleague Senator Ayotte deserves support from this Committee for her Duplication Elimination Act that she introduced with Senator Joe Manchin, and Senator Warner and Senator Ayotte should be congratulated for the work that they have done on Government Performance and Results. That was in effect in 1987 when I came, and I spent a lot of time looking at that. It was not enforced, and hopefully the new initiative will be. That Duplication Elimination Act is designed to ensure implementation of the recommendations in GAO's annual duplication reports. I think Members of Congress share considerable common ground in wanting to ensure that we and the executive branch do a better job addressing spending duplication. And it is my hope that Congress will take strong action this year on the problem. We have gone too long in Washington letting things continue as they are. I guess one of the things we will have to do is craft a definition of "program" so that they know what we are talking about.

So in light of the chronic overspending and dangerous debt, we should act to consolidate duplicative spending programs that sprawl too far across our Government and in so doing save taxpayers billions of dollars.

Senator SANDERS.

## OPENING STATEMENT OF SENATOR SANDERS

Senator SANDERS. Mr. Chairman, thank you. And, Mr. Dodaro, thank you very much for being with us.

I think, Mr. Chairman, that on a lot of issues there will be strong philosophical and ideological differences, but I suspect on this issue you are right, there should be a nonpartisan approach. I am not

sure that anybody, no matter what their political views may be, should be tolerant of waste or fraud or duplicative services.

As you know, every year, as you have indicated, since 2001, the GAO has issued a report on opportunities to reduce fragmentation, overlap, and duplication, and achieve other financial benefits, and this time they have found 188 areas where Federal agencies and Congress can take action to improve Federal programs. The administration and Congress have worked together to address GAO's concerns by finding ways to reduce fragmentation and overlap through better data systems and to improve the management of Federal programs. Clearly, every branch of Government can and must be more efficient and effective, and we all have a responsibility to reduce waste in every branch of Government.

Let me use this opportunity to make three points.

As Willie Sutton famously indicated, he robs bank because that is where the money is. Well, we could go on for hours talking about waste and fraud in all kinds of Government agencies, but the truth is when we speak about discretionary spending, the money is in the Defense Department. That is more than half of our discretionary spending, and I think it is appropriate—and the GAO has taken a hard look at defense spending. Not to say that that is the only agency, but that is where a lot of money is.

At a time when the U.S. spends more on the Pentagon than the next nine countries combined, and when over half of our discretionary spending goes to the Pentagon, we have got to pay close attention to this issue.

Mr. Chairman, GAO has identified over 100 needed reforms at the Defense Department to increase efficiency and reduce waste. But, sadly, only one-third of these proposed reforms have been implemented to date.

Further, every two years, at the beginning of the new Congress, GAO produces a list of agencies and programs that are at high risk of waste, fraud, and abuse. Since GAO began this exercise in 1990, the Pentagon has made the list each and every time.

In addition, GAO has found that almost one-third of the Department of Defense's $1.5 trillion acquisition portfolio—now we are talking about real money here, $1.5 trillion—is attributable to cost overruns. That is cost growth above and beyond what was originally estimated by defense contractors.

So I think when we talk about waste, this is clearly an issue which should be at the top of our list. How does it happen that almost a third of the Department of Defense's $1.5 trillion acquisition portfolio, or $448 billion, is attributable to cost overruns? That is real money.

In my view, these cost overruns are a prime example of wasteful spending that only benefits the bottom lines of some of the largest defense contractors in this country. Many of these defense contractors have paid billions of dollars in fines and settlements for misconduct and fraud over the past two decades while raking in hundreds of billions of dollars in Government contracts over the same period. Just a few examples:

Since 1995, Lockheed Martin has been fined over $600 million for misconduct. Northrop Grumman has been fined more than $850 million for misconduct. And Raytheon has been fined more than

$479 million for misconduct. This is an issue that needs serious discussion.

With respect to financial management, according to GAO, the Pentagon's inability to manage its finances affects its "ability to control costs, ensure basic accountability, anticipate future costs and claims on the budget, measure performance, prevent and detect fraud, waste, and abuse, and address pressing management issues."

Mr. Chairman, this situation has become so absurd—and now we are talking about the largest discretionary fund in the Government. The situation has become so absurd that the Pentagon is unable to even account for how it spends its money. Now, we can argue about whether you need this weapons system or that weapons system or the size of the Pentagon. But I would hope there is no disagreement that at least we should have an understanding of how the Pentagon spends its money.

Time and time again, the GAO has said that it is simply unable to audit the Pentagon. In fact, the GAO has reported that it has been unable to conduct a review of the Pentagon's financial records due to, and I quote, "serious financial management problems at the Department of Defense that made its financial statements unauditable." And this is clearly an issue that we have got to address.

So the first point that I want to make—and I will wrap up in a second here—is that we can talk about a lot of things, and we should talk about a lot of things. And I do not think you and I will have much disagreement on that. But I do think we should go where the money is and take a hard look at an agency which is unable to even audit itself and give us the kind of information that elected officials deserve.

The second point that I would make is that when we look at wasteful spending, wasteful spending is not only what we spend, it is what we do not collect. And as I have said previously, I believe that Members of Congress should take a hard look and ask questions why from 2008 to 2013 companies like General Electric paid not a penny in Federal income taxes and, in fact, received significant rebates. We are talking about GE, Verizon, Citigroup, JPMorgan, and other large corporations. So it is not only wasteful spending, but the absurdity that a truck driver is paying his taxes and some of the largest corporations in America are not.

So, with that, Mr. Chairman, I look forward to hearing the testimony of the GAO, and thank you for holding this hearing.

Chairman ENZI. Thank you for your comments.

One of my irritations is that IRS agents have not been paying their taxes and have been getting bonuses besides. So I appreciate your comments.

Senator SANDERS. Well, let me pick up on that just briefly. That is true. But the other thing, what we know is when you invest in the IRS—and they can do the audits—we bring in significant amounts of money for every dollar we spend in funding the IRS.

Chairman ENZI. Okay. Our witness this morning is Gene Dodaro, the head of the Government Accountability Office. Mr. Dodaro testifies frequently before Congress, but, frankly, I think we should have him appear more often before this particular Committee. GAO

has done great work over the years in identifying waste, fraud, and abuse in Federal spending. We need to wield their work as a tool as we fashion the Federal budget. The GAO is the auditor of the Federal Government, and we should use the work of our auditor to inform our budgeting. As Chairman then, I look forward to this Committee having a productive relationship with Mr. Dodaro and GAO.

Mr. Dodaro is the eighth Comptroller General of the United States. He was confirmed in December of 2010 after serving as Acting Comptroller General since March of 2008. He has been with the GAO for more than 40 years. He served 9 years as the Chief Operating Officer, the number two leadership position at the agency. Prior to that, he headed GAO's Accounting and Information Management Division, which specialized in financial management, computer technology, and budget issues.

For the information of colleagues, he will take about 5 minutes for his opening statement, followed by questions, and we do have a vote at 11:30 today.

Mr. Dodaro?

**STATEMENT OF THE HONORABLE GENE L. DODARO, COMPTROLLER GENERAL OF THE UNITED STATES, U.S. GOVERNMENT ACCOUNTABILITY OFFICE**

Mr. DODARO. Thank you very much, Mr. Chairman. Good morning to you, Ranking Member Senator Sanders, members of the Committee. I am very pleased to be here today to talk about GAO's work for improving the efficiency and effectiveness of the Federal Government.

As the Chairman mentioned, in the last 4 years we have made over 440 recommendations in 180 areas across Government to address fragmentation, overlap, and duplication, as well as outlining areas for cost savings and, as Senator Sanders mentioned, revenue collection as well.

So far, as of November last year, 29 percent of the recommendations have been fully addressed, 44 percent have been partially addressed, and 23 percent have not been addressed at all, either by the executive branch or the Congress, and we have a scorecard on both the executive branch and Congress in terms of the actions taken on our recommendations.

As a result of actions taken to date, I would note that $20 billion has already been saved and about another $80 billion will be saved in future years. However, much remains on the table, and a number of the issues and recommendations we have mentioned and much money remains to be saved by acting on our additional recommendations. The recommendations span the entire Federal Government from defense to health care. They include better management of leveraging the Government's purchasing power by using strategic sourcing objectives; eliminating wasteful information technology acquisitions and operations; and also we have recommendations to stem the tide of tax fraud through identity theft and to increase collections for the Government.

Now, one area in particular that I wanted to point out this morning is also the issue concerning improper payments in the Federal Government. These are payments that should not have been made

at all or were in incorrect amounts. Last year, for 2014, the executive branch estimated the amount of improper payments as $124 billion. That is about a $19 billion increase from 2013. This is a significant problem that needs to be addressed. There are over 100 Federal programs with improper payments across the Government, so it is not an isolated program. There are three programs in particular, though, that account for 75 percent or more of the total $124 billion: Medicare, about $60 billion in overpayments last year; Medicaid, $17 billion in improper payments; and the earned income tax credit at IRS, another $17 billion.

We have many recommendations to help improve this situation in these cases. I am very concerned about this improper payment issue because the highest programs with improper payments are also the fastest growing payments in the Federal Government. I have said for the past couple years I think unless we get on top of this problem and the executive branch improves their efforts, this problem is going to get worse before it gets better over time. So we have a lot of recommendations in this area as well.

Congress has passed legislation in this area, three bills in the last 10 or 12 years, increasingly requiring better reporting, better estimating. I would make the point that even the $124 billion is not yet a complete estimate. For example, estimates are not being made yet in the Temporary Assistance for Needy Families program because HHS says it needs additional statutory authority to collect the information from the States.

So I am very pleased—Mr. Chairman, you mentioned having a productive relationship with GAO. I look forward to appearing before this Committee as often as you would like and to have our work support this Committee as it takes its important responsibilities of preparing a budget resolution and guiding the fiscal path of our Federal Government in the future.

So thank you again for the opportunity to be here this morning, and I would be happy to answer questions.

[The prepared statement of Mr. Dodaro follows:]

United States Government Accountability Office

Testimony
Before the Committee on the Budget,
U.S. Senate

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# GOVERNMENT EFFICIENCY AND EFFECTIVENESS

## Opportunities to Reduce Fragmentation, Overlap, Duplication, and Improper Payments and Achieve Other Financial Benefits

Statement of Gene L. Dodaro
Comptroller General of the United States

GAO-15-440T

# GAO Highlights

Highlights of GAO-15-440T, a testimony before the Committee on the Budget, U.S. Senate

March 4, 2015

# GOVERNMENT EFFICIENCY AND EFFECTIVENESS

## Opportunities to Reduce Fragmentation, Overlap, Duplication, and Improper Payments and Achieve Other Financial Benefits

### Why GAO Did This Study

As the fiscal pressures facing the government continue, so too does the need for executive branch agencies and Congress to improve the efficiency and effectiveness of government programs and activities. Such opportunities exist throughout the government. GAO reports annually to Congress on federal programs, agencies, offices, and initiatives (both within departments and government-wide) that are fragmented, overlapping, or duplicative as well as opportunities for cost savings or enhanced revenues. One area that GAO has highlighted as offering the potential for significant cost savings is improper payments, which are payments that should not have been made or were made in the incorrect amount.

This statement discusses the status of (1) actions taken and remaining opportunities to address fragmentation, overlap, and duplication issues, and achieve other financial benefits as identified in GAO's 2011-2014 annual reports; and (2) efforts to address government-wide improper payment issues. GAO reviewed and updated prior work and recommendations on issues of fragmentation, overlap, duplication, cost savings, and improper payments. GAO also reviewed reports of inspectors general and agency financial reports.

View GAO-15-440T. For more information, contact Orice Williams Brown or A. Nicole Clowers at (202) 512-8678 or Beryl H. Davis at (202) 512-2623.

### What GAO Found

The executive branch and Congress have made progress in addressing the approximately 440 actions across 180 areas that GAO identified in its past annual reports. These issues span the range of government services and programs, from the Medicare and Medicaid programs to transportation programs to weapon systems acquisitions. As of November 19, 2014, 29 percent of these actions were addressed, 44 percent were partially addressed, and 22 percent were not addressed. Executive branch and congressional efforts to address these actions over the past 4 years resulted in over $20 billion in financial benefits, with about $80 billion more in financial benefits anticipated in future years. Although progress has been made, fully addressing all the remaining actions identified in GAO's annual reports could lead to tens of billions of dollars of additional savings, with significant opportunities for improved efficiencies, cost savings, or revenue enhancements in the areas of defense, information technology, education and training, health care, energy, and tax enforcement. Sustained leadership by Congress and the executive branch is necessary to achieve this goal.

**Table: Status of Actions Directed to Congress and the Executive Branch from GAO's 2011–2014 Annual Reports, as of November 19, 2014**

| Status | Number of executive branch actions (percentage) | Number of congressional actions (percentage) | Total (percentage) |
|---|---|---|---|
| Addressed | 116 (30%) | 19 (26%) | 135 (29%) |
| Partially addressed | 189 (49) | 13 (18) | 202 (44) |
| Not addressed | 86 (17) | 37 (50) | 103 (22) |
| Consolidated or other[a] | 13 (3) | 5 (7) | 18 (4) |

Source: GAO. | GAO-15-440T.

[a]Actions and areas included in "consolidated or other" are not assessed due to additional work or other information GAO considered.

Efforts to reduce improper peyments could result in significant cost savings. For the first time in recent years, the government-wide improper payment estimate significantly increased—to $124.7 billion in fiscal year 2014, up from $105.8 billion in fiscal year 2013. This increase of almost $19 billion was primarily due to estimates for Medicare, Medicaid, and the Earned Income Tax Credit, which account for over 76 percent of the government-wide estimate. GAO has made numerous recommendations that, if effectively implemented, could improve program management and help reduce improper payments in these programs. Examples include improving the use of prepayment edits in Medicare and requiring states to audit Medicaid payments to and by managed care organizations. Recent laws and guidance have focused attention on the issue of improper payments. For example, the Improper Payments Elimination and Recovery Improvement Act of 2012 enacted into law elements of the Do Not Pay initiative, which is a web-based, centralized data matching service that could help prevent improper payments. However, agencies continue to face challenges, such as statutory limitations and compliance issues, in reducing improper payments.

Chairman Enzi, Ranking Member Sanders, and Members of the Committee:

The federal government faces an unsustainable long-term fiscal path. Changing this path will require difficult fiscal policy decisions to alter both long-term federal spending and revenue. However, in the near-term, executive branch agencies and Congress can act to improve the efficiency and effectiveness of government programs and activities. Opportunities to take action exist in areas where federal programs or activities are fragmented, overlapping, or duplicative. We annually identify and report on these opportunities as well as those to achieve other cost savings or enhanced revenues.[1] One area that we have highlighted as offering the potential for significant cost savings is improper payments.[2] The federal government is accountable for how its agencies and grantees spend hundreds of billions of taxpayer dollars annually, including safeguarding against improper payments and establishing mechanisms to recover those funds when overpayments occur.

My testimony today describes (1) the status of actions taken by the administration and Congress to address the more than 400 recommendations we identified in our annual reports from 2011 through 2014 on fragmentation, overlap, duplication, cost savings, and revenue enhancement, and (2) actions needed to address government-wide improper payments, most recently estimated to be over $124 billion. My comments are primarily based on our four annual reports and related testimonies, as well as our high-risk update and recent work on improper payments and analysis of agency financial reports and reports of inspectors general (IG).[3] These products include detailed explanations of

[1]GAO is mandated to identify and report annually to Congress on federal programs, agencies, offices, and initiatives that have duplicative goals or activities. Pub. L. No. 111-139, § 21, 124 Stat. 29 (2010), 31 U.S.C. § 712 Note.

[2]An improper payment is defined by statute as any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements. It includes any payment to an ineligible recipient, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except for such payments where authorized by law), and any payment that does not account for credit for applicable discounts. Office of Management and Budget guidance also instructs agencies to report as improper payments any payments for which insufficient or no documentation was found.

[3]See Related GAO Products at the end of this testimony statement.

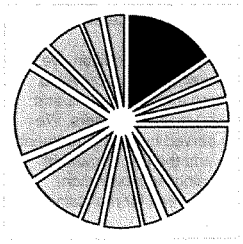
the methods used to conduct our work. In February 2015, we also updated our work on programs noncompliant with reporting requirements for improper payments. We conducted the work that informs this testimony in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## Sustained Attention Is Critical for Addressing Fragmentation, Overlap, and Duplication and Achieving Other Financial Benefits

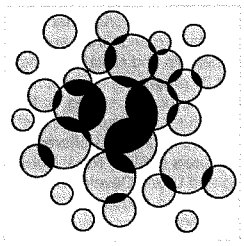
In our four annual reports issued from 2011 through 2014, we identified over 180 areas with approximately 440 actions that the executive branch and Congress could take to address fragmentation, overlap, and duplication; achieve other cost savings; or enhance revenue. Figure 1 outlines the definitions we use for fragmentation, overlap, and duplication. Although it may be appropriate for multiple agencies or entities to be involved in the same programmatic or policy area due to the nature or magnitude of the federal effort, the instances of fragmentation, overlap, or duplication that we include in our annual reports are in areas where multiple programs and activities may be creating inefficiencies.

**Figure 1: Definitions of Fragmentation, Overlap, and Duplication**

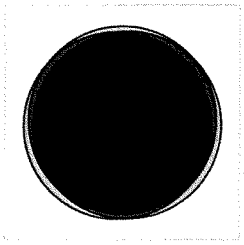
**Fragmentation** refers to those circumstances in which more than one federal agency (or more than one organization within an agency) is involved in the same broad area of national need and opportunities exist to improve service delivery.



**Overlap** occurs when multiple agencies or programs have similar goals, engage in similar activities or strategies to achieve them, or target similar beneficiaries.



**Duplication** occurs when two or more agencies or programs are engaged in the same activities or provide the same services to the same beneficiaries.



Source: GAO. | GAO-15-440T

We consider programs or activities to be fragmented when more than one federal agency (or more than one organization within an agency) is involved in the same broad area of national need, which may result in inefficiencies in how the government delivers services. We have identified fragmentation in multiple programs we reviewed. For example, in our 2014 annual report, we reported that the Department of Defense (DOD) does not have a consolidated agency-wide strategy to contract for health care professionals, resulting in a contracting approach that is largely fragmented. Although some of the military departments attempted to consolidate their health care staffing requirements through joint-use contracts, such contracts only accounted for approximately 8 percent of the $1.14 billion in obligations for health care professionals in fiscal year 2011. Moreover, in May 2013 we identified several instances in which a single military department awarded numerous task orders for the same type of health care professional in the same area or facility. For example,

we identified 24 separate task orders for contracted medical assistants at the same military treatment facility.[4] By not consolidating its requirements, this facility missed the opportunity to achieve potential cost savings and other efficiencies.

Fragmentation also can be a harbinger of overlap or duplication. Overlap occurs when multiple agencies or programs have similar goals, engage in similar activities or strategies to achieve them, or target similar beneficiaries. We found overlap among federal programs or initiatives in a variety of areas, including housing assistance. In particular, in our 2012 annual report, we reported that 20 different entities administered 160 programs, tax expenditures, and other tools that supported homeownership and rental housing in fiscal year 2010. In addition, we identified 39 programs, tax expenditures, and other tools that provided assistance for buying, selling, or financing a home and 8 programs and tax expenditures that provide assistance to rental property owners. We found overlap in products offered and markets served by the Department of Agriculture's (USDA) Rural Housing Service and the Department of Housing and Urban Development's Federal Housing Administration, among others. In August 2012, we questioned the need for maintaining separate programs for rural areas.[5]

In other areas, we found evidence of duplication, which occurs when two or more agencies or programs engage in the same activities or provide the same services to the same beneficiaries. For example, we reported in 2013 that a total of 31 federal departments and agencies invested billions of dollars to collect, maintain, and use geospatial information—information linked to specific geographic locations that supports many government functions, such as maintaining roads and responding to natural disasters. We found that federal agencies had not effectively implemented policies and procedures that would help them identify and coordinate geospatial data acquisitions across the government. As a result, we found that agencies made duplicative investments and risk missing opportunities to jointly acquire data and save millions of dollars.

[4]GAO, *Defense Health Care: Department of Defense Needs a Strategic Approach to Contracting for Health Care Professionals,* GAO-13-322 (Washington, D.C.: May 28, 2013).

[5]GAO, *Housing Assistance: Opportunities Exist to Increase Collaboration and Consider Consolidation,* GAO-12-554 (Washington, D.C.: Aug. 16, 2012).

In addition, opportunities exist to reduce the cost of government operations or enhance revenue collections. For example, our body of work has raised questions about whether DOD's efforts to reduce headquarters overhead will result in meaningful savings. In 2013, the Secretary of Defense directed a 20 percent cut in management headquarters spending throughout DOD, to include the combatant commands and service component commands. However, our work found that mission and headquarters-support costs for the five geographic combatant commands and their service component commands we reviewed more than doubled from fiscal years 2007 through 2012, to about $1.7 billion. We recommended that DOD more systematically evaluate the sizing and resourcing of its combatant commands. If the department applied the 20 percent reduction in management headquarters spending to the $1.7 billion DOD used to operate and support the five geographic combatant commands in fiscal year 2012, we reported that DOD could achieve up to an estimated $340 million in annual savings.

In our 2013 report, we reported that refining return-on-investment measures could improve how the Internal Revenue Service (IRS) allocates enforcement resources (subject to other considerations, such as minimizing compliance costs and ensuring equitable treatment of taxpayers). Our work illustrated that a small shift in existing resources—from examinations of less productive groups of tax returns to more productive groups—could potentially increase enforcement revenue by more than $1 billion. In addition, in our 2011 annual report, we identified opportunities for improving the Department of the Interior's management of federal oil and gas resources. In particular, increasing the diligent development of federal lands and waters leased for oil and gas exploration and production and considering adjustments to Interior's royalty rates to a level that would ensure the government a fair return, among other actions, could result in approximately $2 billion in revenues over 10 years.

## Executive Branch and Congress Continued to Make Progress in Addressing Previously Identified Issues

We found that the executive branch agencies and Congress have made progress in addressing the actions identified in our 2011–2014 annual reports. As shown in table 1, of the approximately 440 actions needed in these areas, 135 (29 percent) were addressed, 202 (44 percent) were partially addressed, and 103 (22 percent) were not addressed as of November 2014.[6]

**Table 1: Status of Actions Directed to Congress and the Executive Branch in Our 2011-2014 Annual Reports, as of November 19, 2014**

| | Executive branch[a] | | Congress[b] | | Grand totals | |
|---|---|---|---|---|---|---|
| Status | Number of actions | Percentage | Number of actions | Percentage | Total number of actions | Overall percentage |
| Addressed | 116 | 30% | 19 | 26% | 135 | 29% |
| Partially addressed | 189 | 49 | 13 | 18 | 202 | 44 |
| Not addressed | 66 | 17 | 37 | 50 | 103 | 22 |
| Consolidated or other | 13 | 3 | 5 | 7 | 18 | 4 |

Source: GAO. | GAO-15-440T

Note: In assessing actions suggested for Congress, we applied the following criteria: "addressed" means relevant legislation has been enacted and addresses all aspects of the action needed; "partially addressed" means a relevant bill has passed a committee, the House of Representatives, or the Senate, or relevant legislation has been enacted but only addressed part of the action needed; and "not addressed" means a bill may have been introduced but did not pass out of a committee, or no relevant legislation was introduced. In assessing actions suggested for the executive branch, we applied the following criteria: "addressed" means implementation of the action needed was completed; "partially addressed" means the action needed was in development, or started but not yet completed; and "not addressed" means the administration, the agencies, or both made minimal or no progress toward implementing the action needed. Actions included in "consolidated or other" were not assessed due to additional work or other information we considered.

[a]Executive branch agencies took steps that addressed four actions directed to Congress.

[b]Congress took steps that fully addressed one action and partially addressed another action directed to executive branch agencies.

Examples of progress made include DOD and Congressional actions to reduce DOD's fragmented approach for acquiring combat uniforms. In 2013, we found that DOD's fragmented approach could lead to increased risk on the battlefield for military personnel and increased development and acquisition costs. In response, DOD developed and issued guidance on joint criteria that will help to ensure that future service-specific uniforms will provide equivalent levels of performance and protection. In

[6]Eighteen actions, or 4 percent, were consolidated into other areas and we did not assess them due to additional work or other information that we considered.

addition, a provision in the National Defense Authorization Act for Fiscal Year 2014 established as policy that the Secretary of Defense shall eliminate the development and fielding of service-specific combat and camouflage utility uniforms in order to adopt and field common uniforms for specific environments to be used by all members of the armed forces.[7] Subsequently, the Army chose not to introduce a new family of camouflage uniforms into its inventory, in part, because of this legislation, resulting in a cost avoidance of about $4.2 billion over 5 years.

In addition, progress has been made in addressing the proliferation of certain programs. For example, the National Science and Technology Council's (NSTC) implemented our suggested actions to better manage overlap across science, technology, engineering, and mathematics (STEM) education programs. Specifically, NSTC released guidance to agencies on how to align their programs and budget submissions with the goals of NSTC's 5-Year strategic plan for STEM education and on developing evaluations for the programs. In addition, several programs were eliminated or consolidated into new programs, with the total number of STEM education programs dropping from 209 funded in fiscal year 2010 to 158 funded in 2012. The President's fiscal year 2016 budget proposes to further consolidate and eliminate 20 STEM programs across eight agencies. These efforts help agencies better target resources toward programs with positive outcomes and achieve the greatest impact in developing a pipeline of future workers in STEM fields. As another example, the Workforce Innovation and Opportunity Act, enacted in July 2014, includes provisions to strengthen the workforce development system under which a variety of employment and training services are provided to program participants. In particular, the law requires that states develop a unified state plan that covers all designated core programs to receive certain funding. States' implementation of the requirement may enable them to increase administrative efficiencies in employment and training programs—a key objective of our prior recommendations on employment and training programs.

[7]Subject to certain exceptions, the provision also prohibits the military departments from adopting new pattern designs or uniform fabrics unless they will be adopted by all services or the uniform is already in use by another service. *See* Pub. L. No. 113-66, § 352(a), (b) (2013). In addition, DOD must issue implementing guidance requiring the military departments to, among other things, ensure that new uniforms meet commanders of combatant command's geographic and operational requirements and continually work together to assess and develop new uniform technologies to improve warfighter survivability. *See* § 352(f).

We estimated that executive branch and congressional efforts to address suggested actions resulted in roughly $20 billion in financial benefits from fiscal years 2011 through 2014, with another approximately $80 billion in additional benefits projected to be accrued through 2023.[8] For example, in our 2011 annual report, we stated that the ethanol tax credit would cost about $5 billion in forgone revenues in 2011 and that Congress could reduce annual revenue losses by addressing duplicative federal efforts directed at increasing domestic ethanol production. To reduce these revenue losses, we suggested that Congress consider whether revisions to the ethanol tax credit were needed and suggested options to consider, including allowing the credit for the volumetric ethanol excise tax (for fuel blenders that purchase and blend ethanol with gasoline) to expire at the end of 2011. Congress allowed the tax credit to expire at the end of 2011.

In our 2012 annual report, we presented options for adjusting the Transportation Security Administration's (TSA) passenger security fee—a uniform fee on passengers of U.S. and foreign air carriers originating at airports in the United States—to offset billions of dollars in civil aviation security costs. The Bipartisan Budget Act of 2013 modifies the passenger security fee from its current per enplanement structure ($2.50 per enplanement with a maximum one-way-trip fee of $5.00) to a structure that increases the passenger security fee to a flat $5.60 per one-way-trip, effective July 1, 2014.[9] Specifically, this legislation identifies $12.6 billion in fee collections that, over a 10-year period beginning in fiscal year 2014 and continuing through fiscal year 2023, will contribute to deficit reduction.[10] Fees collected beyond those identified for deficit reduction

[8]In calculating these estimates, we relied on estimates from the Congressional Budget Office and the Joint Committee on Taxation, where possible. We also developed estimates based on agencies' data and used agencies' developed estimates. The totals reflect a summary of these estimates, which relied on different data sources and methodologies and considered different time periods. They represent a rough estimate of financial benefits and have been rounded down to the nearest $5 billion.

[9]See Pub. L. No. 113-67, § 601(b), 127 Stat. at 1187 (amending 49 U.S.C. § 44940(c)). Pursuant to the act, collections under this modified fee structure will contribute to deficit reduction as well as to offsetting TSA's aviation security costs. In addition, the first $250 million in fees collected each fiscal year are, consistent with existing law, to be deposited in the Aviation Security Capital Fund for use in supporting aviation security-related airport capital improvement projects or for other purposes specified in statute. See 49 U.S.C. §§ 44923(h), 44940(i).

[10]The Bipartisan Budget Act further revoked TSA's authority to collect the Aviation Security Infrastructure Fee, which TSA had been collecting from air carriers pursuant to 49 U.S.C. § 44940(a)(2). See Pub. L. No. 113-67, § 601(a), 127 Stat. 1165, 1187.

are available, consistent with existing law, to offset TSA's aviation security costs. This fee is expected to cover 43 percent of aviation security costs beginning in fiscal year 2014, compared with the approximately 30 percent offset under the previous fee structure.[11]

Table 2 outlines a number of addressed actions that resulted in or are expected to result in cost savings or enhanced revenue. We plan to release an update on the status of all actions presented in our 2011–2014 reports in conjunction with our next annual report in April 2015.[12]

**Table 2: Selected Addressed Actions with Associated Cost Savings and Enhanced Revenues, 2011–2014**

| Annual report | Addressed actions |
|---|---|
| 2011 | **Domestic Ethanol Production** (Area 13): Congress allowed the Volumetric Ethanol Excise Tax Credit to expire at the end of 2011, which eliminated duplicative federal efforts directed at increasing domestic ethanol production and reduced revenue losses by **$4.5 billion** in fiscal year 2012 and **$6.1 billion** in fiscal year 2013. |
| 2011 | **Farm Program Payments** (Area 35): The Agricultural Act of 2014 eliminated direct payments to farmers and should save approximately **$4.9 billion annually** from fiscal year 2015 through fiscal year 2023, according to the Congressional Budget Office. |
| 2011 | **Baggage Screening Systems** (Area 78): The Transportation Security Administration (TSA) estimated that the agency saved a cumulative **$104.5 million** in personnel costs from fiscal years 2011 through 2013 from its efforts to replace or modify older checked baggage screening systems with more efficient in-line systems, as we suggested. |
| 2012 | **Air Force Food Service** (Area 33): In 2011, the Air Force issued a memorandum to the Major Commands directing a review of existing food service contracts. As a result, according to Air Force officials, the Air Force reviewed and renegotiated the food service contracts at eight installations for a total savings of over **$2.5 million per year**. In addition, according to Air Force officials, all food service contracts were validated again during fiscal year 2012 for additional savings of over **$2.2 million per year**. Air Force officials said that the Air Force will review contracts annually for areas where costs can be reduced. |
| 2012 | **Overseas Defense Posture** (Area 37): The United States Forces Korea conducted a series of consultations with the military services to evaluate the costs and benefits associated with tour normalization, as we suggested, and decided not to move forward with the full tour normalization initiative because it was not affordable. DOD's decision to not move forward with this initiative resulted in a cost avoidance of **$3.1 billion** from fiscal years 2012 through 2016. |

[11]In addition to the passenger security fee, TSA also currently imposes a fee on air carriers—the Aviation Security Infrastructure Fee—to further offset the costs of aviation security. See 49 U.S.C. § 44940(a)(2). Pursuant to the Bipartisan Budget Act, TSA's authority to collect this fee will expire effective October 1, 2014. See Pub. L. No. 113-67, § 601(a), 127 Stat. at 1187.

[12]To help maintain attention on these issues, in 2013, we launched *GAO's Action Tracker*, a publicly accessible, online website of the areas and actions presented in this series of annual reports. The *Action Tracker* includes progress updates and assessments of all the actions we suggested for Congress and executive branch agencies.

| Annual report | Addressed actions |
|---|---|
| 2012 | **Passenger Aviation Security Fees** (Area 48): The Bipartisan Budget Act of 2013 modifies the passenger security fee from its current per enplanement structure ($2.50 per enplanement with a maximum one-way-trip fee of $5.00) to a structure that increases the passenger security fee to a flat $5.60 per one-way-trip, effective July 1, 2014.[a] Pursuant to the act, collections under this modified fee structure will contribute to deficit reduction as well as to offsetting TSA's aviation security costs.[b] Specifically, the act identifies **$12.6 billion** in fee collections that, over a 10-year period beginning in fiscal year 2014 and continuing through fiscal year 2023, should contribute to deficit reduction.[c] Fees collected beyond those identified for deficit reduction are available, consistent with existing law, to offset TSA's aviation security costs. According to the House of Representatives and Senate Committees on the Budget, and notwithstanding amounts dedicated for deficit reduction, collections under the modified fee structure will offset about 43 percent of aviation security costs, compared to the approximate 30 percent currently offset under the existing fee structure.[d] |

Source: GAO. | GAO-15-440T

[a]See Pub. L. No. 113-67, § 601(b), 127 Stat. at 1187 (2013), amending 49 U.S.C. § 44940(c).

[b]In addition, the first $250 million in fees collected each fiscal year are, consistent with existing law, to be deposited in the Aviation Security Capital Fund for use in supporting aviation security-related airport capital improvement projects or for other purposes specified in statute. See 49 U.S.C. §§ 44923(h), 44940(i).

[c]See 49 U.S.C. § 44940(i) (identifying, among other things, the specific amount to be credited as offsetting receipts and deposited in the general fund of the Treasury each fiscal year, 2014 through 2023).

[d]The Bipartisan Budget Act further revoked TSA's authority to collect the Aviation Security Infrastructure Security Fee, which TSA had been collecting from air carriers pursuant 49 U.S.C. § 44940(a)(2). See Pub. L. No. 113-67, § 601(a), 127 Stat. at 1187 (2013).

## Leadership Attention Is Required to Continue Progress on Previously Identified Actions

The executive branch agencies and Congress have made progress in addressing some suggested actions, but many other actions require leadership attention to ensure that they will be fully addressed. More specifically, 68 percent of actions directed to Congress and 66 percent of actions directed to executive branch agencies identified in our 2011–2014 annual reports remain partially addressed or not addressed. As illustrated below, our work identified areas of fragmentation, overlap, or duplication that spanned the range of government activities, along with opportunities to address these issues. Without increased or renewed leadership focus, opportunities will be missed to improve the efficiency and effectiveness of programs and save taxpayer dollars.

### Fragmentation, Overlap, and Duplication Opportunities

**Defense**

Our work on defense has highlighted opportunities to address overlapping and potentially duplicative services that result from multiple entities providing the same service, including the following examples:

Defense Satellite Control Operations: In our 2014 annual report, we reported that DOD has increasingly had deployed dedicated satellite control operations networks, as opposed to shared networks that support multiple kinds of satellites. For example, at one Air Force base in 2013,

eight separate control centers operated satellites for 10 satellite programs. Furthermore, the Air Force alone funded about $2.1 billion in fiscal year 2011 on satellite operations.[13] While dedicated networks can offer some benefits to programs, they also can be more costly to maintain and have led to fragmented and potentially duplicative networks that require more infrastructure and personnel to manage as compared with shared networks. We suggested that DOD take actions to improve its ability to identify and then assess the appropriateness of a shared versus dedicated satellite control system, which DOD has begun to address.

- **Electronic Warfare**: We reported in 2011 that all four military services in DOD had been separately developing and acquiring new airborne electronic attack systems and that spending on new and updated systems was projected to total more than $17.6 billion during fiscal years 2007–2016. While the department has taken steps to better inform its investments in airborne electronic attack capabilities, it has yet to assess its plans for developing and acquiring two new expendable jamming decoys to determine if these initiatives should be merged.[14] For example, in fiscal year 2015 one DOD decoy system is already in production, while DOD defines performance requirements for another decoy system. Without an assessment for potential duplication, DOD may preclude the timely identification and prevention of unnecessary overlap between its systems.

- **Unmanned Aircraft Systems**: We reported in 2012 that DOD's cost estimates for acquisition programs for unmanned aircraft systems (UAS) and related systems exceeded $37.5 billion for fiscal years 2012–2016.[15] We found that military service-driven requirements, rather than an effective department-wide strategy, led to overlap in DOD's UAS capabilities, resulting in programs and systems being pursued that have similar flight characteristics and mission

[13]This total includes Research, Development, Test, and Evaluation; Operation and Maintenance (O&M); Personnel; and, Other Procurement funds. Air Force officials could provide data for only 1 fiscal year of funding for satellite operations.

[14]We examined the Air Force and Navy plans for developing and acquiring new expendable jamming decoys (specifically, the services' Miniature Air Launched Decoy—Jammer (MALD-J) Increment II and Airborne Electronic Attack Expendable initiatives).

[15]The $37.5 billion amount includes funding for development, procurement, sustainment, military construction and personnel, and war funding to support UAS activities in then-year dollars identified in the President's 2012 budget submission.

requirements. To reduce the likelihood of overlap and potential duplication in DOD's UAS portfolio, we suggested several actions to DOD that have not been fully implemented. The overlap in current UAS programs, as well as continued potential for overlap in future programs, shows that DOD must do more to implement these actions. Our analysis suggests that the potential for savings would be significant, and with DOD's continued commitment to UAS for meeting strategic requirements, action is all the more imperative.

More broadly, we identified multiple weaknesses in the way DOD acquires weapon systems and the actions that are needed to address these issues, which we recently highlighted in our high-risk series update.[16] For example, further progress must be made in tackling the incentives that drive the acquisition process and its behaviors, applying best practices, attracting and empowering acquisition personnel, reinforcing desirable principles at the beginning of programs, and improving the budget process to allow better alignment of programs and their risks and needs. Addressing these issues could help DOD improve the returns on its $1.5 trillion investment in major weapon systems and find ways to deliver capabilities for less than it has in the past.

**Information Technology**

The federal government plans to spend $79 billion on information technology (IT) in fiscal year 2015. The magnitude of these expenditures highlights the importance of avoiding duplicative investments to better ensure the most efficient use of resources. Opportunities remain to reduce duplication and the cost of government operations in critical IT areas, many of which require agencies to work together to improve systems, including the following examples:

- **Information Technology Investment Portfolio Management**: To better manage existing IT systems, the Office of Management and Budget (OMB) launched the PortfolioStat initiative. PortfolioStat requires agencies to conduct an annual, agency-wide review of their IT portfolios to reduce commodity IT spending and demonstrate how their IT investments align with their missions and business functions, among other things. In 2014, we reported that while the 26 federal agencies required to participate in PortfolioStat had made progress in

[16]GAO, *High-Risk Series: An Update*, GAO-15-290 (Washington, D.C.: Feb. 11, 2015).

implementing OMB's initiative, weaknesses existed in agencies' implementation of the initiative, such as limitations in the Chief Information Officers' authority. As noted in our recent high-risk update, we made more than 60 recommendations to improve OMB and agencies' implementation of PortfolioStat and provide greater assurance that agencies will realize the nearly $6 billion in savings they estimated they would achieve through fiscal year 2015.

- **Federal Data Centers**: In 2014, we found that consolidating federal data centers would provide an opportunity to improve government efficiency and achieve cost savings and avoidances of about $5.3 billion by fiscal year 2017. Although OMB has taken steps to identify data center consolidation opportunities across agencies, weaknesses exist in the execution and oversight of the consolidation efforts. For example, we previously reported that all 24 departments and agencies in the Federal Data Center Consolidation Initiative had not yet completed a data center inventory or the consolidation plans to implement their consolidation initiative. It will continue to be important for agencies to complete their inventories and implement their plans for consolidation to better ensure continued progress toward OMB's planned consolidation, optimization, and cost-savings goals.

- **DOD and Department of Veterans Affairs (VA) Electronic Health Records System**: DOD and VA abandoned their plans to develop a single electronic system for health records that both departments would share. Although the departments' 2008 study showed that over 97 percent of inpatient functional requirements were common to both DOD and VA, they decided to pursue separate electronic health record system modernization efforts. In February 2014, we reported that the departments had based this decision on the assertion that pursuing separate systems would be less expensive and faster than the single, shared-system approach. However, they had not supported this assertion with cost and schedule estimates that compared the separate efforts with estimates for the single-system approach. Through continued duplication of these efforts, the departments may be incurring unnecessary system development and operation costs and missing opportunities to support higher-quality health care for servicemembers and veterans. The departments plan to make the separate systems interoperable as required by law.

Given the federal government's continued experience with failed and troubled IT projects, coupled with the fact that OMB initiatives to help address such problems have not been fully implemented, we added improving the management of IT acquisitions and operations to our 2015

high-risk list. The federal information technology acquisition reforms enacted in December 2014 reinforce a number of the actions that we have recommended to address IT management issues. For example, the law containing these reforms codifies federal data center consolidation, emphasizing annual reporting on cost savings and detailed metric reporting, and OMB's PortfolioStat process, focusing on reducing duplication, consolidation, and cost savings. If effectively implemented, this legislation should improve the transparency and management of IT acquisitions and operations across the government. Twenty-seven federal agencies plan to spend about $58 billion—almost three-quarters of the overall $79 billion budgeted for federal IT in fiscal year 2015—on the operations and maintenance of legacy (i.e., steady-state) investments. The significance of these numbers highlights the importance of ensuring that OMB's PortfolioStat and Data Center Consolidation initiatives meet their cost-savings goals.

**Education and Training**

We identified several opportunities to help address the proliferation of certain education and training programs and improve the delivery of benefits, which the executive branch agencies and Congress have been working to address. However, additional opportunities remain to more effectively invest in education and training programs, including the following examples:

- **Teacher Quality**: Federal efforts to improve teacher quality led to the creation and expansion of a variety of programs across the federal government; however, there is no government-wide strategy to minimize fragmentation, overlap, or duplication among these programs. Specifically, in our 2011 annual report we identified 82 distinct programs designed to help improve teacher quality, either as a primary purpose or as an allowable activity. Many of these programs (administered across 10 federal agencies) shared similar goals. We suggested that Congress could enact legislation to eliminate teacher quality programs that are too small to evaluate cost-effectively or to combine programs serving smaller target groups into a larger program. In February 2015, the House Committee on Education and Workforce reported the Student Success Act, H.R. 5. According to House Report 114-24, H.R. 5 would consolidate most teacher quality programs into a new flexible grant program. In addition, we suggested that Congress could include legislative provisions to help the Department of Education reduce fragmentation, such as by giving broader discretion to the agency to move resources from certain

programs. In February 2015, the Senate Committee on Health, Education, Labor, and Pensions reported the Strengthening Education through Research Act, S. 227, which would authorize the Department of Education to reserve and consolidate funds from Elementary and Secondary Education Act programs to carry out high-quality evaluations and increase the usefulness of those evaluations. These bills, if enacted, could help eliminate some of the barriers to educational program alignment and help invest scarce resources more effectively.

- **Employment for Persons with Disabilities**: In June 2012, we reported on 45 programs administered by nine federal agencies that supported employment for people with disabilities and found these programs were fragmented and often provided similar services to similar populations. OMB has worked with executive agencies to propose consolidating or eliminating some of these programs. In particular, three programs were eliminated in the Workforce Innovation and Opportunity Act: the Veterans' Workforce Investment Program, administered by the Department of Labor, and the Migrant and Seasonal Farmworker Program and Projects with Industry, administered by the Department of Education. However, OMB has not yet systematically looked across all agencies and programs—beyond those already identified in the Departments of Education and Labor—for opportunities to streamline and improve service delivery, which could help achieve greater efficiency and effectiveness.

Table 3 outlines these and other examples of opportunities for consolidating or streamlining programs to better provide services.

**Table 3: Potential Streamlining or Consolidation Opportunities in Selected Areas Identified in Our 2011-2014 Annual Reports**

| Area | Key finding(s) | Related recommendation(s) |
|---|---|---|
| Contracting for Defense Health Care Professionals | According to Department of Defense (DOD) data, joint-use contracts among military departments accounted for only about 8 percent of the $1.14 billion in obligations for health care professionals in fiscal year 2011. Also, we identified several instances where numerous task orders were awarded by a single military department for the same type of provider in the same area or facility, such as 24 task orders in fiscal year 2011 for medical assistants, 16 for licensed practical nurses, 8 for clinical psychologists, and 6 for family practitioners—all at the same military treatment facility. | DOD should develop and implement a consolidated agency-wide strategy to contract for health care professionals to reduce fragmentation and achieve greater efficiencies. |

| Area | Key finding(s) | Related recommendation(s) |
|---|---|---|
| Electronic Warfare | We reported in 2012 that all four military services in DOD separately were acquiring new airborne electronic attack systems and that spending on new and updated airborne electronic attack systems was projected to total more than $17.6 billion from fiscal year 2007 through 2016. | DOD should identify opportunities to consolidate its airborne electronic attack programs to reduce overlap and improve its return on acquisition investments. |
| Nuclear Nonproliferation | In December 2011, we identified 21 government programs and offices under five federal agencies that play a role in preventing and detecting smuggling of nuclear materials and illicit trafficking of related technologies overseas. | The Assistant to the President for National Security Affairs should conduct a comprehensive review to address strategic planning limitations and potential fragmentation and overlap concerns among programs combating nuclear smuggling overseas. |
| Department of Justice Grants | In 2010, the Department of Justice awarded over $3 billion in grants through more than 253 grant solicitations. We found that more than 20 percent provided funds that could be used for victim assistance and related research. | The Attorney General of the U.S. should conduct an assessment to better understand the extent to which Justice grant programs overlap with one another and determine if grant programs may be consolidated. |
| Overseas Administrative Services | We reported in 2011 that the Department of State and other agencies operating overseas have made limited progress in reducing the cost of administrative support services overseas. Agencies continue to provide many services independently, despite economies of scale available through greater participation in the International Cooperative Administrative Support Services system (ICASS). | Congress may wish to consider requiring agencies to participate in the ICASS service unless they provide a business case to show that they can obtain these services outside of ICASS without increasing overall costs to the U.S. government or that their mission cannot be achieved within ICASS. |
| Housing Assistance | We identified 20 different entities that administered 160 programs, tax expenditures, and other tools that supported homeownership and rental housing in fiscal year 2010. Moreover, we identified overlap between products offered and markets served by Department of Housing and Urban Development's (HUD) Federal Housing Administration and the Department of Agriculture's (USDA) Rural Housing Service. | Congress could consider requiring HUD and USDA to examine the benefits and costs of merging the overlapping programs. To help inform Congress's decision-making process, the Secretaries of HUD, Treasury, and USDA along with VA should evaluate and report on the specific opportunities for consolidating similar housing programs, including those that would require statutory changes. |
| Employment for People with Disabilities | In 2012, we reported on 45 programs that supported employment for people with disabilities and found that the programs were fragmented and often provided similar services to similar populations. | The Office of Management and Budget (OMB) should work with agencies to determine whether program consolidation might result in administrative savings and more effective and efficient delivery of services. |
| Financial Literacy | In 2014, we identified 13 significant financial literacy programs or activities among 12 federal agencies. | The Department of the Treasury and the Consumer Financial Protection Bureau should develop clear recommendations on the allocation of federal financial literacy resources across programs and agencies, and identify options for consolidating federal financial literacy efforts. |
| Federal Data Centers | We reported that the number of federal data centers grew from 432 in 1998 to more than 9,658 as of May 2014. The data centers often housed similar types of equipment and provide similar processing and storage capabilities. | OMB should work with agencies to establish goals and targets for consolidation (both in terms of cost savings and fewer data centers), maintain strong oversight of the agencies' efforts, and look for consolidation opportunities across agencies. |

| Area | Key finding(s) | Related recommendation(s) |
|---|---|---|
| Teacher Quality | We identified 82 distinct programs designed to help improve teacher quality, either as a primary purpose or as an allowable activity, administered across 10 federal agencies. Many of these programs share similar goals. | Congress may choose to eliminate programs that are too small to evaluate cost-effectively, combine programs serving smaller target groups into a larger program, or help the Department of Education reduce fragmentation, such as by giving broader discretion to the agency to move resources from certain programs. |

Source: GAO. | GAO-15-440T

## Cost-Savings and Revenue Enhancement Opportunities

Opportunities also exist to achieve cost savings or enhance revenue collection. As with the opportunities to address fragmentation, overlap and duplication, fully achieving these opportunities will require sustained leadership by executive branch agencies and Congress. Examples of these actions include rescinding unobligated funds, improving fiscal oversight over Medicare and Medicaid, reducing contract spending through strategic sourcing, and increasing tax revenue collections.

### Rescinding Unobligated Funds

We reported in March 2013 that the Department of Energy (DOE) was not actively considering any applications under the Advanced Technology Vehicle Manufacturing loan program that was established to provide loans for projects to produce more fuel-efficient passenger vehicles and their components.[17] In our 2014 annual report, we suggested that unless DOE could demonstrate a demand for new loans and viable applications, Congress might wish to consider rescinding all or part of the remaining $4.2 billion in credit subsidy appropriations made available under this program. Since our April 2014 annual report, DOE has not yet demonstrated a demand for these loans that would substantially use the remaining credit subsidy appropriations. The department received four complete applications seeking a total of $945 million in loans, which represents 5.7 percent of the program's remaining $16.6 billion in loan

[17]GAO, *Department of Energy: Status of Loan Programs*, GAO-13-331R (Washington, D.C.: Mar. 15, 2013).

authority.[18] DOE officials stated that the program anticipated issuing conditional commitments for loans in fiscal year 2015.[19] In January 2015, the Savings, Accountability, Value, and Efficiency Act of 2015 was introduced in the House of Representatives, and includes a provision to rescind unobligated balances of funding for the program, including the remaining credit subsidy appropriations.[20]

**Improving Fiscal Oversight of Medicare and Medicaid**

Over the years, we identified a number of actions that have the potential for sizable cost savings through improved fiscal oversight in the Medicare and Medicaid programs. For example, the Centers for Medicare & Medicaid Services (CMS), the agency in the Department of Health and Human Services (HHS) that is responsible for overseeing both programs, could save billions of dollars by improving the accuracy of its payments to Medicare Advantage programs, such as through methodology adjustments to account for diagnostic coding differences between Medicare Advantage and traditional Medicare.[21] In addition, we found that federal spending on Medicaid demonstrations could be reduced by billions of dollars if HHS were required to improve the process for reviewing, approving, and making transparent the basis for spending

[18]The amount of credit subsidy appropriations needed for $945 million in loans would depend on the estimated credit subsidy costs at the time the loans were made. Credit subsidy costs represent the estimated net long-term cost of extending or guaranteeing credit, in present value terms, over the entire period the loans are outstanding (not including administrative costs). The average credit subsidy cost rate from the previous five ATVM loans was about 25 percent. At that rate, the credit subsidy cost for $945 million in loans would be about $236 million, or 5.6 percent of the remaining $4.2 billion in credit subsidy appropriations.

[19]A conditional commitment is a commitment by DOE to issue a loan if the applicant satisfies specific requirements. The Secretary of Energy has discretion to cancel a conditional commitment at any time for any reason before the issuance of a loan guarantee. Should conditional commitments for new loans occur, we would reassess the status of this action.

[20]See H.R. 614, 114th Cong. (2015).

[21]Medicare Advantage is the private plan alternative to the original Medicare program. Medicare Advantage plans are paid a fixed, per member, per month payment to provide all services covered under original Medicare. This payment does not vary on the basis of the services beneficiaries receive.

limits approved for Medicaid demonstrations.[22] In particular, our work between 2002 and 2013 has shown that HHS approved several demonstrations without ensuring that they would be budget neutral to the federal government.

To address this issue, we suggested that Congress could require the Secretary of Health and Human Services to improve the Medicaid demonstration review process, through steps such as improving the review criteria, better ensuring that valid methods are used to demonstrate budget neutrality, and documenting and making clear the basis for the approved limits. In September 2014, the Chairman, House Committee on Energy and Commerce, and Ranking Member, Senate Committee on Finance, sent a letter to CMS asking for additional information on steps the agency was taking to improve the budget neutrality of demonstrations. Enhancing the process HHS uses to demonstrate budget neutrality of its demonstrations could save billions in federal expenditures.

**Reducing Contract Spending through Strategic Sourcing**

In 2013, we reported that federal agencies could achieve significant cost savings annually by expanding and improving their use of strategic sourcing—a contracting process that moves away from numerous individual procurement actions to a broader aggregated approach. In particular, we reported that a reduction of 1 percent in spending from large procurement agencies, such as DOD, would equate to over $4 billion in savings. However, a lack of clear guidance on metrics for measuring success has hindered the management of ongoing strategic sourcing efforts across the federal government. Since our 2013 report, OMB has made progress by issuing guidance on calculating savings for government-wide strategic sourcing contracts and in December 2014 issued a memorandum on category management, which in part identifies federal spending categories suitable for strategic sourcing. These categories cover some of the government's largest spending categories,

[22]Under Section 1115 of the Social Security Act, the Secretary of Health and Human Services can approve waivers of certain Medicaid requirements, and provide states with new spending authorities, for purposes of implementing Medicaid demonstration projects. The demonstrations under the law are for purposes of testing new ways to operate state programs and deliver services, and agency policy requires that the programs not increase federal spending.

including IT and professional services. As part of this effort, OMB directed the General Services Administration to develop additional guidance and performance metrics. However, until OMB sets government-wide goals and establishes metrics, the government may miss opportunities for cost savings though strategic sourcing.

In addition, strategic sourcing could play a role in helping DOD acquire services more efficiently. In our recent high-risk work, we noted that DOD made some progress in acquiring services through strategic sourcing, but had more to do. For example, as of March 2014, DOD had identified some of high-spend categories as candidates for strategic sourcing, such as IT. Further, DOD appointed individuals within specified portfolios of major areas of DOD services spending to help coordinate strategic sourcing efforts. But according to DOD officials, DOD still is developing the roles, responsibilities and authorities for some of these offices. Additionally, the department has not yet issued guidance establishing goals and metrics to track progress.

**Increasing Tax Revenue Collections**

IRS estimated that the gross tax gap—the difference between taxes owed and taxes paid on time—was $450 billion for tax year 2006 (the most recent year for which data were available). IRS estimated that it eventually would recover about $65 billion of this amount through late payments and enforcement actions, leaving a net tax gap of $385 billion. Because of its magnitude, even a 1 percent improvement in net tax gap would generate almost $4 billion in revenue collections annually.

Over the last 4 years, our work identified multiple opportunities for the government to increase revenue collections. For example, in 2014, we identified three actions that Congress could authorize and that could increase tax revenue collections from delinquent taxpayers by hundreds of millions of dollars over a 5-year period: limiting issuance of passports to applicants, levying payments to Medicaid providers, and identifying security clearance applicants. For example, Congress could consider requiring the Secretary of State to prevent individuals who owe federal taxes from receiving passports. We found that in fiscal year 2008, passports were issued to about 16 million individuals; about 1 percent of these collectively owed more than $5.8 billion in unpaid federal taxes as of September 30, 2008. According to a 2012 Congressional Budget Office estimate, the federal government could save about $500 million over a 5-year period by revoking or denying passports in cases of certain federal tax delinquencies.

Table 4 highlights these and other opportunities that could result in tens of billions of dollars in cost savings or enhanced revenue.

**Table 4: Selected Areas with Associated Cost-Savings and Revenue-Enhancement Opportunities from Our 2011-2014 Annual Reports**

| Annual report | Areas identified |
|---|---|
| **Defense and Contracting** | |
| 2011 | **Tactical Wheeled Vehicles** (Area 6): A department-wide acquisition strategy could reduce the Department of Defense's (DOD) risk of costly duplication in purchasing Tactical Wheeled Vehicles. Reducing the number of joint light tactical vehicles DOD procures could result in **billions of dollars** in cost savings. |
| 2011 | **Weapon Systems Acquisition Programs** (Area 38): Employing best management practices could help DOD achieve significant cost savings on the $1.5 trillion (fiscal year 2014 dollars) it expects to invest in the development and procurement of its portfolio of 80 major defense acquisition programs. |
| 2014 | **Combatant Command Headquarters Costs** (Area 12): If the department applied the 20 percent reduction in management headquarters spending to the $1.7 billion DOD used to operate and support the five geographic combatant commands in fiscal year 2012, DOD could potentially achieve up to an estimated **$340 million in annual savings**. |
| 2013 | **Agencies' Use of Strategic Sourcing** (Area 23): Selected agencies could better leverage their buying power and achieve additional savings by directing more procurement spending to existing strategically sourced contracts and further expanding strategic sourcing practices to their highest-spending procurement categories—savings of 1 percent from selected agencies' procurement spending alone would equate to **over $4 billion**. |
| 2013 | **Joint Basing** (Area 20): A plan to achieve the efficiencies and cost savings envisioned from joint bases, coupled with a reevaluation of associated goals and guidance, could lead to greater consolidation of installation services at joint bases and better position DOD to achieve its identified goals. |
| 2012 | **Military Health Care Costs** (Area 36): To help achieve significant projected cost savings and other performance goals, DOD needs to complete, implement, and monitor detailed plans for each of its approved health care initiatives. |
| 2011 | **Military Personnel Costs** (Area 37): A total compensation approach would be needed to manage military personnel costs—which grew 31 percent from fiscal year 2001 to fiscal year 2014. |
| **Information Technology** | |
| 2014 | **Information Technology Investment Portfolio Management** (Area 24): The Office of Management and Budget and multiple agencies could help the federal government realize **billions of dollars** in savings by taking steps to better implement PortfolioStat, a process to help agencies manage their information technology (IT) investments. |
| 2011 | **Federal Data Centers** (Area 15): Consolidating federal data centers would provide an opportunity to improve government efficiency and achieve cost savings and avoidances of **about $5.3 billion** by fiscal year 2017. |
| 2013 | **Information Technology Operations and Maintenance** (Area 30): Strengthening oversight of key federal agencies' major IT investments in operations and maintenance would provide an opportunity for **savings on billions** in IT investments. |

| Annual report | Areas identified |
|---|---|
| 2011 | **Enterprise Architecture** (Area 14): Well-defined and implemented enterprise architectures in federal agencies can lead to consolidation and reuse of shared services and elimination of antiquated and redundant mission operations, which can result in significant cost savings. For example, the Department of the Interior demonstrated that it had used enterprise architecture to modernize agency IT operations and avoid costs through enterprise software license agreements and hardware procurement consolidation, resulting in financial savings of **at least $80 million**. In addition, the Department of Health and Human Services (HHS) will achieve savings and cost avoidance of **over $150 million** during fiscal years 2011–2015 by leveraging its enterprise architecture to improve its telecommunications infrastructure. |
| **Energy and Agriculture** | |
| 2011 | **Oil and Gas Resources** (Area 45): Improved management of federal oil and gas resources could result in approximately **$2 billion in additional revenue over 10 years**. |
| 2014 | **Advanced Technology Vehicles Manufacturing Loan Program** (Area 13): Unless the Department of Energy can demonstrate demand for new Advanced Technology Vehicles Manufacturing loans and viable applications, Congress may wish to consider rescinding all or part of the remaining **$4.2 billion** in credit subsidy appropriations. |
| 2013 | **Crop Insurance** (Area 19): To achieve **up to $1.2 billion per year in cost savings** in the crop insurance program, Congress could consider limiting the subsidy for premiums that are provided on behalf of individual farmers, reducing the subsidy for all or high-income farmers participating in the program, or some combination of limiting and reducing these subsidies. |
| **Health Care** | |
| 2014 | **Medicaid Demonstration Waivers** (Area 21): Federal spending on Medicaid demonstrations could be reduced if HHS were required to improve the process for reviewing, approving, and making transparent the basis for spending limits approved for Medicaid demonstrations. We estimated the federal share of savings could have been **up to $21 billion over 5 years** for two states' recent demonstrations that we reviewed. |
| 2012 | **Medicare and Medicaid Fraud Detection Systems** (Area 46): The Centers for Medicare & Medicaid Services would need to ensure widespread use of its fraud detection systems to better position itself to determine and measure progress toward achieving the **$21 billion** in financial benefits that the agency projected as a result of implementing these systems. |
| **Taxes** | |
| 2014 | **Collection of Unpaid Federal Taxes** (Area 15): The federal government could increase tax revenue collections by **$500 million over a 5-year time period**, according to a 2012 Congressional Budget Office estimate, by identifying and taking actions to limit issuance of passports to applicants with unpaid federal taxes. |
| 2013 | Tobacco Taxes (Area 31): Federal revenue losses ranged from as much as **$615 million to $1.1 billion between April 2009 and 2011** because manufacturers and consumers substituted higher-taxed smoking tobacco products with similar lower-taxed products. To address future revenue losses, Congress should consider modifying tobacco tax rates to eliminate significant tax differentials between similar products. |
| 2011 | **Simple Tax Return Error** (Araa 56): Congress could grant the Internal Revenue Service (IRS) broader authority, with appropriate safeguards against misuse of that authority, to correct math errors during tax return processing. In April 2014, the Joint Committee on Taxation estimated that this change could result in **$161 million in savings**. |

| Annual report | Areas identified |
|---|---|
| **Fees** | |
| 2013 | **Agricultural Quarantine Inspection Fees** (Area 18): The United States Department of Agriculture's Animal and Plant Health Inspection Service could have achieved as much as **$325 million in savings** (based on fiscal year 2011 data, as reported) by more fully aligning fees with program costs; although the savings would be recurring, the amount would depend on the cost-collections gap in a given fiscal year and would result in a reduced reliance on U.S. Customs and Border Protection's annual Salaries and Expenses appropriations used for agricultural inspection services. |
| 2012 | **Immigration Inspection Fee** (Area 49): The user fee for immigration inspection of air and sea passengers should be reviewed and adjusted to fully recover the cost of the air and sea passenger immigration inspection activities conducted by the Department of Homeland Security's U.S. Immigration and Customs Enforcement and U.S. Customs and Border Protection rather than relying on general fund appropriations; in 2012 this could have resulted in reduced reliance on general fund appropriations used for inspection services by about $175 million. |
| **Homeland Security** | |
| 2012 | **Domestic Disaster Assistance** (Area 51): The Federal Emergency Management Agency (FEMA) could reduce the costs to the federal government related to major disasters declared by the President by updating the principal indicator on which disaster funding decisions are based and better measuring a state's capacity to respond without federal assistance. For fiscal years 2004 through 2011, had FEMA adjusted the indicator for increases in inflation or personal income since 1986, fewer jurisdictions would have met the eligibility criteria for federal assistance and federal costs could have been **as much as $3.59 billion lower**. |
| 2013 | Checked Baggage Screening (Area 28): By reviewing the appropriateness of the federal cost share the Transportation Security Administration (TSA) applies to agreements that finance modification projects related to the installation of checked baggage screening systems at airport facilities, TSA could, if a reduced cost share were deemed appropriate, achieve cost efficiencies of **up to $300 million by 2030** and be positioned to install a greater number of optimal baggage screening systems than currently anticipated. |
| **Income Security** | |
| 2011 | **Social Security Offsets** (Area 80): Social Security needs data on pensions from noncovered earnings to better enforce offsets and ensure benefit fairness, which could result in an estimated **$2.4 billion–2.9 billion in savings over 10 years**. |
| 2014 | **Disability and Unemployment Benefits** (Area 8): Congress should consider passing legislation to prevent individuals from collecting both full Disability Insurance benefits and Unemployment Insurance benefits that cover the same period, which could save **$1.2 billion over 10 years** in the Social Security Disability Insurance program according to the Congressional Budget Office. |
| 2014 | **Veterans' and Survivors' Benefits** (Area 23): The Department of Veterans Affairs' direct spending could be reduced—by an average of **about $4 million annually**, according to the Congressional Budget Office—if new statutory provisions were enacted, namely, a look-back review and penalty period for claimants who transfer assets for less than fair market value before applying for pension benefits that are available to low-income wartime veterans who are at least 65 years old or have disabilities unrelated to their military service. |

Source: GAO. | GAO-15-440T

## Tools Exist to Help Address Issues of Fragmentation, Overlap, and Duplication

Addressing fragmentation, overlap, and duplication within the federal government is challenging. Even with sustained leadership, these are difficult issues to address because they may require agencies and Congress to re-examine (within and across various mission areas) the fundamental structure, operation, funding, and performance of a number of long-standing federal programs or activities with entrenched constituencies. As we have previously reported, these challenges are compounded by a lack of reliable budget and performance information. If fully and effectively implemented, the GPRA Modernization Act of 2010 (GPRAMA) and the Digital Accountability and Transparency of 2014 (DATA Act) hold promise for helping to improve performance and budget information and helping to address challenges in identifying and addressing areas of fragmentation, overlap, and duplication. In particular:

- GPRAMA establishes a framework aimed at taking a more crosscutting and integrated approach to focusing on results and improving government performance. Effective implementation of GPRAMA could help clarify desired outcomes, address program performance spanning multiple organizations, and facilitate future actions to reduce, eliminate, or better manage fragmentation, overlap, and duplication.[23]

- The DATA Act requires actions that would help make spending data comparable across programs, allowing executive branch agencies and Congress to accurately measure the costs and magnitude of federal investments. As we have previously reported, better data and a greater focus on expenditures and outcomes are essential to improving the efficiency and effectiveness of federal efforts.

[23]In one example of how GPRAMA could help facilitate a more crosscutting approach focused on results, the act requires OMB to coordinate with executive branch agencies to establish crosscutting priority goals and develop a federal government performance plan that defines the level of performance needed to achieve them. In March 2014, OMB released an updated list of cross-agency priority goals and plans to track progress in achieving these goals on a quarterly basis on Performance.gov. The crosscutting approach required by the act will provide a much-needed basis for more fully integrating a wide array of federal activities as well as a cohesive perspective on the long-term goals of the federal government that is focused on priority policy areas. It also could be a valuable tool for re-examining existing programs government-wide and for considering proposals for new programs.

We are committed to monitoring the implementation of these acts to improve budget and performance information and help executive branch agencies and Congress address fragmentation, overlap, and duplication.

## Addressing Improper Payments Could Help Achieve Cost Savings

Reducing improper payments could result in significant cost savings. The Improper Payments Information Act of 2002 (IPIA)—as amended by the Improper Payments Elimination and Recovery Act of 2010 (IPERA) and the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA)—requires executive branch agencies to (1) review all programs and activities, (2) identify those that may be susceptible to significant improper payments, (3) estimate the annual amount of improper payments for those programs and activities, (4) implement actions to reduce improper payments and set reduction targets, and (5) report on the results of addressing the foregoing requirements.[24]

For the first time in recent years, the government-wide improper payment estimate increased in fiscal year 2014, primarily due to significant increases in the improper payment estimates for Medicare, Medicaid, and the Earned Income Tax Credit (EITC). These programs combined account for over 76 percent of the government-wide estimate. We have made numerous recommendations that if effectively implemented, could help improve program management, reduce improper payments in these programs, and achieve cost savings. While recent laws and guidance have focused attention on the issue, agencies continue to face challenges in reducing improper payments, such as statutory limitations and compliance issues.

### Improper Payments Remain a Government-Wide Issue

Agency improper payment estimates totaled $124.7 billion in fiscal year 2014, a significant increase ($19 billion) from the prior year's estimate of $105.8 billion. The estimated improper payments for fiscal year 2014 were attributable to 124 programs spread among 22 agencies. Table 5 shows the 12 programs with reported improper payment estimates

[24]IPIA, Pub. L. No. 107-300, 116 Stat. 2350 (Nov. 26, 2002), *as amended by* IPERA, Pub. L. No. 111-204, 124 Stat. 2224 (July 22, 2010), *and* IPERIA, Pub. L. No. 112-248, 126 Stat. 2390 (Jan. 10, 2013), *and codified as amended at* 31 U.S.C. § 3321 note. For fiscal year 2014 and beyond, IPIA, as amended, defines "significant improper payments" as gross annual improper payments in the program exceeding (1) both 1.5 percent of program outlays and $10 million of all program or activity payments during the fiscal year reported or (2) $100 million (regardless of the improper payment error rate).

exceeding $1 billion for fiscal year 2014, which accounted for approximately 93 percent of the government-wide estimate.

**Table 5: Programs with Improper Payment Estimates Exceeding $1 Billion in Fiscal Year 2014**

| | | Fiscal year 2014 reported improper payment estimates | |
|---|---|---|---|
| **Program** | **Agency** | **Dollars (in millions)** | **Error rate (percentage of outlays)** |
| Medicare | Department of Health and Human Services (HHS) | $59,914 | — |
| *Medicare Fee-for-Service (Parts A and B)* | *HHS* | *45,754* | *12.7%* |
| *Medicare Advantage (Part C)* | *HHS* | *12,229* | *9.0%* |
| *Medicare Prescription Drug (Part D)* | *HHS* | *1,931* | *3.3%* |
| Earned Income Tax Credit | Department of the Treasury | 17,700 | 27.2% |
| Medicaid | HHS | 17,492 | 6.7% |
| Unemployment Insurance | Department of Labor | 5,604 | 11.6% |
| Supplemental Security Income | Social Security Administration (SSA) | 5,107 | 9.2% |
| Old Age, Survivors, and Disability Insurance | SSA | 3,000 | 0.4% |
| Supplemental Nutrition Assistance Program | Department of Agriculture (USDA) | 2,437 | 3.2% |
| School Lunch | USDA | 1,748 | 15.3% |
| Direct Loan | Department of Education | 1,532 | 1.5% |
| Public Housing / Rental Assistance | Department of Housing and Urban Development | 1,029 | 3.2% |

Source: GAO summary of agencies' data. | GAO-15-440T

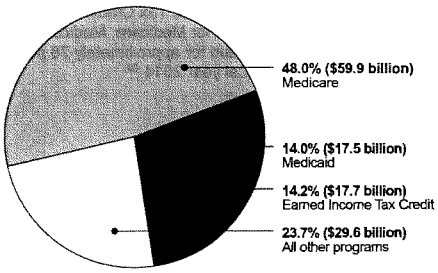
When excluding DOD's Defense Finance and Accounting Service Commercial Pay program, the reported government-wide error rate was 4.5 percent of program outlays in fiscal year 2014 compared to 4.0

percent reported in fiscal year 2013.[25] The increase in the 2014 estimate is attributed primarily to increased error rates in three major programs: HHS's Medicare Fee-for-Service, HHS's Medicaid, and Treasury's Earned Income Tax Credit. As shown in figure 2, improper payment estimates for Medicare, Medicaid, and the Earned Income Tax Credit accounted for approximately 76 percent of the government-wide estimate for fiscal year 2014.[26]

[25]In February 2015, we reported concerns that the fiscal year 2014 improper payment estimate for DOD's Defense Finance and Accounting Service (DFAS) Commercial Pay program may not be reliable. The foundation of reliable statistical sampling estimates is a complete, accurate, and valid population from which to sample. Because of long-standing financial management weaknesses, DOD reported in its fiscal year 2014 agency financial report that it could not demonstrate that all payments subject to improper payment estimation requirements were included in the population of payments for review. Therefore, the fiscal year 2014 improper payment estimate for the DFAS Commercial Pay program may not be reliable. When including the DFAS Commercial Pay program, the government-wide improper payment error rate was 4.0 percent of program outlays in fiscal year 2014, an increase from 3.5 percent in fiscal year 2013. See GAO, *Financial Audit: U.S. Government's Fiscal Years 2014 and 2013 Consolidated Financial Statements*, GAO-15-341R (Washington, D.C.: Feb. 26, 2015).

[26]Medicare consists of four parts. Parts A and B are known as Medicare Fee-for-Service. Part A covers hospital and other inpatient stays, and Part B covers hospital outpatient, physician, and other services. Part C, also known as Medicare Advantage, is the private plan alternative to Medicare Fee-for-Service under which beneficiaries receive benefits through private health plans. Part D is the outpatient prescription drug benefit.

**Figure 2: Government-Wide Improper Payment Estimates by Program for Fiscal Year 2014**




Source: GAO analysis of agencies' data. | GAO-15-440T

## Additional Efforts Are Needed to Reduce Medicare, Medicaid, and Earned Income Tax Credit Improper Payments

Improper payment estimates for Medicare, Medicaid, and the EITC are among the highest estimates government-wide, and federal spending in Medicare and Medicaid is expected to significantly increase.[27] Consequently, it is critical that actions are taken to reduce improper payments in these programs. Over the past several years, we made numerous recommendations that, if effectively implemented, could improve program management, help reduce improper payments in these programs, and achieve cost savings.

### Medicare

In fiscal year 2014, Medicare financed health services for approximately 54 million elderly and disabled beneficiaries at a cost of $603 billion and reported an estimated $60 billion in improper payments. Medicare spending generally has grown faster than the economy, and in the coming years, continued growth in the number of Medicare beneficiaries and in program spending will create increased challenges for the federal government. CMS, which administers Medicare, has demonstrated strong

[27]Based on projections reported in HHS's fiscal year 2014 agency financial report, total outlays for the Medicare and Medicaid programs are expected to increase, on average, by 8.6 percent per year over the next 3 years.

commitment to reducing improper payments, particularly through its dedicated Center for Program Integrity. For example, CMS centralized the development and implementation of automated edits—prepayment controls used to deny Medicare claims that should not be paid—which will help ensure greater consistency in paying only those claims that align with national policies. Additionally, CMS awarded a contract to a Federal Bureau of Investigation-approved contractor that will enable the agency to conduct fingerprint-based criminal history checks of high-risk providers and suppliers.

Nevertheless, in our February 2015 update to our high-risk series, we reported that while CMS has demonstrated efforts to reduce improper payments in the Medicare program, improper payment rates have remained unacceptably high.[28] To achieve and demonstrate reductions in the amount of Medicare improper payments, CMS should fully exercise its authority related to strengthening its provider and supplier enrollment provisions and address our open recommendations related to prepayment and postpayment claims review activities. Table 6 summarizes recommendations we made that are still open and procedures authorized by the Patient Protection and Affordable Care Act (PPACA) that CMS should implement to help reduce Medicare improper payments.[29]

**Table 6: Actions That Could Help Reduce Medicare Improper Payments**

| GAO report | Recommendation |
|---|---|
| GAO-14-474 | Monitor the database used to track recovery audit activities to ensure that all postpayment review contractors submit required data and that the data in the database are accurate and complete. |
| GAO-14-111 | Develop performance measures for the Zone Program Integrity Contractors who explicitly link their work to the agency's Medicare Fee-for-Service program integrity performance measures and improper payment reduction goals.[a] |

[28]GAO-15-290.

[29]Pub. L. No. 111-148, 124 Stat. 119 (2010), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010). In this statement, references to "PPACA" include amendments made by the Health Care and Education Reconciliation Act of 2010.

| GAO report | Recommendation |
|---|---|
| GAO-13-761 | Efficiently and cost-effectively identify, design, develop, and implement an information technology solution that addresses the removal of Social Security numbers from the health insurance cards of Medicare beneficiaries. |
| GAO-13-522 | Reduce differences between contractor postpayment review requirements, when possible. |
| GAO-13-102 | Improve automated edits that assess all quantities provided to the same beneficiary by the same provider on the same day, so providers cannot avoid claim denials by billing for services on multiple claim lines or multiple claims. |
| GAO-13-102 | Require Medicare administrative contractors to share information about the underlying policies and savings related to their most effective edits. |
| **Source** | **Action** |
| PPACA | Require a surety bond for certain types of at-risk providers and suppliers. |
| PPACA | Publish a proposed rule for increased disclosures of prior actions taken against providers and suppliers enrolling or revalidating enrollment in Medicare, such as whether the provider or supplier has been subject to a payment suspension from a federal health care program. |
| PPACA | Establish core elements of compliance programs for providers and suppliers. |

Legend: PPACA = Patient Protection and Affordable Care Act.

Source: GAO summary of prior GAO reports. | GAO-15-440T

[a]Zone Program Integrity Contractors are responsible for identifying potential fraud, investigating it thoroughly and in a timely manner, and taking swift action—such as working to revoke suspect providers' Medicare billing privileges or referring such providers to law enforcement.

Specifically, the following actions could help reduce Medicare improper payments.

- **Improving use of automated edits.** To help ensure that payments are made properly, CMS uses controls called edits that are programmed into claims processing systems to compare claims data with Medicare requirements in order to approve or deny claims or flag them for further review. In November 2012, we reported that use of prepayment edits saved Medicare at least $1.76 billion in fiscal year 2010, but savings could have been greater if prepayment edits had been more widely used.[30] To promote greater use of effective prepayment edits and better ensure that payments are made properly, we recommended that CMS require Medicare administrative

[30]GAO, *Medicare Program Integrity: Greater Prepayment Control Efforts Could Increase Savings and Better Ensure Proper Payment*, GAO-13-102 (Washington, D.C.: Nov. 13, 2012).

contractors to (1) share information about the underlying policies and savings related to their most effective edits; and (2) improve automated edits that assess all quantities provided to the same beneficiary by the same provider on the same day, so providers cannot avoid claim denials by billing for services on multiple claim lines or multiple claims.

- **Monitoring postpayment claims reviews**. CMS uses four types of contractors to conduct postpayment claims reviews to identify improper payments. In July 2013, we found that although postpayment claims reviews involved the same general process regardless of which type of contractor conducted them, CMS had different requirements for many aspects of the process across the four contractor types.[31] Some of these differences might impede efficiency and effectiveness of claims reviews by increasing administrative burden for providers. Furthermore, in July 2014, we reported that while CMS had taken steps to prevent its contractors from conducting certain duplicative postpayment claims reviews, CMS did not have reliable data or provide sufficient oversight and guidance to measure and fully prevent duplication.[32] To improve the efficiency and effectiveness of Medicare program integrity efforts, we recommended that CMS reduce differences between contractor postpayment review requirements, when possible, and monitor the database used to track recovery audit activities to ensure that all data were submitted, accurate, and complete.

- **Removing Social Security numbers from Medicare cards**. The health insurance claims number on Medicare beneficiaries' cards includes as one component the Social Security number of the beneficiary (or other eligible person's, such as a spouse). This introduces risks that the beneficiaries' personal information could be obtained and used to commit identity theft. In September 2013, we reported that CMS had not taken needed steps that would result in selecting and implementing a technical solution for removing Social

[31]GAO, *Medicare Program Integrity: Increasing Consistency of Contractor Requirements May Improve Administrative Efficiency*, GAO-13-522 (Washington, D.C.: July 23, 2013).

[32]GAO, *Medicare Program Integrity: Increased Oversight and Guidance Could Improve Effectiveness and Efficiency of Postpayment Claims Reviews*, GAO-14-474 (Washington, D.C.: July 18, 2014).

Security numbers from Medicare cards.[33] To better position the agency to efficiently and cost-effectively identify, design, develop, and implement a solution to address this issue, we recommended that CMS direct the initiation of an IT project for identifying, developing, and implementing changes that would have to be made to CMS's affected systems.

- **Implementing actions authorized by PPACA**. In addition to provisions to expand health insurance coverage, PPACA provides CMS with certain authorities to combat fraud, waste, and abuse in Medicare. We reported in our February 2015 update to our high-risk series that CMS should fully exercise its PPACA authority related to strengthening its provider and supplier enrollment provisions.[34] For example, CMS should require surety bonds—a three-party agreement in which a company, known as a surety, agrees to compensate the bondholder if the bond purchaser failed to keep a specified promise—for certain providers and suppliers.

## Medicaid

In fiscal year 2014, the federal share of estimated Medicaid outlays was $304 billion, and HHS reported approximately $17.5 billion in estimated Medicaid improper payments. The size and diversity of the Medicaid program make it particularly vulnerable to improper payments—including payments made for people not eligible for Medicaid or for services not actually provided. CMS has an important role in overseeing and supporting state efforts to reduce and recover improper payments and has demonstrated some leadership commitment in this area. For example, CMS issued guidance to improve corrective actions taken by states. CMS also established the Medicaid Integrity Institute, which provides training and technical assistance to states on approaches to prevent improper payments and guidance on program integrity issues.

In our February 2015 high-risk update, we reported that while CMS had taken these positive steps in recent years, in several areas, CMS had still to address issues and recommendations that had not been fully implemented.[35] These issues include improving the completeness and

[33]GAO, *Medicare Information Technology: Centers for Medicare and Medicaid Services Needs to Pursue a Solution for Removing Social Security Numbers from Cards*, GAO-13-761 (Washington, D.C.: Sept. 10, 2013).

[34]GAO-15-290.

[35]GAO-15-290.

reliability of key data needed for ensuring effective oversight, implementing effective program integrity processes for managed care, ensuring clear reporting of overpayment recoveries, and refocusing efforts on approaches that are cost-effective. Table 7 summarizes recommendations we made that remain open and that CMS should implement to help reduce Medicaid improper payments.

**Table 7: Actions That Could Help Reduce Medicaid Improper Payments**

| GAO report | Recommendations to CMS |
|---|---|
| GAO-15-208 | Oversee and support state third-party liability efforts to routinely monitor and share across all states information regarding key third-party liability efforts and challenges. |
| GAO-15-208 | Oversee and support state third-party liability efforts to provide guidance to states on oversight of third-party liability efforts conducted by Medicaid managed care plans. |
| GAO-14-341 | Hold states accountable for Medicaid managed care program integrity by requiring states to conduct audits of payments to and by managed care organizations. |
| GAO-14-341 | Update Medicaid managed care guidance on program integrity practices and effective handling of managed care organization recoveries. |
| GAO-14-341 | Provide the states with additional support in overseeing Medicaid managed care program integrity, such as the option to obtain audit assistance from existing Medicaid integrity contractors. |
| GAO-13-50 | Use the knowledge gained from the comprehensive reviews as a criterion for focusing audit resources toward states that have structural or data analysis vulnerabilities. |
| GAO-13-50 | Reevaluate the agency's methodology for calculating a return on investment for the Medicaid Integrity Program, including reporting and sharing its methodology with Congress and the states. |
| GAO-13-50 | Increase the agency's efforts to hold states accountable for reliably reporting program integrity recoveries as a part of their quarterly expenditure reporting. |

Source: GAO summary of prior GAO reports. | GAO-15-440T

Specifically, we recommended the following actions to help reduce Medicaid improper payments and improve program integrity.

- **Improving third-party liability efforts**. Congress generally established Medicaid as the health care payer of last resort, meaning that if enrollees have another source of health care coverage—such as private insurance—that source should pay, to the extent of its liability, before Medicaid does. This is referred to as third-party liability. However, there are known challenges to ensuring that

Medicaid is the payer of last resort. For example, states have reported challenges working with private insurers, including willingness to release coverage information to states and denying claims for procedural reasons. While CMS has issued guidance to states, we recommended additional actions that could help to improve cost-saving efforts in this area, such as monitoring and sharing information on third-party liability efforts and challenges across all states and providing guidance to states on oversight of third-party liability efforts related to Medicaid managed care plans.[36]

- **Increasing oversight of managed care**. Medicaid finances the delivery of health care services to beneficiaries through fee-for-service payments to participating providers and capitated payments to managed care organizations.[37] Most Medicaid beneficiaries are in managed care, and managed care expenditures have been growing at a faster rate than fee-for-service expenditures. In May 2014, we reported that most state and federal program integrity officials we interviewed told us that they did not closely examine managed care payments, focusing on fee-for-service claims instead.[38] To help improve the efficiency and effectiveness of program integrity efforts, we recommended that CMS require states to conduct audits of payments to and by managed care organizations, update managed care guidance on program integrity practices, and provide states with additional support in overseeing managed care program integrity.

- **Strengthening program integrity**. CMS has taken positive steps to oversee program integrity efforts in Medicaid, including implementing certain recommendations we made.[39] CMS needs to take action to address issues and recommendations that have not been fully

[36]GAO, *Medicaid: Additional Federal Action Needed to Further Improve Third-Party Liability Efforts*, GAO-15-208 (Washington, D.C.: Jan. 28, 2015).

[37]Under a fee-for-service system, health care providers claim reimbursement from state Medicaid programs for services rendered to Medicaid beneficiaries. Under a Medicaid managed care system, states contract with managed care organizations to provide or arrange for medical services and prospectively pay the organizations a per person, or capitated, payment.

[38]GAO, *Medicaid Program Integrity: Increased Oversight Needed to Ensure Integrity of Growing Managed Care Expenditures*, GAO-14-341 (Washington, D.C.: May 19, 2014).

[39]GAO, *Medicaid Integrity Program: CMS Should Take Steps to Eliminate Duplication and Improve Efficiency*, GAO-13-50 (Washington, D.C.: Nov. 13, 2012).

implemented, such as improving reporting of key data, strengthening its efforts to calculate return on investment for its program integrity efforts, and using knowledge gained from its comprehensive reviews of states to better focus audit resources and improve recovery of improper payments.

## Earned Income Tax Credit

In fiscal year 2014, IRS reported program payments of $65.2 billion for the EITC.[40] According to IRS, an estimated 27.2 percent, or $17.7 billion, of these program payments were improper.[41] The estimated improper payment rate for EITC has remained relatively unchanged since fiscal year 2003 (the first year IRS had to report estimates of these payments to Congress), but the amount of improper EITC payments increased from an estimated $10.5 billion in fiscal year 2003 to nearly $18 billion in fiscal year 2014.

We have highlighted the persistent problems with improper EITC payments for years, and it is a factor underlying our continued designation of IRS Enforcement of Tax Laws as a high-risk area.[42] As we have reported, a root cause of EITC noncompliance is the self-determination of eligibility by taxpayers (or their preparer) combined with IRS's limited ability to verify eligibility before payments (refunds) are issued. According to Treasury, EITC improper payments can be divided into two categories—authentication and verification.[43] Authentication errors include errors associated with IRS's inability to validate qualifying

[40]Congress established EITC in 1975. It is used to (1) offset the impact of Social Security taxes on low-income families and (2) encourage low-income families to seek employment rather than public assistance. EITC eligibility depends on an individual's earned income. Credit amounts depend on the number of qualifying children who meet age, relationship, and residency tests. The credit gradually increases with income (the phase-in range), plateaus at a maximum amount (the plateau range), and then gradually decreases until it reaches zero (the phase-out range). For EITC, program payments include tax expenditures (a tax credit that offsets income taxes) and outlays (a refund if the credit exceeds the amount of taxes owed).

[41]EITC overpayments are the difference between the EITC amount claimed by the taxpayer on his or her return and the amount the taxpayer should have claimed. EITC underpayments are defined as the amount of EITC disallowed by IRS in processing that should have been allowed.

[42]GAO-15-290.

[43]Treasury Inspector General for Tax Administration, *Existing Compliance Processes Will Not Reduce the Billions of Dollars in Improper Earned Income Tax Credit and Additional Child Tax Credit Payments*, Reference Number 2014-40-093 (Washington, D.C.: Sept. 29, 2014).

child requirements, taxpayers' filing status, and EITC claims associated with complex or nontraditional living situations. Verification errors relate to IRS's inability to identify individuals improperly reporting income to erroneously claim EITC amounts to which they are not entitled. Verification errors include underreporting and overreporting of income by wage earners as well as taxpayers who report that they are self-employed. Although the EITC program has been modified a number of times since its enactment in 1975 to reduce complexity and help improve the program's administration, complexity has remained a key factor contributing to improper payments in the program.

IRS has undertaken a number of compliance and enforcement activities to reduce EITC improper payments, and in fiscal year 2014 it protected an estimated $3.5 billion in federal revenue.[44] Among other things, IRS uses audits to help identify EITC improper payments, and in June 2014, we reported that about 45 percent of correspondence audits (audits done by mail) that closed in fiscal year 2013 focused on EITC issues.[45] IRS has reported that tax returns with EITC claims were twice as likely to be audited as other tax returns. However, we found that the effectiveness of these audits may be limited because of regular backlogs in responding to taxpayers since 2011 and unclear correspondence that generated additional work for IRS, such as telephone calls to IRS examiners. These issues have imposed unnecessary burdens on taxpayers and costs for IRS. IRS acknowledged these concerns and the limitations faced in significantly reducing EITC improper payments using the traditional audit process. Consequently, IRS initiated several programs to address EITC improper payments, such as increasing outreach and education to taxpayers and return preparers.

Legislative action and significant changes in IRS compliance processes likely would be necessary to make any meaningful reduction in improper payments. Recently, we recommended matters for congressional consideration or executive actions that if effectively implemented, could help to reduce EITC improper payments.

[44]Protected revenue refers to the total value of erroneous payments prevented or recovered through compliance activities.

[45]GAO, *IRS Correspondence Audits: Better Management Could Improve Tax Compliance and Reduce Taxpayer Burden*, GAO-14-479 (Washington, D.C.: June 5, 2014).

- **Regulating paid tax preparers**. In August 2014, IRS reported that 68 percent of all tax returns claiming the EITC in tax years 2006 and 2007 were prepared by paid tax preparers—most of whom were not subject to any IRS regulation—and that from 43–50 percent of the returns overclaimed the credit.[46] Similarly, in our undercover visits to randomly selected tax preparers, a sample that cannot be generalized, we found errors in EITC claims, resulting in significant overstatement of refunds.[47] Establishing requirements for paid tax return preparers could improve the accuracy of the tax returns they prepare. Based in part on our recommendation, in 2010 IRS initiated steps to regulate certain preparers through testing and education requirements. However, the courts ruled that IRS lacked such regulatory authority. Although IRS began a voluntary program to recognize preparers who complete continuing education and testing requirements, mandating these requirements could have a greater impact on tax compliance. In 2014, we suggested that Congress consider granting IRS the authority to regulate paid tax preparers, if it agrees that significant paid preparer errors exist.

- **Accelerating W-2 filing deadlines**. IRS estimates that it paid $5.8 billion in fraudulent identity theft refunds during the 2013 filing season.[48] While we do not know the extent to which invalid EITC payments are the result of identity theft, IRS has reported that improper payments are a mix of unintentional mistakes and fraud. A common EITC error is misreporting income. IRS issues most refunds months before receiving and matching information returns, such as the W-2 "Wage and Tax Statement," to tax returns. Treasury recently proposed to Congress that the W-2 deadlines be moved to January 31 to facilitate the use of earnings information in the detection of

[46]Internal Revenue Service, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006- 2008 Returns*, Publication 5162 (8-2014) (Washington, D.C.: August 2014).

[47]GAO, *Paid Tax Return Preparers: In a Limited Study, Preparers Made Significant Errors*, GAO-14-467T (Washington, D.C.: Apr. 8, 2014), and *Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Significant Errors*, GAO-06-563T (Washington, D.C.: Apr. 4, 2006).

[48]GAO, *Identity and Tax Fraud: Enhanced Authentication Could Combat Refund Fraud, but IRS Lacks an Estimate of Costs, Benefits and Risks*, GAO-15-119 (Washington, D.C.: Jan. 20, 2015).

noncompliance.[49] In August 2014, we recommended that IRS estimate the cost and benefits of options to implement pre-refund matching using W-2 data.[50] Because any change could impose burdens on employers and taxpayers as well as create additional costs to IRS for systems and process changes, Congress and other stakeholders would need information on this impact to fully assess any potential changes.

- **Broadening math error authority**. IRS has statutory authority—called math error authority—to correct certain errors, such as calculation mistakes or omitted or inconsistent entries, during tax return processing of EITC claims. According to the Treasury Inspector General for Tax Administration, IRS has math error authority to address some erroneous claims, but additional authority to systematically disallow certain erroneous EITC claims with unsupported wages could reduce improper payments.[51] Treasury has proposed expanding IRS authority to permit it to correct errors in cases where information provided by the taxpayer does not match information in government databases among other things. Expanding such authority—which at various times we have suggested Congress consider—could help IRS correct additional errors and avoid burdensome audits and taxpayer penalties.

## Recent Efforts Focused Attention on Improper Payments, but Challenges Remain in Estimating and Reducing Them

IPERIA is the latest in a series of laws aimed at reducing improper payments. IPERIA directs OMB to annually identify a list of high-priority programs for greater levels of oversight and review, including establishing annual targets and semi-annual or quarterly actions for reducing improper payments. IPERIA also enacted into law a Do Not Pay initiative, elements of which already were being developed under executive branch authority. The Do Not Pay initiative is a web-based, centralized data-matching service that allows agencies to review multiple databases to determine a recipient's award or payment eligibility prior to making payments.

[49]By law, employers have until February 28 to file W-2 information on paper and until March 31 to file W-2 information electronically, except when those deadlines fall on a weekend or federal holiday. In that case, the deadline is the next federal business day.

[50]GAO, *Identity Theft: Additional Actions Could Help IRS Combat the Large, Evolving Threat of Refund Fraud*, GAO-14-633 (Washington, D.C.: Aug. 20, 2014).

[51]Treasury Inspector General for Tax Administration, *Existing Compliance Processes Will Not Reduce the Billions of Dollars in Improper Earned Income Tax Credit and Additional Child Tax Credit Payments*.

Similarly, the DATA Act calls on Treasury to establish a data analysis center, or to expand an existing service, to provide data, analytic tools, and data-management techniques for preventing or reducing improper payments.[52] Effective implementation of the DATA Act and the use of data analytic tools could help agencies to detect, reduce, and prevent improper payments.

In addition to these legislative initiatives, OMB has continued to play a key role in the oversight of government-wide improper payments. OMB established guidance for federal agencies on reporting, reducing, and recovering improper payments as required by IPIA, as amended, and on protecting privacy while reducing improper payments with the Do Not Pay initiative.[53] For example, the most recent revision to OMB's guidance for estimating improper payments directs agencies to report on the causes of improper payments using more detailed categories than previously required, such as program design issues or administrative errors at the federal, state, or local agency level. As we previously reported, detailed analysis of the root causes of improper payments can help agencies to identify and implement targeted corrective actions.[54]

While these efforts are a positive step toward estimating and reducing improper payments, agencies continue to face challenges in these areas. In our report on the Fiscal Year 2014 Financial Report of the United States Government, we identified the issue of improper payments as a material weakness in internal control because the federal government is unable to determine the full extent to which improper payments occur and reasonably assure that appropriate actions are taken to reduce them.[55] We found that not all agencies have developed improper payment

[52]Pub. L. No. 113-101, 128 Stat. 1146 (May 9, 2014) (*codified at* 31 U.S.C. § 6101 Note). The DATA Act amended the Federal Funding Accountability and Transparency Act of 2006.

[53]Office of Management and Budget, *Appendix C to Circular No. A-123, Requirements for Effective Estimation and Remediation of Improper Payments*, OMB Memorandum M-15-02 (Washington, D.C.: Oct. 20, 2014); Revised, *Financial Reporting Requirements*, OMB Circular No. A-136 (revised 2014); and *Protecting Privacy while Reducing Improper Payments with the Do Not Pay Initiative*, OMB Memorandum M-13-20 (Washington, D.C.: Aug. 16, 2013).

[54]GAO, *Improper Payments: Government-Wide Estimates and Reduction Strategies*, GAO-14-737T (Washington, D.C.: July 9, 2014).

[55]GAO-15-341R.

estimates for all of the programs and activities they identified as susceptible to significant improper payments. Specifically, two federal agencies did not report estimated improper payment amounts for four risk-susceptible programs. For example, HHS did not report an improper payment estimate in fiscal year 2014 for its Temporary Assistance for Needy Families (TANF) program, which had program outlays of about $16.3 billion.[56]

Furthermore, IPERA established a requirement for agency IGs to report annually on agencies' compliance with the criteria contained in IPERA. Under OMB implementing guidance, these reports should be completed within 180 days of the publication of the federal agencies' annual performance and accountability reports (PAR) or agency financial reports (AFR).[57] According to IPERA, if a program is found to be noncompliant

- in a fiscal year, the agency must submit a plan to Congress describing the actions that the agency will take to bring the program into compliance;
- for 2 consecutive fiscal years, and if OMB determines that additional funding would help the agency improve, the agency and OMB may take steps to transfer or request additional funding for intensified compliance efforts; and
- for 3 consecutive years, the agency must submit to Congress a reauthorization proposal for each noncompliant program or activity or any proposed statutory changes the agency deems necessary to bring the program or activity into compliance.

In December 2014, we reported on agency compliance with the criteria contained in IPERA for fiscal year 2013, as reported by IGs.[58] We found

[56]The three remaining risk-susceptible programs that did not report an improper payment estimate for fiscal year 2014 were in DHS—the Customs and Border Protection Administratively Uncontrollable Overtime, Port Security Grant, and Federal Emergency Management Agency Vendor Pay (non-Disaster Relief Fund) programs. DHS plans to report improper payment estimates for these programs in fiscal year 2015.

[57]Generally, agencies must issue their PARs or AFRs by November 15. Fiscal year 2013 was the third year for which IGs were required to issue annual reports on agencies' compliance with criteria listed in IPERA. IG reports on fiscal year 2014 compliance with the criteria listed in IPERA are generally expected to be issued by May 2015.

[58]GAO, *Improper Payments: Inspector General Reporting of Agency Compliance under the Improper Payments Elimination and Recovery Act*, GAO-15-87R (Washington, D.C.: Dec. 9, 2014).

that the most common instances of noncompliance as reported by the IGs related to two criteria: (1) publishing and meeting improper payment reduction targets and (2) reporting improper payment estimates below 10 percent.[59] For fiscal years 2012 through 2014, we also analyzed IG reports and agency PARs or AFRs and identified five programs with improper payment estimates greater than $1 billion that have been noncompliant with at least one of these criteria for 3 consecutive years, as show in table 8.[60] These five programs accounted for approximately $75.9 billion, or 61 percent of the fiscal year 2014 government-wide improper payment estimate.

**Table 8: Major Programs Noncompliant with Improper Payment Requirements for 3 Consecutive Years**

| | | Did not publish or meet reduction target | | | Reported error rate greater than 10 percent | | |
|---|---|---|---|---|---|---|---|
| Program | Agency | 2012 | 2013 | 2014 | 2012 | 2013 | 2014 |
| Medicare Fee-for-Service | Department of Health and Human Services | X | X | X | | X | X |
| Earned Income Tax Credit | Department of the Treasury | X[a] | X[a] | | X | X | X |
| Unemployment Insurance | Department of Labor | X | X | X[b] | X | [c] | X |
| Supplemental Security Income | Social Security Administration | X | X | X | | | |
| School Lunch | Department of Agriculture | | X | | X | X | X |

Source: GAO analysis of agency financial reports and inspectors general reports. | GAO-15-440T

[a]The Department of the Treasury did not set improper payment reduction targets for the Earned Income Tax Credit for fiscal years 2012 or 2013.

[b]The Department of Labor did not set a reduction target for fiscal year 2014 for the Unemployment Insurance program in its fiscal year 2013 agency financial report. However, according to

[59]IPERA contains six criteria for compliance. The six criteria are that the entity has (1) published an annual financial statement and accompanying materials in the form and content required by OMB for the most recent fiscal year and posted that report on the entity website; (2) conducted a risk assessment for each specific program or activity that conforms with IPIA, as amended; (3) published estimates of improper payments for all programs and activities identified as susceptible to significant improper payments under the entity's risk assessment; (4) published corrective action plans for programs and activities assessed to be at risk for significant improper payments; (5) published and met annual reduction targets for all programs and activities assessed to be at risk for significant improper payments; and (6) reported a gross improper payment rate of less than 10 percent for each program and activity for which an improper payment estimate was obtained and published.

[60]It is important to note that additional programs may have been noncompliant for 3 consecutive years when factoring in the remaining four criteria contained in IPERA.

Paymentaccuracy.gov—the federal website for improper payment information—the fiscal year 2014 reduction target for the Unemployment Insurance program was 10 percent, which the department did not meet.

[c]According to its Office of Inspector General, the Department of Labor used a methodology that reduced the improper payments by the amount of subsequent improper payment recoveries for fiscal year 2013. Without netting the subsequent recoveries, the error rate would have been 11.5 percent, exceeding 10 percent.

In addition to the legislative criteria, various IGs reported deficiencies in their most recent annual compliance reports, including risk assessments that may not accurately assess the risk of improper payments and estimation methodologies that may not produce reliable estimates. Similarly, we recently reported on weaknesses in improper payment risk assessments at the Department of Energy and in the estimating methodology for DOD's TRICARE program.[61]

In addition to the challenges that we and the IGs reported, some agencies reported in their fiscal year 2014 AFRs that program design issues could hinder efforts to estimate or recapture improper payments.

- **Coordination with states**. HHS cited statutory limitations for its state-administered TANF program, which prohibited it from requiring states to participate in developing an improper payment estimate for the program.[62] Despite these limitations, HHS reported that it had taken actions to assist states in reducing improper payments, such as working with states to analyze noncompliance findings from audits related to TANF and requiring more accurate information about the ways states used TANF block grants.

- **Recovery auditing**. USDA reported that section 281 of the Department of Agriculture Reorganization Act of 1994 precluded the use of recovery auditing techniques. Specifically, the agency reported that section 281 provides that 90 days after the decision of a state, a county, or an area committee is final, no action may be taken to recover the amounts found to have been erroneously disbursed as a

[61]GAO, *Improper Payments: DOE's Risk Assessments Should Be Strengthened*, GAO-15-36 (Washington, D.C.: Dec. 23, 2014), and *Improper Payments: TRICARE Measurement and Reduction Efforts Could Benefit from Adopting Medical Record Reviews*, GAO-15-269 (Washington, D.C.: Feb. 18, 2015). TRICARE is a health care program for military servicemembers, retirees, and their families.

[62]The term state-administered refers to federal programs that are managed on a day-to-day basis at the state level to carry out program objectives.

result of the decision, unless the participant had reason to believe that the decision was erroneous. This statute is commonly referred to as the Finality Rule, and according to USDA, it affects the Farm Service Agency's ability to recover overpayments.

With outlays for major programs, such as Medicare and Medicaid, expected to increase over the next few years, it is critical that actions are taken to reduce improper payments. In addition to agencies' efforts, legislation, OMB guidance, and auditor oversight of agency spending and related internal controls have been important factors in addressing improper payments. There is considerable opportunity here to achieve cost savings without reducing or detrimentally affecting the valuable programs that serve our citizens. For this reason, we will continue to focus attention on improper payments to assist Congress in ensuring that taxpayer dollars are adequately safeguarded and used for their intended purposes.

Chairman Enzi, Ranking Member Sanders, and Members of the Committee, this concludes my prepared statement. I would be pleased to answer questions.

## GAO Contacts

For further information on issues of fragmentation, overlap, duplication or cost savings, please contact Orice Williams Brown, Managing Director, Financial Markets and Community Investment, who may be reached at (202) 512-8678 or williamso@gao.gov; or A. Nicole Clowers, Director, Financial Markets and Community Investment, who may be reached at (202) 512-8678 or clowersa@gao.gov. For information on improper payment issues, please contact Beryl H. Davis, Director, Financial Management and Assurance at (202) 512-2623 or davisbh@gao.gov. Contact points for our Congressional Relations and Public Affairs offices may be found on the last page of this statement.

# Related GAO Products

*Improper Payments: TRICARE Measurement and Reduction Efforts Could Benefit from Adopting Medical Record Reviews.* GAO-15-269. Washington, D.C.: February 18, 2015.

High-Risk Series: An Update. GAO-15-290. Washington, D.C.: February 11, 2015.

*Medicaid: Additional Federal Action Needed to Further Improve Third-Party Liability Efforts.* GAO-15-208. Washington, D.C.: January 28, 2015.

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*Improper Payments: DOE's Risk Assessments Should Be Strengthened.* GAO-15-36. Washington, D.C.: December 23, 2014.

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*Medicare Program Integrity: Increasing Consistency of Contractor Requirements May Improve Administrative Efficiency.* GAO-13-522. Washington, D.C.: July 23, 2013.

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*2012 Annual Report: Opportunities to Reduce Duplication, Overlap and Fragmentation, Achieve Savings, and Enhance Revenue.* GAO-12-342SP. Washington D.C.: February 28, 2012.

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Chairman ENZI. Thank you for your information and even more so for all the information you collect that there would not be time for you to share with us here. But we have some people that are anxious to ask some questions, so I appreciate your brief comments.

We will be recognizing the members in their order of arrival after the gavel, so I get to start the questions.

We created a Bureau of Consumer Financial Protection which added another entity to the cluster of Federal agencies, although they are under the Federal Reserve and not technically under us, and we have no control over them whatsoever. In 2012, GAO recommended a prioritization and consolidation of the financial literacy programs and activities that are taking place in 14 different agencies. Last spring, GAO reported that the prioritization had yet to take place.

The CFPB is using its Civil Penalty Fund to pay for financial literacy programs. I believe GAO recently reviewed that fund and its expenditures. Has the CFPB appropriately documented the rationale for its expenditures on financial literacy programs? And do we know whether these new programs duplicate other programs being administered by the Federal agencies?

Mr. DODARO. First, with regard to our report on the Civil Penalty Fund, we found that the programs that were authorized under that fund were not properly documented. We made recommendations to the Consumer Financial Protection Bureau. They have adopted new procedures, but they have yet to approve any additional programs out of the Civil Penalty Fund, so we do not know how effective those procedures will be.

We have looked more broadly at the issue of potential duplication among the programs. We find a considerable amount of overlap between the programs, and for that reason, we suggest that the Consumer Financial Protection Bureau and Treasury, who are the Chair and Co-Chair of the financial group that oversees these literacy programs, prioritize the funding and look for opportunities to consolidate the programs. Those two recommendations have yet to be implemented.

Chairman ENZI. Okay. Thank you.

Switching over to the STEM education programs, we found that two-thirds have not undergone an evaluation between 2005 and 2011. How do we know how to consolidate the programs if we do not know which ones work and which ones do not? And are there other areas where we lack the data to determine whether the Federal programs are working?

Mr. DODARO. This is a very significant problem. In undertaking the work over the past 4 years, we found many Federal programs across a wide range of areas that really were lacking in evaluation to know what programs were working and what were not. STEM is one, as you mentioned. The programs for economic development, we found over 80 programs there, many of which were never evaluated to determine how effective they were.

In the teacher quality area, improving teacher quality, we found 82 programs at 10 Federal agencies. Many of them were too small to really be effectively evaluated. And we found problems in domestic food assistance. There were 18 programs there. The 7 largest

ones had some good evaluations, but 11 of the other ones did not. We recommended that the Agriculture Department look at consolidating some of these smaller programs into those areas.

So this is a very significant area. You mentioned, Mr. Chairman, there is not a good definition consistently applied to programs. There is really not a lot of good information about specific funding aligned with those programs and activities available, and even still we are lacking in the type of performance information that would enable Congress to make an informed decision.

However, there are some things that could be done. As you mentioned, in the STEM area they have begun consolidating particularly the smaller programs. I think you can do it and still provide effective coverage.

But I think the real question here is: Why would Congress want to continue funding programs that do not have a demonstrated track record of improving their objectives, achieving their objectives and having proper performance?

Chairman ENZI. I will change topics a little bit again, because in the 2011 and 2012 reports by your agency, you identified 94 Federal initiatives to promote green buildings in the non-Federal sector and recommended that agencies collaborate to identify inefficient or costly duplication.

Have the agencies made progress in that area? And do you have any idea the amount of funds that are allotted to those programs?

Mr. DODARO. Yes, they have taken some very limited steps to try to study the reporting in the non-Federal sector, but I am not satisfied that they are taking this very, very seriously and have come up with a plan to coordinate the Federal Government's activities in this area and to establish goals and performance metrics. In two-thirds of the 94 programs we looked at, they had no specific goals and metrics for the program, so we are kind of lacking in that. And there is no effective coordinating mechanism as there is on the Federal side. So this scenario I think warrants congressional attention and direction to the agency to implement our recommendation, and we really do not know how much money has been spent. We made an attempt to do this. Part of what is proposed with the green buildings, first, their definition of "green buildings" is a little loose, but also they fund it out of larger programs and really do not track specifically how much money goes to this particular area. Another opportunity, I think, for Congress to provide some direction.

Chairman ENZI. Thank you. My time has expired.

Senator Sanders?

Senator SANDERS. Thank you, Mr. Chairman.

Let me focus briefly on two areas. One is where in terms of discretionary spending we spend the most money, and I want to talk about money that we should be collecting that we are not.

Mr. Dodaro, according to a GAO analysis, $448 billion in cost overruns have been added to the Department of Defense's $1.5 trillion acquisition portfolio. That is a lot of money. In 2001, Secretary of Defense Donald Rumsfeld, not one of my favorite Secretaries of Defense, said—and he said this literally the day before 9/11, never got a whole lot of attention. But he spoke—I think it was at the Pentagon—and he said that the Pentagon could not account for some $2.3 trillion in transactions. Even here in D.C. that is a lot

of money. And yet 14 years later, the Pentagon still cannot pass an audit.

Now, explain to me what goes on when the agency that receives most of the discretionary spending, close to $600 billion, cannot give us an audit, has huge cost overruns, and then comes before us and tells us, gee, we need even more money? I was a mayor for eight years. That did not happen when I was a mayor. You hold people accountable. So we talk about accountability a lot. Tell me about accountability in the DOD and tell me about these huge cost overruns. Why do they happen? What do we do to end that practice?

Mr. DODARO. First, with regard to financial management at DOD, we put them—you mentioned our high-risk list. We put them on our high-risk list for financial management in 1995. The Congress passed legislation—before 1996, there was not a requirement to prepare financial statements and have them audited across the Federal Government. So in 1996, 6 of the 24 largest departments and agencies in the Federal Government were able to pass the test of an independent audit. Now virtually all the 24 agencies can pass the test of an audit except for the Defense Department. For many years, they did not focus a lot on this activity. They are focused now on auditing their budget numbers, and some of their attempts to audit budget numbers for multiple years have not been successful, so now they are trying to audit budget numbers for one fiscal year, which I agree with—we have to start somewhere—and also to identify the completeness and existence of their assets. They have a long way to go.

Senator SANDERS. If somebody is watching this on TV, might they think it is a little bit absurd that the agency that has most of the discretionary spending cannot give us an audit? Is that a fair statement?

Mr. DODARO. Well, it is definitely a problem. I have pointed it out many times, and, actually, last week we issued our annual—we have a requirement to audit the consolidated financial statements of the Federal Government, and for 17 years we have not been able to give an opinion largely because the Department of Defense has not been able to—

Senator SANDERS. Thank you. What I would say to my colleagues—thank you—is we can argue about what the size of the Pentagon budget should be. That is going to be a debate. I would hope that there is no argument and that some people take issue with the fact that when folks want more and more money—you talk about this issue in a different context. People want more and more money, and we do not even know how they are spending their money right now. I do not think that should make sense to anybody in this Committee.

Mr. DODARO. On that point, Senator, the Congress has required they state that they are auditable by 2017, so we are tracking their progress.

Senator SANDERS. Let me switch gears.

Mr. DODARO. Okay.

Senator SANDERS. We are talking about wasting money here. Now let's talk about the acquisition of money, money coming in. The IRS has estimated that each and every year about $350 billion

in taxes go uncollected. This has been referred to as the "tax gap." The Department of Treasury estimates that for every $1 spent on IRS enforcement, $6 is gained in increased revenue. But, meanwhile, in the last several years, the ability for the IRS to collect taxes has been severely hampered because its budget has been reduced by 10 percent in the last five fiscal years.

In your judgment, does it make sense to cut back on those people who can enforce tax law and bring in needed revenue?

Mr. DODARO. First, I would say I agree that the tax gap is a very significant problem. The estimates that I have seen—the most recent estimate is a net tax gap of $385 billion, and it ranges across the different types of taxpayers.

We have had on our high-risk list since 1990 some form of tax enforcement responsibilities. The latest we—

Senator SANDERS. But my question is—

Mr. DODARO. But on the revenue side, definitely revenue directed toward enforcement is productive. But whatever Congress decides on funding, they need to also take into account our recommendations that IRS could do a better job with the funding that they do have. You know, we have found that they do not have good return on investment measures. Overall it works out, but for specific enforcement programs—like, for example, we found if they shifted $124 million from field exams to correspondence audits, they would likely collect an additional $1 billion.

Senator SANDERS. Good. But bottom line is spending money on enforcement will bring in a lot more money than we are spending—

Mr. DODARO. Well, and also I think you have got to be concerned about level of service over time and the effect on voluntary compliance. Voluntary compliance right now is about 84 percent, so we have about—and if the people are not getting their questions answered by the IRS on the phone, they are waiting longer on the lines, I am concerned that over time there could be a cumulative effect on compliance issues, that even if you throw more people at it, you are not going to solve it.

Senator SANDERS. Fair point.

All right. Thank you, Mr. Chairman.

Chairman ENZI. Senator Ayotte—oh, Senator Perdue, I am sorry. Senator Perdue is next.

Senator PERDUE. Thank you, Mr. Chairman.

Mr. Dodaro, I have been a fan of yours since you took this office, and even before I got into politics, I have been a student of your output. Besides killing trees, there is a lot of information in here. I agree with the Ranking Member that what we are talking about today really is not a partisan issue. This is about getting a return on our investment, making sure the money is spent where it needs to be spent.

I have just got a real question, and that is, after reading through this and being a student for several years, I have a problem getting to the bottom line. What is the potential? And you gave us some numbers and percentages of what has been done. You have identified what has been done, what is in process, and what is open. Can you give us a little more detail about that? And break it, if you can, by DOD and other.

I agree with the Ranking Member that there is no sacred cow here. Everywhere we spend money has got to—we have got to get a return on that. But speaking of the IRS and collection, I would like to make sure that we are getting a return on what we are already spending, to your point, before we spend any more money. But the bigger question is: Help us understand what the starting point is about what the potential is as we look at this opportunity.

Mr. DODARO. Yes, there is definitely potential. As I mentioned, $20 billion has been saved already, and another $80 billion is in the works, that Congress has already approved, that will be saved over the next several years. There are tens of billions of dollars more in that area. There is a lot of room in defense and health care, which is where the money is.

Senator PERDUE. I am sorry. Could I interrupt you on that?

Mr. DODARO. Sure.

Senator PERDUE. So the 20 and the 80, is that just on discretionary, or is that overall in the total budget?

Mr. DODARO. That is overall. That is overall.

Senator PERDUE. Okay. So it is both discretionary and mandatory.

Mr. DODARO. Yes, yes. Yes, we have pointed out areas, for example, in the Medicaid area, we are very concerned that HHS is approving demonstrations in States without ensuring that it is budget neutral to the Federal Government. It ends up costing the Federal Government tens of billions of dollars, and, you know, Congress has no visibility.

Senator PERDUE. So the $80 billion that is open, that is still out there—

Mr. DODARO. No, no, no. That is already solved.

Senator PERDUE. All right. So the 80—

Mr. DODARO. We have got about—you can look at it, there are $100 billion in the bank. Okay?

Senator PERDUE. Got it. So what is left? What is the remaining potential that you have identified bottom line?

Mr. DODARO. It is tens of billions. I have not put a final figure on it.

Senator PERDUE. Could you do that for us?

Mr. DODARO. Well, I do not know if we could do it. It depends on what the Congress does based upon what our recommendations are in those areas. We have a number of areas where CBO has already scored what would happen if our recommendation was implemented. Those are noted in our testimony. We can add those up for you and give you those numbers and then say, well, here is the potential for the rest.

Senator PERDUE. Well, what I am really interested in is what the potential is by discretionary and mandatory.

Mr. DODARO. Okay.

Senator PERDUE. And by priority as well.

Mr. DODARO. Yes.

Senator PERDUE. You know, the 80/20 rule I am sure applies here as well, that 20 percent of the potential areas will give us 80 percent of the results. But I am not sure of that here. The question is: If you can give us that potential, that would be very helpful.

Mr. DODARO. Yes. I am just informed by my team that CBO has already scored at least $25 billion that could be saved, but there is more.

Senator PERDUE. Well, we would be very anxious to get that.

Mr. DODARO. Okay.

Senator PERDUE. The next thing, when you look at who is responsible—I think you mentioned 29 percent had been fully addressed.

Mr. DODARO. Right.

Senator PERDUE. Who addressed that?

Mr. DODARO. We broke it out in the table in our testimony. It is roughly around—you know, 28, 29 percent was addressed both by the executive branch and by the Congress. But the partially addressed, the executive branch addressed them more, because to score a partial in our scoring on the Congress, the executive agency—Congress addressed 26 percent of what we addressed to Congress; the executive branch, 30 percent of what we addressed to them. But to get it partially addressed for the Congress, there has to be a bill introduced and actually reported out of Committee as a starting point. Just a bill being introduced, we are counting that as not addressed.

Senator PERDUE. Well, I understand the scoring. Mr. Chairman, I think it would be great—and, Mr. Dodaro, thank you for your testimony. I think it would be great if we could get a summary of that, even if it is bracketed by estimates, educated estimates. I realize that it depends on how we score it and what we do legislatively.

Mr. DODARO. Right.

Senator PERDUE. But as a budgeting matter, I would really love to see your idea of what that potential might be.

Mr. DODARO. Okay. We will do what we can.

Senator PERDUE. Thank you.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Senator Warner, and then Senator Ayotte.

Senator WARNER. Well, thank you, Mr. Chairman. Mr. Dodaro, good to see you again, as always, and let me just say that for particularly Senator Perdue, who, like me, comes from the business sector, you know, this is a challenging area. And, unfortunately—and Senator Johnson and I have worked on this; Senator Ayotte and I have worked on these issues together. You know, there is some progress, and I want to go through in my couple of minutes some of the progress we have made, because this is not an area that is very sexy or keeps people's attention very long.

The challenge sometimes is making sure we just have commonality of terms. One of the things that we passed a few years back was the GPRA bill, which says, you know, traditionally what happens, every administration comes in, they set a whole new set of management objectives, and they last for a few years until the next administration comes in. For the first time ever, we have said agencies actually have to identify their strategic goals, limit those goals—anybody who has done business knows if you have got 30 goals, you do not have any goals. Limit it to two or three, report on them on a quarterly basis. You have been very supportive of

this effort, and for the first time ever, agencies actually have to identify not only their great performing programs but their three worst performing programs.

We have got OMB that comes up with an annual list, but if you do not have actually the agencies, the people running these programs themselves, identifying where their problems are, we are not going to get to the bottom of it. And in this year's fiscal year 2016 budget, for the first time ever, we have got some of that data.

Last year, this Committee worked together, and we passed the DATA Act, and I think, again, you called it, Mr. Dodaro, one of the most single biggest things you could do to help find and fix wasteful programs, because one of the challenges is—and the Ranking Member has talked about the Defense Department, but this is everywhere—there is no common definition of what a program is. So somewhere in our budget, something appears as a grant, somewhere else it appears as an expenditure, and the DATA Act does not go as far as some of us would like. But it really is the first time ever that there has been an effort to try to start some level of consolidation. The Ranking Member should know, you want to really get a good talking point, there are over 250 separate financial reporting systems just inside the DOD. How do you ever compare apples to apples if you have got different financial reporting systems?

Again, I am going to come back and get you a question on this one. An item that Senator Kaine and I have worked with, with Congressman Whitman over on the House side, the Chesapeake Bay Accountability Act. We have got a slew of programs, Federal, State, and local, around the Chesapeake Bay. This is the first time ever we have tried to say let us do a cross-cutting budget analysis of all these programs and actually try to evaluate where we get the most value for our dollars. And a small area, a small segment, but even within the Chesapeake Bay there are literally dozens of programs, State, Federal, and local, and this will be the first time we try to analyze this on a cross-cutting basis.

And one that Senator Ayotte and I have worked on got us some good attention, maybe not fully transformative, but we spent a slew of time perusing reports of agencies that nobody ever looks at. So we started with your good work. When it finally got through the sausage-making process of each committee re-evaluating, we only ended up with—I think they identified 300 reports. We got about 50 reports eliminated. But this literally is thousands and thousands of man hours and hundreds of thousands if not millions of dollars spent on activities that could be more usefully spent.

So action is needed, and it is one of the reasons why under Senator Ayotte's leadership this task force that continues to focus on areas of Government performance, efficiency, duplication I really think, Mr. Chairman, needs to continue, and under Senator Ayotte's leadership I know it can continue to do good things, because this is an area that, unless you stay focused on it, it tends to always get pushed aside.

If you could comment for a moment, Gene, on the DATA Act, we have got a fairly aggressive timeline. You might want to give us an update on how you are helping OMB and Treasury get the program definitions right and what you want to share with us in terms of metrics we ought to look at going forward.

Mr. DODARO. Yes, I think the DATA Act is very important, but it has to be implemented effectively. So we are working to monitor what Treasury and OMB are doing to implement it.

The first big milestone is coming up in May. In May 2015, they have to produce data standards for the agencies to implement. So we are monitoring what they are doing. They got off to a pretty good start. They are supposed to consult with people. But they are working now to come up with those data standards.

Even though the law does not require GAO to report on progress in the DATA Act until 2017, I am going to report this year on the progress so that Congress has a good idea where things stand and whether the data standards developed are comprehensive, whether they are going to be clear enough.

They have also decided that they are going to link the definition of "program" under the Government Performance and Results Act with implementation of the DATA Act, which has some intellectual merit to it, but it has to be done properly; otherwise, you are not going to have the good definition. We have suggested that they use web-based technology so that a lot of this information can be sorted. GPRA requires it to be linked to the program activity accounts in the budget submission, but that has not yet happened.

So the bottom line is they got off to a decent start. I am cautiously optimistic. There is a lot that needs to be done. GAO will be involved early and advising the Congress.

Senator WARNER. Mr. Chairman, last, just one—30 seconds.

Chairman ENZI. Your time has expired. We have got a vote at 11:30, so I do have to move on. You can submit it in writing.

Senator Ayotte?

Senator AYOTTE. Thank you, Chairman.

I wanted to first of all thank you for your important work. I appreciate your being here. And, you know, I think as Senator Warner said, I have been glad to work with him on the Budget Performance Task Force. And one of the things that I am interested in getting at as well is—and you and I have talked about this in the past. As I understand your testimony, only 29 percent of the issues raised by GAO have actually been fully addressed—29 percent.

Mr. DODARO. Right.

Senator AYOTTE. And so a lot of these reports sit on the shelf. You know, I have got a bill with Senator Manchin that the Chairman referenced called the Duplication Elimination Act, and it is really what I like to call a bill that kicks all of us where we need to be kicked to act, the executive branch actually take up the work that you are doing and provide recommendations to Congress, and then provides an expedited process for Congress to act so we can really move these recommendations either affirmatively or negatively and really act on them.

What else do you think we should do to ensure that your recommendations are fully addressed? Because you do such important work, and my colleagues have already talked about some of it today that needs to be addressed.

Mr. DODARO. One of the things in particular this Committee is poised to do that other committees would not, a lot of the areas that we suggest be addressed span jurisdiction of multiple commit-

tees in the Congress, and as a result, unless there is action by multiple committees, there is really not going to be much progress in those areas. I am not optimistic based on the track record that that would—

Senator AYOTTE. So our jurisdiction becomes fragmented as well.

Mr. DODARO. Yes. Yes, and the same thing happens in the executive branch. The departments and agencies are in their lanes, and OMB is the only one that can look across the agencies, like we have made recommendations that some of the loan programs we believe between Agriculture and HUD can be merged. You would have a more efficient structure and better service to the public. But nobody is taking the initiative within the executive branch when there are multiple agencies involved very often.

So I think that is going to be the pivotal point and whether that 29 percent is really going to move much or not in the future.

Senator AYOTTE. So this is a great bipartisan opportunity we have here in the Senate Budget Committee because we cross jurisdictions.

Mr. DODARO. Yes.

Senator AYOTTE. Excellent. Great. And I look forward to working with the Chairman and the Ranking Member because I think this is something we all can agree on, and all of our constituents, it drives them crazy, for good reason, when they look at your—when we talk with them about your reports on duplication and fraud, and they say, "Well, that is our money going there." So I hope we can work together on that with this Committee's jurisdiction.

I wanted to ask you about a particular area, and that is STEM education. STEM education is so important. In 2010, you found 209 STEM education programs, and as I understand, based on your recommendations, they have been consolidated to 158. The President's 2016 budget proposes to eliminate another 20 STEM programs.

Here is my interest in this. We happen to have in New Hampshire an inventor named Dean Kamen, who came up with a brilliant basically public-private partnership in FIRST Robotics that is across this country that actually keeps metrics about kids going in STEM, learning how to build a robot, and then going back into the field.

So of the 138, assuming that we eliminate the 20 the administration has asked for, of the 138 that are left, that still seems like quite a bit. And I know that the National Science and Technology Council has developed a 5-year strategic plan. But help me understand. Are we measuring what these programs are doing? Because it seems like we have a bipartisan interest in improving STEM education in this country. And how good are we measuring whether these 138, even from the progress we have made, are actually helping improve STEM education and getting more of our kids ready for the jobs of the 21st century?

Mr. DODARO. First, I am encouraged that the 5-year plan and the guidance that the National Technology Council has put out provides some guidelines on what should be evaluated. But the last time we looked at this—now, admittedly, we looked at the larger set of STEM programs—we found very few of them had been evaluated. In fact, 66 percent had not been at that time.

Now, I do not know how many of the remaining 136—we can go back and take a look at it, but based on what our prior experience would be, there is—you know, not enough of them are getting evaluated in order to know what effectively works or not, and that should be something that the Congress—I mean, it is already required under the Government Performance and Results Act, but nobody is enforcing it.

Senator AYOTTE. Right.

Mr. DODARO. And I think the Congress could do a lot to require that.

Senator AYOTTE. I think this is an issue across programs, so we have got these—it is required, but we are not really measuring whether they are getting results out of where we are putting in programs.

Mr. DODARO. Right. Well, I think that, you know, until the Congress starts saying, "Look, we are not going to fund you unless you tell us and demonstrate that you are effective and the money we are going to give you is going to be invested well," there is no incentive for the agencies to change what they have been doing.

Senator AYOTTE. Right, I agree with you. And I am hoping even just a measure like Joe Manchin and my bill might just at least get people knowing that we are not going to let these reports sit on the shelf, that we are going to say, "What are you doing with the taxpayer dollars?" I think that would be helpful. And I know my time is up. My clock is not moving, but I am assuming it is up soon. I wanted to ask a specific request, if you would be able to provide a list of—we cannot find the STEM programs. Like we cannot get a list of what is left.

Mr. DODARO. Okay.

Senator AYOTTE. So if you can help us with that, because we are very interested in it, I would appreciate it.

Mr. DODARO. Sure.

Chairman ENZI. Senator Kaine.

Senator KAINE. Thank you, Mr. Chairman, and thank you, Mr. Dodaro, for your testimony.

You gave some statistics about the degree to which your advice is being followed, and I was kind of curious. I saw a piece—I think it was in Government Executive, a publication in the middle of February—that begins—it says, "Reports and congressional testimony from the GAO often note Federal agencies' failure to act on past recommendations. But a unique study using data analytics shows that agencies ultimately have acted on more than four-fifths of the recommendations from Congress' top watchdog over the past quarter-century." And this was a study that was done by Deloitte Public Sector Research. I am assuming that you are familiar with the report.

Mr. DODARO. Yes.

Senator KAINE. How does that differ—they are sort of analytic—differ from your calculation on the numbers? I am just curious.

Mr. DODARO. Well, actually their study basically verifies the statistics that we have reported to Congress every year. If you look at all of GAO's work collectively, 80 percent is implemented over a 4-year period of time. The 29 percent and the 44 and 23 that I report are just for the overlap, duplication, and fragmentation area.

Senator KAINE. I see.

Mr. DODARO. You know, that is a subset of our reports.

Senator KAINE. I think that is—I mean, it is important because it says to me two things. One is you are doing good work if they are accepting that many of your recommendations. If they are accepting 80 percent of your recommendations, that must mean they know you are right and you are pointing out things that they need to fix.

Mr. DODARO. Right.

Senator KAINE. And, secondly, if they are fixing 80 percent of the recommendations you make, essentially, that also says some good things about the folks out there who want to improve. And so I was pleased to see that.

I want to ask you, since you have been at GAO for such a long time, I am kind of curious about your thought about how to build in a culture of improvement. So, you know, one way to improve is when you send a report from the GAO and you point out things that are wrong, then, oh, gosh, GAO says it is wrong, I guess we better fix it. But you would obviously want to build in a culture of improvement that, even if they were not getting that report from you, there is an effort systemwide to look at duplication or look at, gosh, we do not have any data that says this program or performance is working, it should not take a GAO report to convince an agency, a Cabinet Secretary, the entire Government, to kind of build a culture of improvement.

What kinds of things have you seen in your GAO career that you think are good examples? I remember Vice President Gore did the Reengineering Government Commission. I guess this is supposed to be part of OMB's charter, to kind of perennially—on the management side of OMB, perennially improve better management. But what strategies are good strategies for driving down duplication and driving on, you know, getting value and measuring outcomes?

Mr. DODARO. Part of the problem is you have perverse incentives in place in a lot of agencies in the culture. For example, on weapons systems acquisition, you know, we find time and time again that when we have got Defense to put in their policies best practices, where we have done studies in the private sector and other areas, but they do not get executed properly. There are still requirements not developed in some of the programs. I mentioned improper payments of $124 billion. The culture and the incentives were to pay quickly and worry about later finding out whether everybody was eligible or did we pay the right amount or whatever. So the incentives are skewed right now, and they need to be directed.

Unfortunately, the only major management improvements that have worked successfully over the years have actually been those that have a statutory underpinning in the Congress because that provides continuity over time. And every time you change an administration, you have 3,000 new political appointees come in. There are a lot of acting people. Average tenure is about maybe a year and a half, 2 years. And so there is a lot of churn in the leadership in the agencies, and it is hard to change these incentives so that they work effectively over time and people get properly rewarded.

The budget and appropriations process makes people make decisions too early in the process sometimes, and the preparation of it. If you save money, you do not get to keep it. You have a smaller budget at the end of the day, so it does not get reinvested.

Senator KAINE. Right. That is a bad incentive.

Mr. DODARO. Yes.

Senator KAINE. What is an example—you mentioned the best ones have a statutory underpinning because there is a continuity.

Mr. DODARO. Right.

Senator KAINE. What is your opinion of the best thing Congress has done statutorily to push a culture of improvement in performance?

Mr. DODARO. The passage of the Chief Financial Officers Act and the Management Reform Act, which required for the first time the preparation of financial statements and audits. Right now—I mentioned earlier that that first started in 1996. Well, first of all, the Federal Government required State and local governments to have financial audits. The private sector has had it following the stock market crash. The Federal Government was very late to the party to implement that. Six of 24 agencies when we first started could get clean opinions. Now routinely 22 of 24 get clean opinions. So that culture has changed, and it is a result of Congress and a lot of hard work by the agencies.

Senator KAINE. I would love to ask more, but my time is up. Thank you, Mr. Chairman. Thank you to you, Mr. Dodaro.

Chairman ENZI. Thank you.

Senator King?

Senator KING. Thank you, Mr. Chairman.

First, I want to thank you for your testimony and your amazingly good work. What you are doing is good and very important work, particularly given the size of the enterprise that we are discussing here. Do you have sufficient staff and authority to continue doing this work? Do you need more? I mean, I just think we are dealing with such a large enterprise and what you are doing is so crucial, I just wonder if you are—I realize everybody says, "I always need more people," but give me your thoughts on that.

Mr. DODARO. Yeah, well, I was concerned. From 2010 to 2013, we lost 15 percent of our staff. We were subject to the sequester just like everybody else. So we were at our lowest staffing level since 1935. Obviously—

Senator KING. Which is crazy, considering the growth of the size of—

Mr. DODARO. Well, the Federal Government is a little bigger than it was then at that time. And our results, I mean, 80 percent of our recommendations that I mentioned are implemented over time, but last year, our work resulted in $54 billion in financial benefits to the Government. So we get about $100 return for every dollar invested in GAO.

Fortunately, with the Bipartisan Budget Act, in 2014 and 2015, that offset the sequester, we have been able to gain back some of those staff resources, but we are not at our optimum level yet, which I think should be around 3,250 people. I have submitted a request to continue incrementally, you know, recognizing our deficit and debt situation. You know, I audit the financial statements of

the Federal Government, so I know very well what our fiscal dilemma is right now. We are not on a long-term sustainable path. So we could use a little bit more resources, and I would invest them in this tax gap and improper payments areas, is what I have told our appropriators.

Senator KING. I want to follow up on that in minute. But what you are saying is that the sequester would diminish your capacity to find savings in the Federal Government, which would be the ultimate Catch-22.

Mr. DODARO. Yes.

Senator KING. One more reason to try to do something—not try but do something about the sequester.

I was going to ask you about overpayments. You identified a lot of money there. Is that an area that is worth its own special focus? Do you have a division, a directorate, or a department that focuses on that? That seems like a ripe area for work.

Mr. DODARO. Yes, we have a GAO-wide plan. We have our specialists in each program area who are working on it, but we have a coordinated plan across GAO. I wanted to make sure we did that. But, you know, we do not—you know, the problem is growing, and we do not have enough resources to do what I would like to do, which is get at root causes in a lot of places. So that is one where we could—I am planning to invest more resources if the Congress responds.

Senator KING. I would urge you to be specific about what you need and where those resources would go so we can help you. Again, I think the investment is so powerful that we should pursue that.

Finally, I have inquiries about evaluation. We do all these different things, and as you point out, sometimes they are evaluated and sometimes they are not. What about a neutral body—maybe it is you, maybe it is part of GAO, maybe it is somebody else—to evaluate Federal programs and also at the same time to evaluate tax expenditures? Tax expenditures are essentially Federal programs. They are equal in dollar value to the entire discretionary budget, over $1 trillion. And yet I just would—I think it would be helpful to all of us in making policy to know what is working and what is not working. And should we pass a kind of general, generic evaluation statute? And I hate to talk about creating a new bureau, but an Office of Evaluation, because I am not—I am a little suspicious of an agency evaluating its own performance. Of course, all their programs are working beautifully. Thoughts on that?

Mr. DODARO. Yes, first, we have recommended for years that the Congress and OMB start evaluating tax expenditures in any one year that it is more than the entire discretionary spending and revenue foregone. But we have not gotten very much traction on that. I think it needs to be done. It ought to be part of the regular budget process and you have routine scrutiny, just like you do with discretionary spending.

Secondly, I think evaluating the programs is a fundamental management responsibility of the agencies running the programs. They have been required by law to do this since 1993, but nobody is following—

Senator KING. But is it realistic to expect an agency to evaluate its own programs?

Mr. DODARO. I think it has to start there to be a management responsibility. You can have—a lot of times we are asked to look at whether the evaluation by the agency is done properly. Sometimes the Congress will require us to consult with the agency to make sure it is done properly. I think that—I mean, that is where all the money is right now, you know, in terms of running the programs. And if you set up something separate, it would take a lot of time and years to do what should be done as a normal part of management. You can have independent scrutiny of the evaluations, but if they are not done by the managers, there is no incentive to improve either. I mean, they will just have—they will fight the evaluation—

Senator KING. Unless the managers know that somebody is going to be coming in and looking over their shoulder.

Mr. DODARO. Yeah, I mean—

Senator KING. I am just trying to think of a structural way to get at this problem of lack of evaluation.

Mr. DODARO. Yeah, I do not think it is a structural problem. I think it is a discipline problem on the part of the agencies in following the law Congress said and Congress following—requiring the agencies to do what they have already asked them to do and use the results. Even when evaluations are made, I am not sure they are always used effectively.

Senator KING. Do most statutes that create programs require evaluation?

Mr. DODARO. I would have to go back and we will give you an answer, but there is a general statute that requires it across the Federal Government, the Government Performance and Results Act, and there was a modernization passed in 2010 that not only requires it now for agencies, but on cross-cutting governmentwide priorities.

Senator KING. Thank you, Mr. Chair.

Chairman ENZI. Thank you. I want to thank our witness. I am always fascinated by this evaluation prioritization, and the only thing I have ever found that would get an agency to do their evaluation is to ask them for a list of what they would cut if they had to cut 2 percent, if they had to cut 4 percent, if they had to cut 6 percent, if they had to cut 8 percent. If it shows up on all the lists, it is not that important to them. But, otherwise, there is a tendency by the agencies to say all of them are spectacular.

So I want to thank the witness for agreeing to testify this morning, for all the information you have shared with us, for all of the questions that are still pending.

I want to remind colleagues that questions can be given to the record for the Comptroller General by 6:00 p.m. today. And we would hope that you would respond within 7 days because we are going to be getting close to our budget markup by that time.

Mr. DODARO. Okay.

Chairman ENZI. So with no further business to come before the Committee, we stand adjourned.

[Whereupon, at 11:34 a.m., the Committee was adjourned.]

# THE BETTER WAY: BENEFITS OF A BALANCED BUDGET

**WEDNESDAY, MARCH 11, 2015**

UNITED STATES SENATE,
COMMITTEE ON THE BUDGET,
*Washington, D.C.*

The committee met, pursuant to notice, at 10:30 a.m., in Room SD–608, Dirksen Senate Office Building, Hon. Mike Enzi, chairman of the committee, presiding.

Present: Senators Enzi, Sessions, Crapo, Johnson, Wicker, Perdue, Sanders, Stabenow, Whitehouse, Warner, Merkley, Baldwin, and King.

Staff Present: Eric M. Ueland, Republican Staff Director; and Warren Gunnels, Minority Staff Director.

## OPENING STATEMENT OF CHAIRMAN ENZI

Chairman ENZI. I call this hearing to order. Good morning, everyone.

Hard-working taxpayers deserve a government that is efficient, effective, and accountable to them. Washington should spend your tax dollars wisely and responsibly and give you freedom and control to pursue your future the way you choose. That is what every American deserves and that is what I am committed to here today.

We must all face the truth. America's budget is at a crisis. We did not get there overnight and we will not fix it overnight, but we can begin to solve this crisis if we act now. We must take responsibility to act with integrity in an open, honest way to solve this problem and start at once. This will deliver the healthy economy that hard-working taxpayers deserve, a healthy economy that creates real opportunity for all, where job creators can grow, where if you work hard and play by the rules, you have a shot at the financial independence you deserve and the peace of mind you need.

That is why I was so disappointed in the administration's recent budget. After adding $7.5 trillion in debt since taking office, this administration proposes to add five-and-seven-tenths trillion more. That is actually $5,700 billion more in debt.

Take a look at the screen. Over the past six years, we have learned that wasteful Washington spending does not solve problems, it sidesteps them. We need to eliminate deficits instead of exploding them. Hmm—

Senator SANDERS. That is not what the screen says.

Chairman ENZI. Yes, I know.

[Laughter.]

Chairman ENZI. Well, I want you to imagine that.

[Laughter.]

Chairman ENZI. There. A little help with the—now you can see clearly what I am saying.

Senator SANDERS. Oh.

Chairman ENZI. I am glad my description was so good.

You can see the little blue hatched parts up there. That is actually each year's deficit through the next ten years, the little kind of blue cross-hatched, kind of a purple, kind of a combination red and blue, because it is everybody's fault.

But, what the red bars are is the cumulative amount of that, and you can see that it adds up over time.

What are the long-term consequences of this approach? It means higher interest rates for consumers, because government is borrowing more, and it means higher taxes for every American to pay for more overspending. It also means more waste and unaccountable spending that puts an anchor on our economy, costing us stable, good-paying jobs.

Look at this chart. Because of the President's budget, interest costs will more than triple. Let me say that one more time. The interest costs will triple. In ten short years, we will be spending $785,000—$785 billion on interest every year. That spending will do nothing to help hard-working taxpayers meet the costs and challenges of everyday life. Interest does not build anything. In fact, it will make it even harder.

The administration's budget sends a very clear message. In this economy, with fewer jobs and less opportunity than ever, taxpayers may have to learn to do more with less, but so far, Washington does not have to. That is simply wrong, and it only deepens the distrust, the skepticism, and the cynicism our citizens feel about their government and this Congress.

Americans have worked hard, harder than we can imagine, to claw back from the Great Recession and its aftermath. It is time for Congress to work just as hard to protect them. By spending responsibly, by making taxes fairer, simpler, and more straightforward, by putting our fiscal books in order in a balanced, responsible way, there are three significant benefits.

First and most importantly, we can restore the trust that we have broken with the American people. According to Gallup last month, only 20 percent of those surveyed approve of how we, their elected representatives, are doing their job. Sadly, that poor number is an improvement over the 12 percent who approved in February of last year. The biggest reason for this broken trust is because of our failure to do what voters have long demanded, to eliminate wasteful Washington overspending, to make government truly more efficient, more effective, and more accountable to them, to improve the programs that protect our most vulnerable and strengthen the health and retirement security of our seniors. They see trillions in waste, fraud, and abuse, and ask why we do not do what obviously must be done. We must be committed to rebuilding, to truly earning the trust of the American people.

This leads me to the second benefit. A responsible, balanced budget requires us to actually set priorities and stick to them. We live in an age when everything is a priority. As we know from life, when everything is a priority, nothing is. The Comptroller General

of the United States, Gene Dodaro, who appeared here at our last hearing, came before us and presented a catalog of inefficient, ineffective, and duplicative programs. Why do they still exist? It is long past time for every program to be evaluated and prioritized. If they are not delivering results, we should improve them. If they are not needed, we should eliminate them. If they are being done by multiple offices, we should streamline them.

Getting our budget balanced and staying there, except for extraordinary circumstances, means a constant examination of what needs funding and what does not. A responsible balanced budget ensures that we actually prioritize and demand results. Hard-working taxpayers, along with every business in America, do this every day. We must play by the same rules in Washington.

Finally, a responsible balanced budget demonstrates that Washington is doing its part to deliver a healthy economy for everyone. A government that is more efficient, more effective, and more accountable is absolutely essential for strong economic growth and job creation. This will help build the opportunities that so many people deserve. In the real world, this means investors can find new opportunities, and most importantly, it means every American who wants to find a good paying job and a fulfilling career has the opportunity to find it. That is what a balanced budget can deliver and that is what the American people deserve.

I want to mention a letter that I got. One of the people I was interested in having as a witness was Mitch Daniels, who is with Purdue University right now. He just finished speaking at the National Academy of Engineers, and in that he said, "In my view, the nation's transcendent problem, the one that endangers our entire position as the leading country in the world, is also the single biggest danger to the future of our historically dominant scientific research enterprise. I refer to our national debt, which I have elsewhere labeled the 'red menace,' this time consisting not of militarily aggressive Soviet imperialism, but in perhaps the more dangerous red ink in which our national finances are drowning."

I would ask unanimous consent to have the letter in its entirety appear in the record. Without objection.

[The information of Chairman Enzi follows:]

**Chairman Mike Enzi**

**Statements for the Record**

The Better Way: The Benefits of a Balanced Budget

Senate Budget Committee

March 11, 2015

Letter to Chairman Enzi from Mitch Daniels, President of Purdue University
March 6, 2015

(Letter Attached)

PURDUE
UNIVERSITY

OFFICE OF THE PRESIDENT

March 6, 2015

The Honorable Mike Enzi
Chairman
US Senate Committee on the Budget
624 Dirksen Senate Office Building
Washington, DC 20510

Dear Chairman Enzi;

Thank you for the opportunity to submit testimony to the Senate Budget Committee as part of the upcoming hearing, "The Better Way: Benefits of a Balanced Budget." I applaud your leadership and sincerely hope you will address the most pressing domestic problem – the historic debt we will leave behind to the next generation, including the more than 40,000 students here at Purdue University.

Over a year ago, I delivered a speech to the National Academy of Engineers that still represents my strongly held viewpoint. For the record, I share with you an excerpt:

*... In my view, the nation's transcendent problem, the one that endangers our entire position as the leading country of the world, is also the single biggest danger to the future of our historically dominant scientific research enterprise. I refer to our national debt, which I have elsewhere labeled the "new Red Menace", this time consisting not of a militarily aggressive Soviet imperialism, but in the perhaps more dangerous red ink in which our national finances are drowning.*

*The terrible inequity, through which massive national borrowing will penalize future economic growth and plunder the same young people we are now striving to educate at Purdue and your universities, is a sermon for another Sunday. For today, allow me to focus on the direct hit our federal deficit and so-called entitlement spending in specific increasingly impose on the NSF, the NIH, and other federal departments like Defense, Homeland Security, Agriculture, and others. These vital research budgets are being brutally squeezed by the way in which Social Security, Medicare, Medicaid, food stamp, and other automatic spending programs are devouring all the dollars American taxpayers can produce. Within a decade or so, autopilot spending and debt service will consume every dollar Americans pay in taxes, meaning that every dollar for the discretionary core of government would have to be borrowed money.*

Hovde Hall, Room 200 ▪ 610 Purdue Mall ▪ West Lafayette, IN 47907-2040 ▪ (765) 494-9708 ▪ Fax: (765) 494-7875

*Much of the research community's advocacy in recent days has concentrated on making the case for the value of scientific inquiry, and its huge and often unforeseen contributions to national wealth and wellbeing. We can never make this point too frequently.*

*But in large measure, this is pushing on an open door. Ironically, the importance of basic research and public support of it is one of the few things on which I find that decision makers who differ on other questions generally agree. The real problem is that there isn't any money; more each year, it flows out the Treasury door in the form of checks and payments for medical bills. And, unjustifiably, it flows not just to poor or middle-income people, but also to the wealthiest among us, in systems fifty to eighty years old, designed for bygone eras.*

*...Friends of the research enterprise should be out front in demanding bold action to reform entitlement spending and again liberate resources for the investments in new knowledge that, without public dollars, are unlikely to come any other way.*

Sincerely,

Mitchell E. Daniels, Jr.
President

Chairman ENZI. Working together, we can deliver real solutions, real results, and real progress if we look for the common ground and cooperate to get things done. A responsible balanced budget that makes government more efficient, more effective, and more accountable is not only possible, it is doable.

Senator SANDERS.

**OPENING STATEMENT OF SENATOR SANDERS**

Senator SANDERS. Thank you very much, Mr. Chairman, and thanks for holding this important hearing.

For most Americans, the economic reality of today is pretty clear. For the last 40 years, the American middle class has been disappearing while the people on top, the wealthiest people, have been doing better and better and better. Today, real median family income is almost $5,000 less than it was in 1999. The typical male worker, despite huge increases in productivity, made $783 less last year than he did 42 years ago, after adjusting for inflation. The typical female worker is making $1,300 less than she did in 2007.

Despite the modest gains of the Affordable Care Act, 40 million Americans continue to have no health insurance, and more people are living in poverty today than almost any time in the modern history of America.

Despite a significant improvement in the economy since President Bush left office, real unemployment is not 5.5 percent, it is 11 percent, counting those people who have given up looking for work or are working part-time when they want to work full-time. Youth unemployment, the future of our nation, is 17 percent, and African American youth unemployment is far higher than that.

Throughout this country, a significant number of young people have given up the dream of going to college because of the high cost of tuition, while millions of others are struggling with the yoke of excessive debt around their necks, and I am sure that every member of this committee has talked to young people who are trying to figure out how they deal with $50,000, $80,000 of debt for the crime of having gone to college.

The Federal minimum wage today of $7.25 an hour is a starvation wage, and half the kids in public schools are eligible for free or reduced-price school lunches.

And, while the middle class disappears, the people on top and the largest corporations have never had it so good, and any serious discussion of deficit and debt has to take that into consideration. Today, the top one percent earns more income than the bottom 50 percent. And since the Wall Street crash of 2008, over 99 percent of all new income goes to the top one percent. Corporate profits are soaring, and CEOs now earn over 270 times what their average employee makes.

Today, incredibly, the top one-tenth of one percent owns almost as much wealth as the bottom 90 percent. And the wealthiest family in this country—one family—owns more wealth than the bottom 42 percent of the American people.

The fact of the matter is that over the last 40 years, we have witnessed an enormous transfer of wealth from the middle class and the poor to multi-millionaires and billionaires. Between 1985 and 2013, the bottom 90 percent of the people in our country lost $10.7

trillion in wealth that it otherwise would have had if the distribution of wealth had remained at the same level as it was in 1985. Meanwhile, the top one-tenth of one percent experienced an $8 trillion increase in wealth as the distribution of wealth became increasingly unequal.

And today, we are going to hear testimony from our Republican friends, invited witnesses that I can only refer to their testimony as the Robin Hood principle in reverse—we are going to hear from witnesses who suggest that in the midst of this massive income and wealth inequality, that we cut programs that the elderly, the children, the sick, the poor, and working families desperately depend upon, and then at the same time they want us to give more tax breaks to the rich and large corporations.

And, unless I am very mistaken—and if I am, I owe you an apology, Mr. Chairman—that is exactly what the Republican budget will be doing, taking from the working people and the poor and giving to the wealthy and large corporations. And, that is exactly what the Ryan budget did last year when it was passed by the Republican House.

Further, we will hear testimony today from one of our Republican witnesses about the need to make major cuts in Social Security and Medicare. In other words, not only do some of my Republican colleagues want to provide huge tax breaks for the wealthy, not only do they want to make cuts in health care, nutrition, education, heating assistance, Food Stamps, Meals on Wheels, and affordable housing, they also want to cut Social Security benefits for elderly seniors in Vermont and throughout this country struggling to survive on $14,000 or $15,000 a year or less, and, by the way, also cut back on benefits for disabled veterans.

That is wrong. That is terribly wrong. Frankly, it is almost laughable that this advice that cuts Social Security and Medicare comes from the Business Roundtable, an organization representing the CEOs of many of the largest corporations and Wall Street financial institutions in this country.

While these people tell us that we should cut Social Security for a senior in Vermont who today does not have the funds to heat her home or pay for her medicine, a study from the Institute for Policy Studies tells us that the CEOs of these major corporations in the Business Roundtable can expect a monthly retirement check of $88,576 a month. So, we have people who are getting a retirement benefit of over $88,000 a month coming here telling us that we should cut Social Security benefits for elderly people in Vermont who are trying to live on $14,000 a year. I thank you for your advice, but that is advice that this Senator will not accept.

Further, when we talk about the deficit and debt, which is the focus of this hearing, I find it interesting that some of my colleagues seem to ignore the fact that we have major corporation after major corporation, including many in the Business Roundtable, that pay virtually no taxes at all in the United States. To name just three companies in the Business Roundtable, General Electric, Verizon, and Boeing, and there are many others. These are enormously profitable corporations that in some recent years have paid zero in Federal income taxes. And today, we are going

to be lectured about how we have to cut programs for working families to balance the budget.

This country is losing approximately $100 billion a year in revenue because American companies and the wealthy are stashing their profits in the Cayman Islands, Bermuda, and other tax havens. The situation has become so absurd that one five-story office building in the Cayman Islands is the home of more than 18,000 corporations. Maybe, if we are serious about deficit reduction, rather than cutting Social Security or Medicare, we might want to examine that reality.

Last point. If we are serious about lowering the deficit and the debt, the best way to do that is not by developing an austerity program which increases suffering for those already hurting. The best way forward is to create a full employment economy with jobs that pay good wages. When people work and when people have jobs, they pay taxes. When people have jobs that pay them a livable wage, they no longer need government programs, in my view. The best way to do that is to rebuild our crumbling infrastructure, to put millions of people back to work. And I would all remember—all of us hope to remember—that the last time we eliminated a deficit, from 1998 to 2001, we had a full employment economy.

And with that, Mr. Chairman, I yield.

Chairman ENZI. Thank you.

It is important for my colleagues to appreciate the concept of a balanced budget is not new or untried. Most of the States have long abided by balanced budget requirements. It is a rich record of fiscal success and failure in the States and we should draw heavily on it.

I just noticed that 24 States have already passed a Balanced Budget Constitutional Convention Amendment. Ten more are considering it, while I know of one more that has already passed it, so we are at 25 now. If we get to 34, we have to balance the budget.

Last year, we spent $1,100 billion, so we have got to make decisions on $468 billion we spent more than that, which would be about a 50 percent cut, and I do not think we can do that.

So, that is why we are doing a hearing to try and talk about some of these things, so to guide us to a better understanding of the benefits for moving toward a balanced budget, we have three exceptional witnesses. Let me introduce each in the order they will offer testimony.

First, we have Governor John Engler. Governor Engler was the 46th Governor of Michigan, from 1991 to 2003. He is currently the President of the Business Roundtable, an association of chief executive officers of leading U.S. corporations that produce seven-and-four-tenths trillion in annual revenues and employ more than 16 million people. During Engler's tenure as Governor of Michigan, he signed 32 tax cuts into law, saving Michigan taxpayers some $32 billion, and helped create more than 800,000 new jobs, taking the State's unemployment rate to a record low.

Our second witness is Maya MacGuineas. Maya MacGuineas is the President of the Committee for a Responsible Federal Budget. There probably are few in this town who have served on as many fiscal commissions and task forces than Ms. MacGuineas, with the

probable exception, of course, of Pete Domenici. Senator Domenici, of course, used to chair this committee for many years. Ms. MacGuineas has worked at the Brookings Institution and on Wall Street. She serves on the boards of a number of national nonpartisan organizations and received a Master's in Public Policy from the John F. Kennedy School of Government at Harvard University.

Our third witness is Dr. Mark Blyth. Dr. Blyth is the Eastman Professor of Political Economy in the Watson Institute for International Studies at Brown University, where he has taught since 2009. He has published extensively on topics in international relations, comparative politics, and recently on fiscal questions.

Welcome to all of you. Governor Engler, we will start with you. I hope that all the witnesses will kind of condense their presentation to five minutes so that we can have questions. There will be more showing up for questions. So, Governor Engler.

**STATEMENT OF JOHN ENGLER, PRESIDENT, BUSINESS ROUNDTABLE, AND FORMER GOVERNOR, STATE OF MICHIGAN**

Mr. ENGLER. Thank you, Mr. Chairman. I could tell from the opening comments there will be questions, so I am delighted to have an opportunity to be here, and Ranking Member Sanders, members of the committee, Senator Stabenow from my home State of Michigan, my former colleagues, the Governors of Virginia and Maine, members, thank you for the opportunity to testify today on the benefits of a balanced budget.

Business Roundtable commends this committee for your work to produce a serious budget resolution. Above all, a budget must be a blueprint for action, action that restrains spending, modernizes entitlements, and fosters the robust economic growth required to meet America's many challenges. Business Roundtable's CEOs believe achieving robust economic growth is one of our nation's most important priorities. Further, they believe growth is achievable through policies like business tax reform, expanded trade, investments in physical and digital infrastructure, a fix for our broken immigration system, and a smarter approach to regulations.

This committee understands very well the costs of inaction. An America that remains on a worsening and unsustainable fiscal path, as some of these charts indicated. The doubling of annual deficits within a decade, more than doubling, in fact, from the $483 billion in the fiscal year 2014 to $1.1 trillion in fiscal year 2025. Soaring Federal debt, another concern, rising from more than $7.6 trillion over the next decade, representing 79 percent of GDP by fiscal year 2025. This would be the highest ratio, by the way, since the end of World War II. Federal Government spending itself rising from $3.6 trillion today to more than $6.1 trillion by 2025.

Medicare, Medicaid, Social Security, and net interest on the debt would drive government spending, accounting for about 85 percent of the increase in outlays over the next ten years. Interest payments, which the Chairman referred to, on the debt pose a real and fiscal economic threat. Interest actually represents the fastest growing component of government spending. As a share of the

economy, interest payments will climb from 1.3 percent of GDP to 3.0 percent by 2025, and certainly even higher in future years.

So, the consequences of all of this, the government paying higher interest rates to borrow, producing even higher deficits, leading to even more expensive future borrowing.

Balancing budgets is difficult, no question, but doable. And, again, as the Chairman mentioned, States can show the way. As a new Governor in 1991, Michigan was faced with a $1.8 billion deficit. Business as usual, no longer affordable. But, in the 1990s, Michigan budgets actually did downsize government, reduced the number of State employees, lowered property taxes—Senator Stabenow played a role in that—and reformed welfare and made education a priority. By the end of the decade, we were able to restore Michigan's credit to a triple-A rating, something not seen in the State of Michigan in 25 years. Investment rose. The State's economy grew.

Growth makes budgeting a whole lot easier. It brings in revenues that allow us to address our nation's priorities. A CBO report has compelling data. A sustained increase in the growth rate of GDP of a full percentage point annually reduces the deficit, the budget deficit, by $3.3 trillion over a decade.

And, I want to highlight two priorities from the Roundtable's "Achieving America's Full Potential" report that we believe will contribute and produce substantial economic benefit.

Entitlement reform, been mentioned already. For future generations of American retirees to rely on the assurances of basic retirement security, changes are needed to strengthen and sustain Medicare and Social Security. Business Roundtable supports gradually increasing the eligibility age for full benefits, updating the method of computing cost-of-living adjustments, as the President has proposed, and implementing means testing for higher-income recipients, and expanding competitive models of care much broader within the Medicare system.

Pro-growth tax reform is another one. The U.S. corporate tax system does hinder the ability of American companies to compete in the global economy. The result is less investment in the U.S. and an underperforming economy with fewer job opportunities and, as has been mentioned, lower wages. Roundtable CEOs believe business tax reform has the greatest potential for immediate positive growth.

We have identified two reforms that could put the U.S. at the forefront of global competitiveness, invigorating economic growth and spurring job creation: A competitive corporate rate of 25 percent and a modern international tax system that ends the double taxation of U.S. corporations' foreign earnings and encourages the profits to come home to the U.S. of A. I am certainly happy to address these reforms in more detail in the Q and A.

So, Mr. Chairman, Ranking Member Sanders, members of the committee, thank you again for the opportunity to address the need for a balanced budget. It has many benefits, and the pro-growth policies will help reinvigorate our nation. We look forward to working closely with you.

[The prepared statement of Mr. Engler follows:]

**Statement of John Engler**
**President of Business Roundtable**
**Before the**
**Committee on the Budget**
**United States Senate**
**Hearing on**
**"The Benefits of a Balanced Budget"**
**March 2015**

Good morning, Chairman Enzi, Ranking Member Sanders, and members of the Committee.

My name is John Engler, and I am President of Business Roundtable, an association of CEOs of major U.S. companies operating in every sector of the economy.

Business Roundtable CEOs lead companies with $7.2 trillion in annual revenues and nearly 16 million employees. Member companies comprise more than a quarter of the total market capitalization of U.S. stock markets and invest $190 billion annually in research and development (R&D) – equal to 70 percent of total U.S. private R&D spending. Our companies pay more than $230 billion in dividends to shareholders and generate more than $470 billion in sales for small and medium-sized businesses annually.

Thank you for the opportunity to appear before you today to discuss the pressing need to address America's major fiscal challenges and the economic benefits associated with a balanced budget.

First, I would like to commend this Committee for your work to produce a serious budget resolution. Congressional passage of a serious budget plan would go a long way toward restoring America's confidence in government. In addition, a budget resolution serves the important purpose of informing the national debate on policy and spending priorities that will affect all Americans.

Despite near-term projections of a declining federal budget deficit, annual deficits are projected to begin expanding further in the next few years. For the United States, this is an unsustainable fiscal path. To avoid this fate, America needs a balanced approach to fiscal reform that controls government spending while enacting policies to attain robust economic growth.

Business Roundtable members believe that strengthening the U.S. economy requires the federal budget process to be conducted in a timely, responsible and predictable manner. Recent history has taught us that the American economy pays a steep price for budget showdowns and fiscal uncertainty.

Given the need to reduce future annual federal budget deficits, Congress and the Administration should establish economic growth as a core principle of fiscal and budget

reform. Without healthy growth, it will be dramatically more difficult – if not impossible – to reduce future deficits and secure America's fiscal future.

The highest priority of Business Roundtable is achieving sustained, robust growth of the U.S. economy. A growing economy provides more and better paying jobs – the means by which we can achieve a higher standard of living for all Americans.

We believe that Congress and the Administration must work together to adopt pro-growth policies to put America on a fiscal path toward stability and prosperity. These policies include enacting pro-growth tax reform, expanding U.S. trade, investing in physical and digital infrastructure, fixing our broken immigration system and adopting a smarter approach to regulation.

Ultimately, modernizing Medicare and Social Security is also a critical element for ensuring long-term fiscal stability and our country's prosperity.

### A. The U.S. Federal Budget's Unsustainable Path

While budget deficits have been the subject of fewer headlines over the past year, the business community remains deeply concerned about their impact on the U.S. economy. According to the Congressional Budget Office's (CBO) March projections, federal deficits are expected to remain stable in the near term, but more than double over the next decade. (See figure 1).

Specifically, annual deficits are forecast to increase from $483 billion in fiscal year 2014 to $1.0 trillion in fiscal year 2025. If such a scenario plays out, federal government debt will increase by $7.2 trillion over the next decade, and the debt held by the public will increase to 77 percent of GDP by 2025 – the highest ratio since the immediate aftermath of World War II.[1] As recently as 2007, debt held by the public was 35 percent of GDP.

After four years of trillion dollar deficits between 2009 and 2012, deficits have come down by more than half as the economy gradually recovered from the Great Recession. The improving economy contributed to government revenues increasing by 9 percent from 2013 to 2014, including a 17 percent increase in revenues from corporate income taxes. All of this despite U.S. GDP growth not exceeding 3 percent in any single year.

Clearly, America should pursue a balanced approach to fiscal reform that controls government spending while enacting policies to achieve robust economic growth. Government outlays are projected to increase from $3.5 trillion in 2014 to $6.1 trillion by 2025.[2] Driving this increase will be spending on the entitlement programs. The CBO forecasts that spending on Medicare, Medicaid and Social Security along with net interest on the debt will account for 85 percent of

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[1] Congressional Budget Office. (March 2015). "Updated Budget Projections: 2015 to 2025."
[2] Ibid.

the increase in outlays over the next 10 years. By mid-century, in fact, spending on Social Security, government health-care programs and interest on the debt would equal 100 percent of revenues – leaving discretionary spending a thing of the past.

If we do not meet this challenge now, the future becomes ominous. Spending on government entitlement programs is projected to continue to grow faster than the economy over the next decade and beyond, more than offsetting projected decreases in discretionary spending as a share of the economy. Such rapid increases in government spending will result in slower economic growth and reduce workers' wages and limit the earnings of future generations. Compound that through higher taxes that further reduce employment and investment, or through larger deficits that draw private capital from productive, wage-increasing and job-creating investments, and you have a result that should be terrifying.

Net interest payments on the debt represent the fastest growing component of government spending. As interest rates rise and annual deficits continue, the government's cost of financing its borrowing will increase sharply from $229 billion in fiscal year 2014 to $808 billion in fiscal year 2025. As a share of the economy, net interest payments will climb from 1.3 percent of GDP in 2014 to 2.9 percent in 2025.[3] CBO's long-term projections show net interest payments continuing to increase relative to the size of the economy in the decades beyond. (See figure 2). The large and growing debt will likely further increase the interest rate the government must pay to borrow funds. With public debt approaching 100 percent of GDP, each one percentage point increase in interest rates translates into an increase in the deficit of one percentage point of GDP. The hard fact is these growing deficits will in turn further drive up government debt and future borrowing costs.

Mr. Chairman, the federal government is on an unsustainable and dangerous fiscal path that threatens the U.S. economy. It will be important to reduce future deficits and achieve more fiscally sound budget management, and to do this by passing laws and adopting regulations that support economic growth rather than hamper it.

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[3] Ibid.

**B. Budget Discipline in Michigan**

As a former governor of Michigan, I know first-hand the difficulties of reining in spending. Budget discipline has been a priority for me throughout my public life. It's a matter of principle and good policy.

As a newly elected governor in 1991, my state was faced with a $1.8 billion deficit. Like almost all states, Michigan's constitution requires a balanced budget. We could have played the usual budgetary games: shift funds, extend payments, borrow against the future or simply raise taxes. But I proposed, as did the Michigan Legislature, that the state and its people could no longer accept business as usual.

In the 1990s Michigan's budgets downsized state government, reduced the number of state employees, reduced property taxes, reformed welfare and made education a priority. These changes served the people of Michigan well. With a balanced budget and a smaller tax burden, Michigan became attractive for investment and a leader in recruiting new businesses.

During my tenure as governor from 1991 to 2003, I was privileged to sign major tax changes into law, saving Michigan taxpayers some $32 billion. Some 800,000 new jobs were created and Michigan's unemployment rate went down to a new low. Finally, after 25 years, we were able to restore Michigan's credit to a AAA rating.

At the same time, governors in other states were also enjoying success. The lesson for this Committee is this: Balanced budgets are achievable and the economic benefits of responsible budgets are clear. We see this truth not only by looking back at Michigan but also other states – e.g., Wisconsin, Ohio and Indiana – where leaders made difficult but necessary policy decisions.

**C. Deficit Reduction Remains a National Imperative**

Reducing the federal budget deficit is a national imperative. Business Roundtable believes that the most important contributor to future U.S. economic growth can be private sector investment. This is the investment in equipment, software, intellectual property and new factories that increases the productivity of American workers, supports higher wages and job creation, and leads to the economic growth that supports increased living standards now and for future generations.

Government budget deficits reduce private sector investment and are bad for the American economy for a number of reasons. First, large budget deficits drive up the cost of capital and "crowd out" private investment. As financial conditions normalize in the coming years, large budget deficits will place significant upward pressure on interest rates and reduce the credit needed for the housing industry and to support private investment. Lower private investment spending means a lower U.S. capital stock – fewer new factories, with less equipment and less R&D to support American workers. This in turn will mean lower productivity growth, lower

wage growth and lower GDP growth. The result is a lower living standard for the American people.

Second, large budget deficits and government debt levels create risks that undermine confidence in financial markets and can cause painful financial crises, with real and lasting repercussions throughout the economy. One never knows exactly when a collapse in investor confidence will occur or what might serve as the trigger. However, as events in recent decades have illustrated, no country is immune to such risks. It is not just countries with extremely high debt levels, such as Greece, that have been damaged. Weak fiscal conditions in South Korea, the United Kingdom and Sweden, for example, have contributed to sharp losses of confidence in these markets, collapses in currency values and spikes in interest rates.[4] The U.S. business community believes it is irresponsible to take any unnecessary risks of this sort.

Large and persistent budget deficits also generate policy uncertainty. Even if a full-blown crisis is avoided, research shows that policy uncertainty itself can undermine consumer and business confidence. (See figure 3).[5] Even mildly lower levels of business confidence and capital investment can have depressing effects on growth that cumulate over time. (See figure 4.)[6]

Third, large budget deficits can restrict the range of government policy responses in the face of unexpected and severe events, such as a deep recession, a catastrophic natural disaster, or a national security crisis. Such events often precipitate a rapid increase in spending or a sharp decrease in revenues that could rapidly widen the deficit. If the government's books are in good shape at the start of such a challenge, the situation will be more manageable. However, if governments are running major deficits, the additional burden will significantly increase the risk of a financial crisis, or limit the government's capacity to respond in general.

Finally, large budget deficits increase the risk that debt levels will rapidly spiral out of control if there are shifts in interest costs or sharp reductions in economic growth. The average yield on all U.S. government debt is about 2 percent today – one of the lowest rates in American history.[7] The CBO forecasts the yield on the 10-year Treasury note to increase from about 2 percent today to 4.6 percent by the end of the decade.[8] If inflation expectations shift or if foreign investors take a dimmer view of U.S. investment prospects, this yield could move up significantly in coming years. Increased interest costs could rapidly increase the deficit and

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[4] Currency and financial crises in the 1990s in South Korea, the U.K., and Sweden were precipitated by outsized budget deficits. Budget deficits in South Korea, the U.K., and Sweden peaked at 4.6%, 7.6%, and 9.0% of GDP, respectively, prior to each country's crisis. All data taken from IFO Economic Situation Surveys.

[5] See Baker, S., Bloom, N., and Davis, S. (January 2013). "Measuring Economic Policy Uncertainty". Chicago Booth Research Paper no.13-02. Retrieved from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2198490.

[6] Macroeconomic Advisors. (October 2013). "The Cost of Crisis-Driven Fiscal Policy", prepared on behalf of the Peter G. Peterson Institute. Retrieved from http://pgpf.org/special-reports/the-cost-of-crisis-driven-fiscal-policy.

[7] Treasury Direct. (February 2015). "Public Debt Average Interest Rate: February 2015". Retrieved from http://www.treasurydirect.gov/govt/rates/pd/avg/2015/2015_02.htm.

[8] Congressional Budget Office. (January 2015). "The Budget and Economic Outlook: 2015 to 2025", page 9.

create a vicious circle of higher interest costs and higher deficits that undermine growth and job creation. Again, these risks threaten economic stability.

**D. Policy Solutions to Improve America's Fiscal Future**

A sustained effort to reduce budget deficits in coming years is a national imperative. "How" we reduce the debt is just as important as "how much" we reduce it. Business Roundtable believes that we need to move toward a balanced budget with a collection of actions that are responsible, balanced, and that enhance growth. Today, I will discuss three components of a balanced solution that our elected leaders must address:

**1. Strengthen Medicare and Social Security**

One priority is dealing with the entitlement programs. Spending on Social Security, Medicare, Medicaid, and other government health programs is set to rise from 9.7 percent of gross domestic product in 2014 to 11.9 percent by 2025. This is an increase of $1.6 trillion – significantly more than enough to fund the Legislative Branch, Judicial Branch and Executive Office of the President for an entire decade. Despite this looming fiscal danger, entitlement spending has not received the necessary focus of Congress, even throughout the budget battles of the last several years.

For future generations of American retirees to rely on the assurance of basic retirement security, changes are needed to strengthen and sustain Medicare and Social Security.[9] Our proposals would gradually bring these programs into alignment with America's fiscal and demographic realities while fully protecting current retirees and those near retirement. Our goal is to preserve the safety net for future generations. Specifically, Business Roundtable supports:

- Gradually increasing the eligibility age for full benefits,
- Updating, as suggested by the President, the method of computing cost-of-living adjustments,
- Implementing means testing for higher-income recipients and expanding competitive models of care within Medicare.

Acting sooner rather than later means the changes can be gradual, current retirees and those near retirement would be fully protected, and the programs can be strengthened, which preserves the programs for future generations.

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[9] Business Roundtable. (January 2013)."Social Security Reform and Medicare Modernization Proposals", available at http://businessroundtable.org/resources/social-security-reform-and-medicare-modernization-proposals.

**2. Enact Pro-Growth Tax Reforms**

Another priority for reducing future budget deficits should be to promote faster economic growth, and nowhere can this be achieved more effectively than through tax policy. A powerful symbiotic relationship exists between growth and sustainable budgets. Policies focused on growth can expand the American economic pie, reduce relative debt burdens, and put the country on a more sustainable fiscal path. CBO estimates that adding a sustained one-tenth of one percent to GDP growth would reduce budget deficits by more than $300 billion over a decade. A sustained increase in the growth rate of GDP of a full percentage point annually would reduce the budget deficit by $3.3 trillion over a decade.[10]

To reinforce that point on growth: Had the United States not experienced the 2008 recession and had maintained the previously forecasted economic growth, total economic output between 2008 and 2017 would have been $12 trillion greater. Naturally, that kind of economic performance makes addressing budget priorities a much less disagreeable task.

Pro-growth tax reform is particularly well-suited to boosting America's economic output and easing our fiscal position. Today, the U.S. corporate tax system hinders the ability of U.S. companies to grow and compete in the world economy with the consequence of less investment in the United States, and a weaker economy with fewer job opportunities and lower wages. The ability of American companies to compete and invest abroad is vital for opening foreign markets to U.S.-produced goods and expanding the scope of investments in R&D and other activities in the United States.

The Business Roundtable key tax reform recommendations for corporations include:

- Setting the corporate tax rate at a competitive 25 percent; and
- Adopting a modern international tax system (a "territorial-type" tax system) that ends the taxation of U.S. corporations' active foreign earnings above and beyond foreign taxes paid and permanently removes the penalty for returning foreign earnings to the United States, thereby aligning the U.S. system with the tax systems of our major trading partners.

Business Roundtable supports these reforms being undertaken in a fiscally responsible manner, understanding that rate reduction will require base broadening such as elimination or modification of tax credits and deductions to offset the revenue loss. As for the U.S. international tax system, reform should be accompanied by appropriate safeguards to protect America's tax base, consistent with the rules of our major trading partners.

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[10] Congressional Budget Office. (January 2015). "The Budget and Economic Outlook: 2015 to 2025," page 133.

These reforms would have major growth effects for the economy and for the budget. Business Roundtable commissioned Rice University Professors Diamond and Zodrow to independently analyze former Ways and Means Chairman Dave Camp's proposed Tax Reform Act of 2014.[11] Among other benefits, they concluded: The legislation would increase U.S. annual GDP by 0.9 percent two years after enactment and by 2.2 percent after 10 years. Smart tax reform proposals such as these would simultaneously enlarge the U.S. economic pie and substantially close the fiscal gap.

Business Roundtable believes that business tax reform that results in a modern tax system with competitive rates and competitive international tax rules would be one of the most effective means of accelerating business investment, boosting job creation and wages, and providing greater opportunity for America's working families. Enactment of a competitive tax system in a fiscally responsible manner while restraining spending growth would serve as a powerful magnet for investment and job creation, reversing recent economic decline and stagnation, and securing the economic well-being of American families now and for future generations.

**3. Pass Immigration Reform to Reduce Deficits**

Immigration reform is another priority that would brighten the country's long-term fiscal outlook. The immigrant population, on average, is younger than the overall U.S. population, and immigration reform policies that resolve the status of undocumented immigrant workers and establish the rules for their participation in the U.S. economy would help offset the effects of the country's aging workforce and contribute new revenue to the federal government through collection of payroll and income taxes.[12]

In an analysis of immigration reform legislation that passed the Senate in 2013, CBO found that enacting immigration reform legislation would, on net, decrease federal budget deficits by $197 billion over the next 10 years and by $700 billion over the subsequent decade.[13]

The Bipartisan Policy Center, using slightly different economic assumptions, estimated that federal deficits would decrease by almost $1.2 trillion over a 20-year period.[14] Further, the Social Security Administration estimated that legislation would be a net positive for the program's finances, generating more than $275 billion in new revenue for Social Security by 2024.[15]

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[11] Diamond, J. and Zodrow, G, Tax Policy Advisers LLC. (March 2014). "Dynamic Macroeconomic Estimates of the Effects of Chairman Camp's 2014 Tax Reform Discussion Draft," available at http://businessroundtable.org/media/news-releases/new-study-shows-ways-and-means-committee-chairman%E2%80%99s-tax-draft-would-boost-us-gdp.

[12] See Ortman, J, Velkoff, V, and Hogan, H. (May 2014). "An Aging Nation: The Older Population in the United States." Census Bureau. Retrieved from http://www.census.gov/prod/2014pubs/p25-1140.pdf.

[13] Congressional Budget Office. (2013). "The Economic Impact of S. 744, the Border Security, Economic Opportunity, and Immigration Modernization Act."

[14] Bipartisan Policy Center. (2013). "Immigration Reform: Implications for Growth, Budgets, and Housing."

[15] Social Security Administration. (2013). "Letter to Senator Marco Rubio." Office of the Chief Actuary, May 8, 2013.

In all, economic studies performed by researchers from across the political spectrum that consider both the costs and benefits of immigration reform demonstrate that the budgetary impacts are overwhelmingly positive. As such, enforceable and common-sense immigration policies should be a component of government efforts to achieve long-term fiscal stability.

**E. Conclusion**

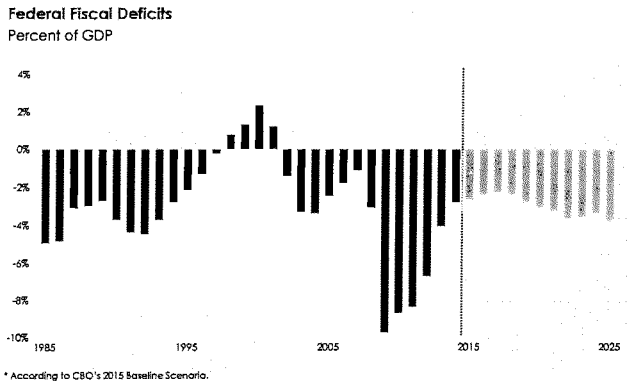
Mr. Chairman, thank you again for the opportunity to discuss an issue that I know both you and I consider an economic imperative. Business Roundtable supports this Committee's dedication to fiscal stability and is ready to support smart, effective and responsible policies that will help us achieve this goal.

Business Roundtable believes that many policies should be enacted to achieve more vigorous economic growth in a fiscally responsible manner. My testimony has highlighted just three areas – modernizing entitlements, tax reform, and fixing our broken immigration system. As indicated at the start of my testimony, a "pro-growth" agenda should also embrace expanded trade, investment in physical and digital infrastructure and a smarter approach to regulation.

We have a lot of work to do, but we are encouraged by your efforts to achieve fiscal stability. I am happy to answer any questions you may have.

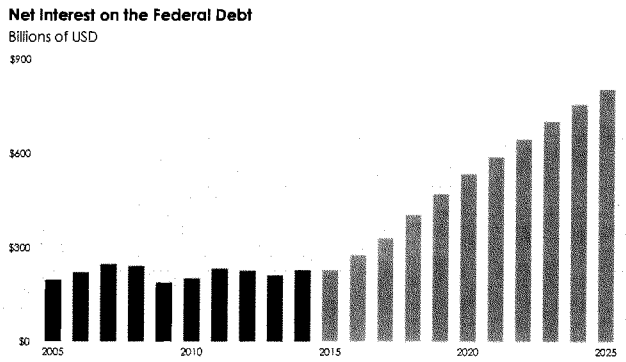
## A. *Charts*

**Figure 1: Federal Fiscal Deficits, 1985-2025**



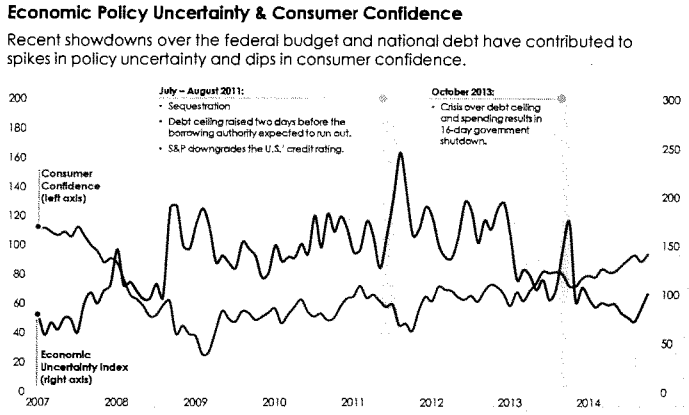

Source: Congressional Budget Office. (March 2015). "Updated Budget Projections: 2015-2025", page 2.

**Figure 2: Net Interest on the Federal Debt**



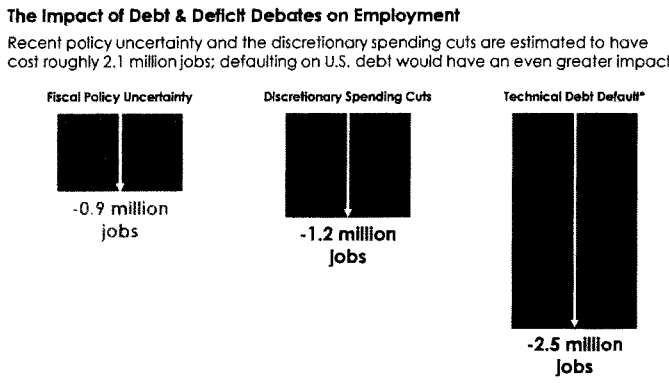

Source: Congressional Budget Office. (March 2015). "Updated Budget Projections: 2015-2025", page 2.

**Figure 3: Economic Policy Uncertainty and Consumer Confidence**




Source: Baker, S., Bloom, N., and Davis, S. (January 2013). "Measuring Economic Policy Uncertainty". Chicago Booth Research Paper no.13-02. Retrieved from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2198490.

**Figure 4: The Impact of Debt and Deficit Debates on Employment**




* Based on a hypothetical scenario in which the U.S. experiences a brief, technical debt default that is quickly resolved.

Source: Macroeconomic Advisors. (October 2013). "The Cost of Crisis-Driven Fiscal Policy", prepared on behalf of the Peter G. Peterson Institute. Retrieved from http://pgpf.org/special-reports/the-cost-of-crisis-driven-fiscal-policy.

Chairman ENZI. Thank you, Governor.
Ms. MACGUINEAS.

**STATEMENT OF MAYA MacGUINEAS, PRESIDENT, COMMITTEE FOR A RESPONSIBLE FEDERAL BUDGET**

Ms. MACGUINEAS. Good morning. Chairman Enzi, Ranking Member Sanders, and members of the committee, thank you for inviting me here today to talk about this important topic.

I am going to make several main points today in my remarks. The first is that our deficit and debt problems are still far from solved. The second is that having a fiscal goal is key to making progress. Third, there are many advantages to getting the debt to more manageable levels than where it currently is. And, finally, policy makers do need to avoid backsliding and adding more to the debt than we are already on the path to do.

So, let me start by saying that I think the United States has the potential for a real economic renaissance. We just heard from the head of the IMF that we are described as the best economic performer, and that is really remarkable coming out of the terrible, terrible economic downturn that we just went through. Still, we are nowhere close to being out of the woods, and the fabric of a successful economy will be strong production, good jobs, investment in the future, and a growing standard of living. The best solutions will enhance our competitiveness, grow our economy, and make sure that the benefits of that growth are spread more broadly. Controlling our debt is a key factor to achieving all of these objectives.

So, let me start by recognizing the good news. The deficit has come down by about two-thirds since its peak in 2009, and health care cost growth has slowed significantly, leading to a savings of a trillion dollars from what we had been projecting.

That said, our debt situation is still very troubling. Our debt is twice the historical average relative to the economy. Interest payments, as the Governor just said, are the single fastest growing part of the budget. Our budget favors consumption over investment, and we are dangerously short-sighted in how we budget.

There also seems to be a near endless list of political reasons not to make any changes for getting this situation under control when, really, there are no economic reasons for delaying figuring out the kind of changes that we are going to put in place.

Some have pointed to the recent decline in the deficit as a reason not to worry about the situation, but keep in mind that the 66 percent decline followed an unprecedented increase in the deficit of 780 percent. And, the decline is temporary. Deficits are expected to hit a trillion dollars again by 2025.

Moreover, I would argue that the short-term deficit was never the primary concern, and it should not have been, given that we are still focusing on helping the economy to recover. A much smarter approach would have been to include real reforms of the tax code and entitlement reform than the kind of short-sighted and blunt tools that were used to bring the deficit down and to have focused on controlling the debt for the longer term.

More troubling, still, is our national debt. At 74 percent of GDP, it is currently the highest it has been as a share of the economy since World War II, and it is more than double the size of the debt

as a share of the economy compared to when we went into the national crisis in 2007, and having very low debt levels at the time gave us the flexibility to respond.

So, there is no question that our projected deficits and debt are too high, and ideally, what we should do is strive to balance the budget over a business cycle, which would allow us to save money when times are good and spend more money when the economy is in bad shape.

The first step towards getting towards balance is getting the debt on a downward path as a share of the economy, and that comes with a number of benefits. Starting with economic benefits, it leads to greater investment and economic growth, and from our estimates based off of CBO numbers, getting the budget to balance would lead to an increase in the size of the economy of more than two percent in 2025 and more than ten percent in 2040.

That leads to higher income and wages. Again, using CBO's rule of thumb, the increase due to a balanced budget in wages would be $6,000 per person per year, or $200,000 in additional income for an average worker.

It also leads to lower interest rates. Under a balanced budget, according to CBO, the interest rates could be roughly one point lower than under current law. So, to put that another way, if you think about a family with a mortgage of $300,000, that could lead to savings of $60,000 over the life of that mortgage.

It also would lead to declining interest payments. Right now, we are projected to be spending over $800 billion in interest payments by the end of the budget window, certainly, that is money that could be better spent on many other priorities if we did not have such high payments.

And, the fiscal flexibility that we were allowed when we entered the crisis, because our debt levels were low, was instrumental in helping us get out of the crisis. Were we to go into another crisis—and there will be one sometime—with debt levels as high as they are, we would be constrained in a way that we were not before.

And, finally, getting rid of high debt levels, getting rid of them, balancing your budget, reduces the risk of a fiscal crisis. CBO has warned that the larger a government's debt, the greater the risk of a fiscal crisis.

There is a final advantage, also, I think, of getting a balanced budget, which is it is an easy, tangible and measurable goal that can be easily explained to the American people, and that has been shown to help keep plans on track. Right now, there are virtually no limits on borrowing, no agreed upon fiscal goal, and if there were one, policy makers would be required to show their preferred paths for getting there and then we would have a real discussion on the budget. We would discuss the various trade-offs of the various plans to achieve that goal, whatever it is.

Finally, I encourage all of us in this coming year not to take a step backwards, and I think there is a very real risk there. Last year, lawmakers added $100 billion to the debt beyond what was projected from a variety of things that they either did not want to pay for or that they used gimmicks to pay for. This year, we will face a number of these fiscal speedbumps, from SGR, to highway,

to tax extenders. Not paying for them could add another $2 trillion to the debt.

So, I want to close by saying that controlling America's debt is a key part of a comprehensive economic growth plan. We need to grow our economy. We need to keep our businesses competitive. We need to invest in our workers, innovations, and infrastructure. We need to ensure that the gains from growth are broadly shared. And, we need to control our debt for any of these efforts to be effective.

To truly tackle our fiscal challenges, we are going to need to reform our tax code, we are going to need to strengthen our entitlement programs, and we are going to need to control and better target our spending. All of those things have to be on the table.

The payoffs from responsible fiscal policies are immense, and I really do think that they are the key to getting this economic growth to stick and take off and help American families.

So, thank you to the committee for hosting this hearing today.

[The prepared statement of Ms. MacGuineas follows:]

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Hearing before the Senate Budget Committee
**Benefits of a Balanced Budget**
Wednesday, March 11, 2015

Testimony of Maya MacGuineas
Committee for a Responsible Federal Budget

Chairman Enzi, Ranking Member Sanders, and Members of the Committee, thank you for inviting me here today to discuss the important topic of how our country can best budget for the future. The fiscal challenges we face are significant, and I appreciate the opportunity to discuss the types of solutions that can move us towards a healthier economy.

I am Maya MacGuineas, president of the Committee for a Responsible Federal Budget and head of the Campaign to Fix the Debt. The Committee for a Responsible Federal Budget is a non-partisan organization dedicated to educating the public about and working with policymakers on fiscal policy issues. Our board includes past directors and chairs of the Office of Management and Budget, the Congressional Budget Office, the Federal Reserve System, the Treasury Department, and the Budget Committees. Our partner organization, Fix the Debt, is a nonpartisan movement that mobilizes key communities – including leaders from business, government, policy, and academia – who believe lawmakers must work together to deal with the nation's fiscal challenges to help protect our citizens and grow the economy.

I will make several main points today:

1. Our deficit and debt problems are far from solved
2. Having a fiscal goal is a key part of budgeting
3. There are many advantages to getting the debt to more manageable levels
4. Policymakers should avoid backward steps that add to the debt

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**Our Deficit and Debt Problems are Far From Solved**

The United States has the potential for a real economic renaissance. We're still coming out of the terrible downturn, but we were recently described by the head of the IMF as the best performer of the advanced economies.[1] Low energy prices, strong consumer demand and impressive job growth and all assisting in our economic recovery. Given the damage and severity of the downturn, this is tremendous news.

But we are not yet out of the woods. We face very real economic challenges and we need to make sure the economic recovery holds. The fabric of a successful economy is strong production, good jobs, investment in the future, and a growing standard of living. The best solutions would enhance our competitiveness, grow our economy, and make sure the benefits of that growth are shared broadly.

Controlling our debt is a key factor in achieving all of these critical national objectives.

And on this front, we are not doing well. Our debt is twice the historical average relative to the economy, and it is on an unsustainable path. Interest payments are projected to be the single fastest growing part of the budget; our budget favors consumption rather than investment, which does not bode well for future growth; and we are dangerously short-sighted in how we budget. There also seems to be a near endless list of *political* excuses about why we should not do anything to get our debt under control, while there are no *economic* reasons to delay coming up with solutions to our medium and long-term debt challenges. Needed changes, which are manageable now, will get much more difficult over time.

Let me dig into our current debt situation a little deeper.

To start, let us recognize the good news. The deficit has come down by about two-thirds since the 2009 peak. On top of that, significant deficit reduction has been enacted – mainly through higher taxes on upper income households and lower discretionary spending, including from sequestration. Furthermore, health care costs are growing much slower than anticipated, leading to $1 trillion less spending from 2012-2021 compared to what we thought in 2011 and over half of those reductions come from Medicare.[2]

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[1] See the appearance of Christine Lagarde on MSNBC's *Morning Joe*. March 4, 2015. Available at http://www.msnbc.com/morning-joe/watch/study--equality-laws-are-good-for-the-economy-407975491726.

[2] A fuller, though slightly dated analysis is available from CRFB, "The $900 Billion Slowdown in Federal Health Care Spending," May 6, 2014, http://crfb.org/blogs/900-billion-slowdown-federal-health-care-spending.

However, the good news has led some to conclude that we no longer need to address our fiscal challenges—a dangerous conclusion.

First, this 66 percent decline in the deficit since 2009 follows an unprecedented ***780 percent increase*** in the prior two years, when deficits rose from $160 billion to *$1.4 trillion.*

Of course, that huge increase in deficits was mostly the result of the Great Recession (and the subsequent decline largely the result of the recovery). Specifically, large drops in employment, wages, profits, and capital gains during the Great Recession all led to much lower revenue collection and higher spending on countercyclical programs like unemployment benefits and SNAP. Meanwhile, the economic rescue cost hundreds of billions of dollars, and the money injected into the financial system and for the bailout of Fannie Mae and Freddie Mac added to the deficit.

Likewise, much of the recent decline in deficit is largely due to the economic recovery. As unemployment is falling and profits are rising, we're seeing higher revenue and lower countercyclical spending. Meanwhile, nearly all federal stimulus spending has tapered off. And instead of the government paying money to financial firms and Fannie Mae and Freddie Mac, it's *receiving* money from those organizations. On top of that, deficits remain low in part due to the Federal Reserve's continued actions to fight deflation and support full employment, which have resulted both in historically low interest rates paid by the government and higher Federal Reserve profits remitted back to the Treasury.

There have also been policy changes that have reduced the deficit, notably the fiscal cliff deal, which raised taxes on wealthier Americans, and cuts in discretionary spending from caps and the sequester. However, depending on how you measure it, these changes only account for about one-fourth of the drop in the deficit since 2009. Furthermore, I would also argue that these have not been the wisest of policies to help bring down the deficit, especially given that they are focused mainly on the short-term when reductions in the short-term deficit is far less important than a reduction in the medium- and long-term debt, given that we are still focusing on helping the economy recover.[3] A much smarter approach would have included real reforms of the tax code and entitlement programs.

Importantly, the recent reductions we've seen in the deficit are only temporary.

Under CBO's current law projections, deficits will begin to rise rapidly after 2017, from today's levels of about $490 billion (2.7 percent of GDP) this year to more than *$1 trillion*

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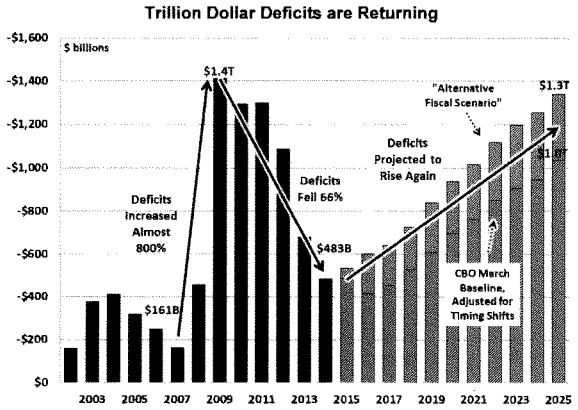
[3] For more information, see my piece "Yes, the Deficit Is Smaller. But That Wasn't the Main Problem," Oct 21, 2014, http://blogs.wsj.com/washwire/2014/10/21/yes-the-deficit-is-smaller-but-that-wasnt-the-main-problem/.

(3.8 percent of GDP) by 2025. In other words, the deficit is only projected to shrink for the next three years, and trillion-dollar deficits are projected to come back within a decade. Normally our group worries about politicians pushing hard choices into the future and then never really doing them. But in this case, I would have traded larger deficits today as the economy continues to recover, for more progress on the future imbalances we face as a result of continued structural deficits, growing healthcare costs, the aging of the population, and growing interest payments.

Unfortunately, CBO's already bleak projections might be too optimistic, since they assume that lawmakers won't further increase the deficit, including by continuing current or recent policies as they often have in recent years. Under CBO's "Alternative Fiscal Scenario, which includes more pessimistic projections by assuming temporary tax policies are continued, the sequester is repealed, and a permanent "doc fix" is enacted, trillion-dollar deficits will return by 2021 and the deficit will reach more than $1.3 trillion in 2025.[4]

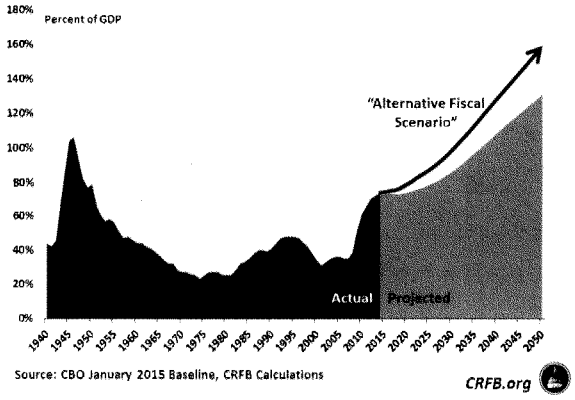



[4] CBO has not published an Alternative Fiscal Scenario since July 2014, when it represented additional ten-year deficits approximately $2 trillion above the current law baseline. CRFB constructs a similar "Alternative Fiscal Scenario" using estimates that CBO provides, which combine for about an additional $2.5 trillion in deficits over ten years. The alternatives used are: repealing the sequester, extending all expiring tax provisions, permanently averting the doc fix.

More troublesome than our rising deficits is our too large and growing national debt. Over the same period that nominal deficits fell by 66 percent, our national debt grew by roughly 70 percent – from $7.5 trillion in 2009 to $13 trillion today. And based on CBO projections, debt will continue rising, reaching $21 trillion within a decade under current law and nearly $24 trillion under the more pessimistic scenario.

Arguably the most important metric of a country's fiscal health is its debt-to-GDP ratio. At 74 percent of GDP, debt is currently the highest it has ever been as a share of the economy in this nation's history, other than around World War II. This is more than *double* the size of our national debt back in 2007 before we entered the economic crisis. And after remaining roughly stable through 2020 at this record-high level, debt-to-GDP will again grow reaching 77 percent of GDP by 2025, exceeding the size of the economy before 2040, and doubling it by the 2070s. Under our approximation of CBO's Alternative Fiscal Scenario, debt would reach 84 percent by 2025, exceed the size of the economy by the early 2030s, and double it by the 2060s.

**Debt Heights Will Be Unprecedented**




This pace of debt growth is clearly unsustainable. As the non-partisan Congressional Budget Office (CBO) explained in the January 2015 baseline:

> *Such large and growing federal debt would have serious negative consequences, including increasing federal spending for interest payments; restraining economic growth in the long term; giving policymakers less flexibility to respond to unexpected challenges; and eventually heightening the risk of a fiscal crisis.*

Similar warnings have been issued by Chair of the Federal Reserve Janet Yellen. Yellen said:

> *I also worry that if we were to again be hit by an adverse shock, that there's not much scope to use fiscal policy. It was used in the early years after the financial crisis -- we ran large deficits -- but in the course of doing that, the debt-to-GDP ratio rose. And were another negative shock to come along, it's questionable how much scope we would now have to put in place even on a temporary multiyear basis expansionary fiscal policy, and I think it's important to deal with these issues – for the Congress to do so.*[5]

In one of his last testimonies in front of Congress, Federal Reserve Chairman Ben Bernanke said:

> *To promote economic growth and stability in the longer term, it will be essential for fiscal policymakers to put the federal budget on a sustainable long-run path. Importantly, the objectives of effectively addressing longer-term fiscal imbalances and of minimizing the near-term fiscal headwinds facing the economic recovery are not incompatible. To achieve both goals simultaneously, the Congress and the Administration could consider replacing some of the near-term fiscal restraint now in law with policies that reduce the federal deficit more gradually in the near term but more substantially in the longer run.*[6]

### Benefits of Reducing the Debt and Balancing the Budget over the Business Cycle

The last time this country seriously confronted our deficit challenges in the 1990s, a series of three major deficit reduction agreements – in 1990, 1993, and 1997 – ultimately lead to a balanced budget, even generating surpluses between 1998 and 2001.

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[5] Yellen, Janet, *Semiannual Monetary Policy Report to the Congress*, Testimony Before the Senate Committee on Banking, Housing, and Urban Affairs, February 24, 2015, http://www.federalreserve.gov/newsevents/testimony/yellen20150224a.htm and Lagarde's remarks at the Council on Foreign Relations, January 15, 2015, http://www.cfr.org/economics/christine-lagarde-new-multilateralism-global-economy/p35973.

[6] Bernanke, Ben, *The Economic Outlook*, Before the Joint Economic Committee, May 22, 2013, http://www.federalreserve.gov/newsevents/testimony/bernanke20130522a.htm

There is no question that long-term deficits are projected to remain far too high.

Ideally, our country would balance the budget over the business cycle. This doesn't mean we should balance the budget every year. In fact, it makes economic sense to borrow during recessions, and save during times of higher growth. But getting to balance on average would allow us to save when the economy is strong and have the government help inject more money into the economy when it is weak. Yet we seem much better at the borrowing part than the saving part. As John Maynard Keynes once said:

> *"Just as it was advisable for the Government to incur debt during the slump, so for the same reasons it is now advisable that they should incline to the opposite policy… The boom, not the slump, is the right time for austerity at the Treasury."*[7]

The reality is that balancing the budget for any sustained period is probably not in our immediate future. Our projected deficits are too large for us to reach balance in the very near future without making some extremely difficult choices about what spending to cut and/or taxes to raise. For instance, balancing the budget starting next year would require $7.2 trillion of deficit reduction over the next decade. Depending on the path of savings, balancing the budget by 2025 would require roughly $5.5 trillion of deficit reduction. For perspective, $5.5 trillion is 8 times as much as raised in the fiscal cliff deal, 7 times as much as the initial spending reductions in the Budget Control Act, and 65 times more than the gross savings in the Ryan-Murray Bipartisan Budget Act.

**Ten-Year Savings Needed to Reach Fiscal Targets**

| Target | Current Law | Alternative Fiscal Scenario |
|---|---|---|
| Stabilize Debt at 2015 Level through 2025 | $0.8 trillion | $3.3 trillion |
| Reduce Debt to 70% of GDP by 2025 | $1.9 trillion | $5.3 trillion |
| Reduce Debt to 60% of GDP by 2025 | $4.7 trillion | $7.2 trillion |
| Balance the Budget by 2025 | ~$5.5 trillion | ~$8.0 trillion |
| Balance the Budget Every Year through 2025 | $7.2 trillion | $9.7 trillion |

Source: CRFB calculations based on Congressional Budget Office documents and assuming deficit reduction is gradually increased over the budget window. These numbers are illustrative representations of one potential savings path. All numbers are rounded.

[7] Keynes, John Maynard. *The Collected Writings of John Maynard Keynes,* Volume 11, ed. by Donald Moggridge, Cambridge University Press, p. 390.

And the political system has shown very little willingness to confront even small difficult choices let alone the large ones. The polarization between the parties and the unwillingness of many to compromise has made this even more difficult.

The first step towards balance will be keeping our deficits from significantly increasing again and getting to at least a place where the debt is shrinking relative to the economy. Once the debt is on a downward path, we will start to see a number of the benefits that come with balance.

These important benefits include:

- **Greater Investment and Economic Growth.** When the government borrows, it diverts savings away from productive private investments and toward government bonds. This ultimately "crowds out" new growth opportunities and in doing so slows GDP growth. Based in part on CBO projections, we estimate balancing the budget within a decade could increase the size of the economy above current law projections by more than 2 percent in 2025 and almost 10 percent by 2040.
- **Higher Income and Wages.** Faster economic growth translates to a higher average income. Using the Congressional Budget Office's rules of thumb, we calculate that a balanced budget would increase per-capita GNP (or roughly average income), by 7 percent more in 2040, relative to following current law. In today's dollars, that's a $6,000 annual wage increase per person. And over a 40-year career starting today, it represents $200,000 of additional income for an average worker.
- **Lower Interest Rates.** Growing national debt can drive up interest rates throughout the economy, leading to higher interest payments on mortgages, car loans, student loans, and credit card debt. Under a balanced budget, according to CBO's rules of thumb, interest rates could be roughly 1 point lower than under current law. Put another way, a family with a $300,000 mortgage could expect to pay at least $60,000 less over the course of the mortgage. While interest rates have not been an issue in recent years, keeping them low would provide significant benefits to families.
- **Declining Government Interest Payments, Thus Freeing Up Resources.** Under current law, the government will spend about $230 billion on interest payments this year, and is projected to spend $810 billion in 2025 and $2.5 trillion in 2040. Ten years from now, interest on the debt is projected to consume more of the budget than on research, education, highways, and all spending on children combined.[8] Were we to get to balance in 2025, interest would consume about $630

[8] CRFB calculations based on various Congressional Budget documents and *Kids' Share 2014: Report on Federal Expenditures on Children Through 2013, published by The Urban Institute in September 2014.*

billion in 2025 and about $960 billion in 2040, leaving more room for other important priorities.

- **Increased Ability to Respond to Problems.** Governments often borrow to address unexpected events, like wars, financial crises, and natural disasters. This is relatively easy to do when the federal debt is small as a share of the economy. However, with a large and growing federal debt, government has fewer options available. For example, borrowing was a helpful response to the financial crisis several years ago, increasing spending and cutting taxes in order to stimulate the economy. However, the federal debt is more than double what it was in 2007 as a share of GDP and we could be dangerously constrained were we to face another crisis while debt is this high.
- **Reduced Risk of Fiscal Crisis.** If the debt continues to climb, at some point investors will lose confidence in the government's ability to pay back borrowed funds. Investors would demand higher interest rates on the debt, and as a result interest rates could rise sharply and suddenly, creating a debt spiral crisis, as we have seen in other nation's when their debt is no longer manageable. While there is no country historically analogous to the United States position in the world economy, so there's no sound mechanism for determining if and when a fiscal crisis could occur, CBO warns that, "the larger a government's debt, the greater the risk of a fiscal crisis."[9]

Importantly, many of the benefits to balanced budget described above would also apply to other amounts of deficit reduction. But one major advantage of specifically getting to a balanced budget is that it is a tangible, easily measurable goal that can be easily explained to the American people. Numerous international and domestic examples show the power of having fiscal goals. CRFB published a paper "Fiscal Turnarounds" that showed "Credible fiscal rules and fiscal goals… helped policymakers and taxpayers maintain discipline" in six countries that turned around large deficits and debt: Canada, Denmark, Finland, Ireland, and Sweden.[10] Our *Better Budget Process Initiative* also explained the benefits of an easy-to-understand budget in *The Budget Act at 40: Time for a Tune Up?*.

It is critical that the country pick a fiscal metric. Right now, there are virtually no limits on our borrowing, and no agreed-upon fiscal goal. If there were one, such as balancing the budget by a date certain, or getting the debt to a specific level in a certain amount of time, policymakers would be required to show their preferred paths for doing so, and we could discuss the various trade-offs of different approaches. That is a core principle of what budgeting is supposed to be. Right now, we have a free-for-all with lawmakers often invoking fiscal discipline only as a means of stopping the other party's priorities, but not

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[9] CBO, *The 2014 Long-Term Budget Outlook*, July 2014, p. 15.
[10] CRFB, "Fiscal Turnarounds," February 2010, http://crfb.org/sites/default/files/Fiscal_Turnarounds.pdf

applying the same discipline to their own. A unified fiscal metric is a very important step in responsible budgeting, and one we strongly encourage lawmakers to adopt.

All of the advantages of a balanced budget do not mean we need to balance our budget immediately. Not only does the political system not seem able to agree on such a large plan, the economy is still recovering from a devastating crisis. The timing of consolidation is therefore extremely important. This is the reason so many bipartisan deficit reduction plans phased in their savings slowly, and often deferred them until the economy was expected to be on more solid ground. This was true of the Simpson-Bowles Fiscal Commission, which included a specific principle not to "disrupt the fragile economic recovery."[11]

At this time, it is most important we focus on getting the longer-term situation under control. Thus the smartest policies we could implement would be those where the savings grow gradually and compound over time, and are conducive to economic growth.

In addition to timing deficit reduction to the business cycle, it is important to recognize balancing the budget can take time. Rising interest rates on a significant new stock of debt, the retirement of the baby boom population, and political promises made to limit changes on the over 65 population, all make achieving a near-term balanced budget more difficult. Most plans phase in changes gradually and with at least some amount of grandfathering. As a result, the House budget resolution last year didn't achieve balance until 2024, and the Simpson-Bowles plan didn't do so until 2035. But they do reach balance. And importantly, in the interim years, the plans keep deficits low and slowly introduce ways to reduce them.

### Avoid Stepping Backwards by Adding to the Debt

I'm encouraged the Budget Committee is holding a hearing on the merits of reducing deficits and balancing the budget. One concern of ours – based on experience - is that Congress and the President will instead act to *increase* deficits over the next year, particularly when faced with the multitude of upcoming "Fiscal Speed Bumps".

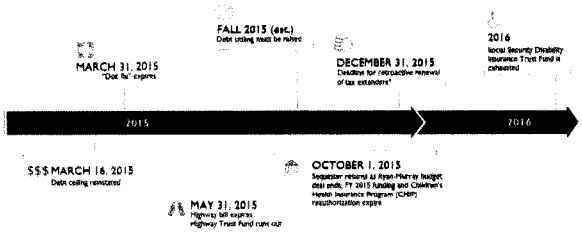
Last year, as an example, lawmakers deficit-financed new funding for veterans health care, fighting Ebola and ISIS, and a package of "tax extenders," while relying on budget gimmicks (fake savings) to help pay for shoring up the highway system and passing a "doc fix," and also sneaking significant new spending into the end of year "CROmnibus" bill. In total, these changes added more than $100 billion to the debt through 2024, which translates to over $1,100 per household. Many of these were important priorities that

[11] "The Moment of Truth," The National Commission on Fiscal Responsibility and Reform," p. 13.

made sense as policies, but given that they were important enough to do, **they should have been paid for**.

Over the next year, Congress will again face a number of "Fiscal Speed Bumps" which could prompt further borrowing. Among those with the most potential to lead policymakers to add to the debt are the expiration of the "doc fix" and the return of the SGR at the end of March, the expiration of the highway bill at the end of May, the return of sequestration on October first, and the desire to retroactively renew expired tax extenders before the end of the year. The Social Security Disability Trust Fund will also become exhausted sometime in late 2016.

## Impending "Fiscal Speed Bumps"
2015 - 2016




*The tax extenders officially expired at the end of 2014, but can be restored retroactively until this point.

These Fiscal Speed Bumps represent challenges and risks, but also opportunities. Addressed responsibly, they offer policymakers the opportunity to at least stabilize the national debt at its current levels. Each one of these offers lawmakers the opportunity to swap not-very-sensible policies with more thoughtful, targeted and lasting reforms.

If policymakers act irresponsibly at each of these bumps, on the other hand, they could increase debt levels by over $2 trillion above what current law allows, to 85 percent of GDP by the end of the decade. Acting to offset the costs of these changes with smarter policies will not fix the debt, but will represent steps towards that goal and avoid

backsliding. We encourage you to take meaningful and responsible actions to offset the costs of all of these speedbumps, and we will be providing "mini-plans" for each one of them.

| Speed Bump | One-Year Cost | Ten-Year Cost |
|---|---|---|
| **Sustainable Growth Rate** | $15 billion | $135-$175 billion |
| **Highway Trust Fund** | $20 billion | $170 billion |
| **Sequestration** | $100 billion | $1.01 trillion |
| **Tax Extenders** | $45 billion | $470-$695 billion |
| **Disability Insurance Trust Fund** | $30 billion | $340 billion |
| Total | $210 billion | $2.1–$2.4 trillion |

To be sure, addressing our Fiscal Speed Bumps responsibly won't get us to a balanced budget or even put us on a sustainable debt path. But it can help us make things a little better, and avoid making them much worse. As CBO Director Elmendorf explained to the Budget Conference Committee in 2013, "big steps are better than small steps, but small steps are better than no steps at all. And no steps at all would be better than steps backwards." We couldn't agree more.

Growing debt levels will dramatically impact Americans, who will feel the effects through slower economic growth, lower wages, fewer government investments, and higher interest rates on everything from mortgages to small business loans.

### Conclusion

Controlling America's debt is a key part of a comprehensive economic growth plan. We need to grow our economy, keep our businesses competitive, and invest in workers, innovations and infrastructure. We need to ensure the gains from growth are broadly shared. And we need to control our debt for any of these efforts to be effective.

To truly tackle our fiscal challenges we need to reform our tax code, strengthen our entitlement programs and control and better-target our spending.

Tax reform will require broadening the tax base and ridding it of many of the $1.3 trillion in annual tax expenditures that are largely regressive, ineffective, economically distorting, and tilt the playing field in undesirable ways. A broader base can pay for lower tax rates and a simpler and more competitive code while contributing to deficit reduction, and helping to grow the economy.

We need to fix our important entitlement programs so we can make good on what we promise. For starters, our disability program will run out of reserves next year. It is

stunningly irresponsible that we have done nothing to get ahead of this problem. There are many reasonable reforms that could be enacted today that would actually help SSDI better serve its beneficiaries and taxpayers, providing services to help people with disabilities remain in the workforce. Moreover, we need to do more to prepare for an aging population and growing health care costs, keeping Social Security, Medicare and other important programs strong. And yet, even as the programs' Trustees warn that changes need to be made, we delay year after year.

And we need to think about how we spend more thoughtfully to direct resources to investments, particularly those that will strengthen the country for the next generation. Finding ways to make the budget more focused on the long-term would be beneficial in many ways.

The pay-offs from responsible fiscal policies are immense. I thank the committee for holding this hearing today and would be delighted to work with you on any of these issues.

Thank you.

1900 M Street NW • Suite 850 • Washington, DC 20036 • Phone: 202-596-3597 • Fax: 202-478-0681 • www.crfb.org

Chairman ENZI. Thank you.

Dr. BLYTH.

**STATEMENT OF MARK BLYTH, EASTMAN PROFESSOR OF POLITICAL ECONOMY, WATSON INSTITUTE FOR INTERNATIONAL STUDIES, BROWN UNIVERSITY**

Mr. BLYTH. Good morning, Mr. Chairman, Ranking Member Sanders, and members of the committee. It is a real honor for me to be here as an immigrant to the United States, so I just want to acknowledge that before I begin.

I am going to show some slides. I am kind of a data-driven guy, so if I can have my slides. Can we go to the next slide, please.

You do not really have a spending problem. You have a revenue problem, so I am going to show you why. Next slide.

You have been cutting taxes on top—on basically everyone, but really it is the top end that matters—basically since the 1960s, and if you have a look—next slide, please—what you will see there, the green line is the United States Federal and State tax take as a percentage of GDP. That is the average of all the other rich countries in the world. So, basically, you are massively under-revenuing, if you want to make that into a word. Next slide, please.

That is the United States on the blue line at the bottom. That is everyone you compare yourself to and the OECD average. You are just not raising revenue. Next slide, please.

This is an old story. As you can see, taxes have outpaced—revenues have fallen short of taxes all the way through the 1980s, as well, actually. It was only briefly in the 1990s it was ever any different. And, the reason you see this large, huge build-up in debt and spending is because we bailed the entire global financial system and had a huge recession. So, of course, taxes are going to go down as revenues dry up from an already low baseline and spending is going to go up. Your debts become your deficit. It is all quite normal why that should happen. And, as you can see, they are trending down again to being almost normal. Next slide, please.

In fact, in comparison to the average of all other countries, the United States tax gap is actually smaller than many other countries. So, you are actually even in better shape, comparatively, even though you actually spend very little through the government. Now, next slide, please.

If the U.S. was overspending, it would show up in bond deals, because the people holding all of that debt would freak out and would want more interest payments. Well, here is the funny thing. It has been falling consistently since 2006, right through the financial crisis. You create a giant tsunami of a financial crisis and people want to hold your debt. In fact, interest payments keep going down in terms of bond yields. If you have a problem in spending, it is simply not showing up in the way that investors' appetite shows up in bonds. The 30-year bond, it is rated 2.8 percent. That does not even cover inflation over the period. No one can get enough of this debt. This is an entirely different story. Next slide, please.

You cannot really see this, but, basically, what it shows is a regression between the degree of budget tightening, what you want to do, on the horizontal axis, and then what happens to your debt, and that dot at the top is Greece and the ones in the middle are

Spain and Ireland and Portugal. And, guess what. The more that they tightened, the more debt they got, because the underlying GDP got smaller and the same constant stock of debt got bigger rather than smaller. So, the more you tighten, the more you shrink your economy, the more debt you end up with. It is quite a paradox, but it is a very robust finding. Next slide, please.

This is the same thing seen the other way. This is basically the wonders of austerity, part two. The stronger the budget tightening, the sharper the decline in GDP. Again, that is Greece at the bottom. They have cut more than any country in modern history and they have lost a third of their economy and their debt has doubled despite the cuts, in fact, because of them. Next slide, please.

This is hardly a surprise, because when you spend all that time shrinking your economy by obsessively balancing your budget, you build fragilities into the system going forward such that when you get hit with an external shock, your economy craters because it is much more fragile. And, what we have here are years in which the budget was paid down, very long periods, and they are all followed by recessions or depressions the minute you get hit with a shock, because you have been artificially constricting your GDP growth for no good reason. Next slide, please.

We wonder a lot about—we have heard a bit about interest payments on the debt. One of the other things I find fascinating is this idea that we are all in hock to foreigners, right, so, you know, foreigners own our debt. If you look at this slide, you will find that most, in fact, 70 percent of U.S. debt is domestically held, and that matters for your interest payment story, because although I pay taxes which become payments on the debt, pension funds and banks use debt very productively. And when you pay them interest, that goes back into my pension. We are all borrowers and lenders at the same time. The notion that debt interest is some deadweight loss is just simply not true. Next slide, please.

So, we have a lot of debt, and you can see here two lines. The blue line is the United States and the other one is the European Union, Eurozone countries, and you can see the effects of the crisis going on. Basically, government spending is pretty constant going all the way across the decade. There is no orgy of spending. It simply did not happen. Then there is a huge blow-up with the global financial crisis. You bail out the banks, and at the same time without recapitalization and so on, you end up constricting the economy. You have a big recession and that is where your debt came from. Europe has been tightening. Remember that they have been doing the budget cuts that you want so much. They are in exactly the same position. Last slide, please.

However, the story is much worse, because if you look at this another way, there is your spend going on. There is GDP growth. There is the effect of the financial crisis going down. Look at the blue line. That is America. We did not cut. We grew five times as fast as Europe did last year. Look at what happened to Europe. The more they cut, that dotted line going down at the end, that is 20 percent unemployed in the periphery and 12 percent unemployed in the core. They are in a miserable state because they have been balancing their budget.

One last thing I want to end on. You do not have a budget crisis now. You did not have it in the past. But you project it into the future. Everything I have heard is ten-year projections in the future. These straight-line one-year projections ten years out. One thing you can bet on: Knowing your projection ever comes true. Imagine you did a ten-year lineal projection in 2004. Do you think you would have picked up the financial crisis? Imagine the CBO did a ten-year projection in 1987. Do you think they would have picked up the cost savings of the end of the Cold War?

Worlds are non-linear generators. You have no idea what it will be like in ten years' time. But, one thing we do know is the American economy will be much better than it is now. In 2006, it was $13 trillion, $13.6. Today, it is $17 trillion. When we go out ten years, we will have a much bigger economy on which we will be paying back a smaller share of debt. If you start cutting now, you will end up in worse fiscal shape than you actually would if you just stayed on the course you are on now. Growth cures debt. Cuts cause debt.

Thank you.

[The prepared statement of Mr. Blyth follows:]

Statement of Mark Blyth
Eastman Professor of Political Economy
The Watson Institute for International Studies and Brown University
Before the Committee on the Budget
United States Senate
Hearing on "The Benefits of a Balanced Budget"
March 11th 2015

Good Morning Chairman Enzi, Ranking Member Sanders, and Members of the Committee

My name is Mark Blyth and I am the Eastman Professor of Political Economy at the Watson Institute for International Studies and Brown University in Providence RI. I am also the author of a book entitled *Austerity: The History of a Dangerous Idea* (Oxford University Press 2013) a book, which oddly just received a national award in Germany, the country most associated with budgetary austerity. Given that irony is not a German national trait, it might be the case that even the Germans are re-thinking their stance on balanced budgets. As I shall show you today, it's really not working out so well in Europe and it would be a disaster if it were tried here too.

And yet balancing the budget as a matter of principle is intuitive. After all, you can't spend more than you earn. It is also appealing. After all, people want more money in their pockets rather than less, so spending 'other people's money' now so that they would have less in the future because of debt interest repayments seems to be the height of folly. But balancing the budget because of these arguments is also folly. While they are intuitive, these arguments are systematically wrong, because they are based upon two faulty analogies: one drawn between households firms and states and another between savings always being good and spending always being bad. I begin by taking each in turn before giving more specific examples.

The flaw in the first analogy is that the national or federal government's budget is nothing but the sum of the budgets of the households and firms that comprise it. This is wrong, and for the United States of America in particular, it is absurd.

First, national governments do not have income in the same way individuals have income. Rather, individuals only have income by virtue of the existence of the government. Think of earning a buck in a job. What makes that possible is not just the labor contract, but also the existence of property rights, courts, police, roads, airports, education, and a host of other state provided functions. Don't believe me? Go look at Somalia's rate of job growth. With no state to protect both parties to the transaction, it's hard to make a buck.

Second, states' incomes are not like private incomes. No one 'pays' the state an allowance that it spends. States cannot 'live beyond their means' precisely because they set those means. If those means fall short, then there are deficits. Given this, it's pretty easy to understand why there are deficits. The US has been cutting taxes at a federal level, especially on high earners, since 1979 (slide 1). Given this, the US federal state taxes in real terms at

about 17 percent of GDP and spends about 21 percent. That's a revenue-generated deficit. It's not a spending problem because in comparison to all the other rich countries in the world, the US spends much less through the government (see slide 2), and apart from the deficit rising because of the financial crisis, federal spending has hovered around 20 percent of GDP since 1980 (slide 3). So if there is a spending crisis, it's on the revenue side. We have cut too much tax, especially on the top end of the income distribution.

Third, unlike households, the United States issues its own cash, owes itself money, borrows other people's savings with its own paper, and brings new people into the household so that it can tax them across the next several generations. National governments can do all that, families and firms cannot and US states cannot. And no one can do that better than the United States national government since its debt is backed up by the world's most dynamic economy, 14 aircraft carriers, and positive intergenerational capacity to tax. Let me unpack this.

During the 2008 financial crisis, despite the crisis developing in the United States, the only asset investors around the world wanted to hold was US dollars and US dollar debt. The yields on the US ten year T-Bill FELL at the height of the crisis. (See slide 4) If there was any investor concern about the stability of the US those yields should have gone up. They went down despite the crisis and the federal debt going up as a result of bailing out the financial sector and the ensuing recession. The whole world, it seemed, wanted dollars and dollar debt despite the US generating the crisis. Why was this?

Simply because, and quite unlike on the state level, because it controls its own money, the US federal government was able to quickly bail its banks and triage the economy via quantitative easing. In countries that could not do this, those in the Euro area for example, they were forced to try and balance their budgets. The result in Europe has been plain to see - a massive contraction in economic activity, with those that cut the most seeing the steepest collapse in growth and, paradoxically, the biggest buildup in debts. This is hardly a surprise historically since pretty much all attempts to balance budgets have resulted in recessions or depressions (see slide 5).

Indeed, the family-state analogy is not just wrong, it is harmful since it makes us forget that the money that the state borrows is not money from some outside agency that will come and shut us down if we fail to make payments - like 'The Iron Bank of Bravos' in 'Game of Thrones' - its money that we owe ourselves.

The government's debt is the asset of the private sector. It is simply a set of credit claims of one part of society on another, intermediated by the government so that we can collectively make investments in our future. So when you say you want less government debt, what you are really saying is that you want less private sector assets, since we are often both borrowers and lenders at the same time.

For example, if you have a private pension you have government debt in you portfolio. It's a safe, and in the case of the US, guaranteed return. It anchors, as a hedge, the other assets in that portfolio that make you more money. You may pay taxes and some part of that may go to

pay debt interest, but that debt interest is paid to your pension fund and so adds cash to your pension.

Indeed, US debt, particularly the ten-year bond, plays a critical role in our economy that is seldom recognized. It is what regulators call a 'zero risk weighted' asset. So when banks buy them and put them on their books this forms the base-asset of their funding and lending pyramid. It is the asset that banks use as collateral to borrow money from other banks and nonbanks to fund themselves. Reduce the supply of ten year T-Bills by paying back 'all that debt' and banks' funding costs, and quite quickly the rates ordinary Americans' pay on their mortgages and car loans, will rise precipitously. Indeed, as our society ages and investors increasingly move from equity to fixed income investments, what would happen to their returns if we reduced the supply of fixed income investments, the first line of which is US debt? They would pay more for less, and have lower retirement incomes. I'd like to see a politician taking the blame for that one.

Similarly, the notion that we are all 'in hock to foreigners' paying them interest is also mistaken. As slide 6 shows, not only is around 70 percent of US debt domestically held (doing quite productive things as per above), its good that foreigners hold our debt.

China, for example, owns $1.24 trillion of our debt, which is not nearly as bad as one thinks. Because for the past twenty years we have been selling them bits of paper yielding two percent interest and they have been giving us super-cheap everything else (from TV's to Computers to Toys) in exchange. As a result our real consumption increased despite a slump in wage growth and the off-shoring of manufacturing jobs while we intermediated their savings. That meant our lending rates went down so we could enjoy lower rates on mortgages and other products.

Even better, China is an export dependent economy and will be for at least the next ten years. So until such a time as they clean up their own banking sector, which is in far worse shape than the US, they will continue to accumulate our debt without being able to liquidate it, for if they did (and what else are they going to hold – the Euro?) it would hurt us but it would destroy their exports and hence their economy. The damage would be completely asymmetric. The fact that we pay them interest is a small price to pay because, guess what they do with the interest? That's right, they buy more of our debt, driving the price down once again. This is trade of the century. We should worry when it ends, not that it exists.

And as for the sustainability of all this debt, only three things matter. The first is the rate of growth in the stock of debt, the second is the rate of growth in GDP, and the third is rate of growth in population. On all three measures the US fares better than almost anyone else in the developed world.

Our demographics are positive and this is important because what matters for government debt in a fiat money system is the intergenerational capacity to tax. Promises made now will be redeemed by a claim on a bigger population and a bigger economy. If you economy is growing (and the US is leading the pack) and your population if growing (we do OK there), then your stock of debt as a share of your GDP declines while your ability to service that debt increases. If you are Japan or Italy, with low growth, high debt, bad demographics and an

inability to get immigration right, then you do have a long run fiscal problem. But the US, which issues the global reserve asset (the dollar) that every other country wants to hold and indeed has to earn in order to conduct foreign trade, has all three things heading in the right way.

In short, the day the US is insolvent is the day that every other sovereign alternative on earth has already gone up in flames. The notion that we have a fiscal crisis that can only be alleviated by balancing the budget is not just wrong. It's harmful.

Turning now to savings and spending, it's interesting to compare the way different countries speak about debt and savings and the like. For the Germans, debt is 'Schuld' – which means 'guilt.' Little wonder perhaps that they insist on the Greeks paying theirs' back when the Germans were among the prime defaulters and debt-forgiveness beneficiaries of the 20th Century. For the English speaking world, 'credit' comes from the Italian "Credere' – to believe – as in the Catholic statement of faith – the "Credo." So we have belief on the one hand when it comes to debt, but can feel guilty about it too. We also inherit a bit of the German attitude to savings "Sparen" – which appears in the English "sparingly." The net result is a bias in our language where debt and spending is bad and savings are good. But if debt is simply a credit claim of one part of society on another, and it all sums to zero – assets must equal liabilities after all – and if my income comes from your debt – and debt, crucially, allows long term investments, this bias does astonishing harm.

Government debt is productive insofar as it funds activities that the private sector cannot fund given their respective time horizons. Many firms have tried to make money out of roads. Most have failed and ended up being bailed-out, for example. But more importantly, if debt is guilt, it can be a very productive guilt. Consider US investment in basic Research and Development (R and D).

Around 40 percent of the basic R and D that makes the pharmaceutical and biotech industries comes from National Institutes of Health funding. Similarly, take out the I-Phone in your pocket. The critical technologies that made this amazing product possible are the TCP/IP internet protocol (DARPA), the GPS network (US Navy) and the touch-screen interface (US Air Force). That Apple put it all in a shiny box and became the best company ever is true. But without those investments, made possible by long-term patient debt, there would be no I-Phone. Indeed, if you want to see how important federal R and D funded by debt is, try playing the stock market over the next decade with this observation.

In the 1960s the US government funded microelectronics. In the 1980s we had the microchip revolution. In the 1970s we began to fund computers. In the 1990s we had the tech stock boom. The federal government can't take the blame for the mortgage boom, no matter how hard we try to blame Fannie and Freddie - lots of countries had mortgage busts with neither a Fannie nor a Freddie anywhere near them – but we did start to seriously fund biotech in the late 1990s. No prizes for guessing where the next industrial revolution comes from? But if that is the case, what would happen if our technological edge withered, which is exactly what would happen if funding is cut due to our 'guilt' overriding our 'belief' in our future as a country and our resulting confusions over debt? Debt is investment, even public debt, it is not a deadweight loss, and without it we would never have the industries that we have today.

A similar confusion pervades the discussion on productive and unproductive – wasteful – government spending. No doubt there is waste. But the private sector has waste too. It's just that they get to write it off against taxes. But both sectors generate income and the money spent in a local business makes no distinction about who spends it or which sector it came from. Allow me to update a story once told, I believe, by the economist Robert Solow, to make this point clearer.

Imagine the world's worst author. Truly, he is a literary disaster. Despite his epic will to publish that novel, it will never happen. But he keeps going, living in poverty and dying in obscurity. But he bought a series of Apple computers to help him on his epic journey, and all that added to GDP, so that's good.

Now consider a government employee whose income is generated by taxes, taxes that also bought the Apple Computer that she uses to process an NIH grant that goes to a researcher at a state university. That researcher, funded by the federal government, goes on to invent a molecule that the pharmaceutical industry buys and turns into a major new therapy. Yet we tend to see this as 'unproductive spending.' Yet what is the difference between the two, especially when that same federal worker goes to the supermarket and shops with her government paycheck at the end of the week, and spends more than our heroic author? Does that not add to the economy either? Somehow we seem to think not.

There is so much confusion, politically sown, about what debt is, what it does, and what it costs. They tend to cluster around three themes:

1) *We have a fiscal crisis in this country - our debt and deficits are unsustainable.*

I think I have shown why this is nonsense already, but one further point is worth making. To know that this is the case you would have to know what the economy looks like 20 years from now. Indeed, the CBO makes such projections at the request of Congress, with the document, "Budgetary and Economic Outcomes Under Paths for Federal Revenues and Noninterest Spending Specified by Chairman Ryan, April 2014," being a particular example of this genre.

It's rubbish. Not because the good people in the CBO don't know what they are doing, but because you (Congress) have given them an impossible task. You are asking them to estimate the budget of the US and its debt levels out to 2040. Exercises such as this are worse than useless, they are harmful because the give a false sense of certainty where none should exist.

Imagine that the CBO was asked to do the same projections in 1989 for 2009. What would it have looked like? Well, even if it had got the end of the cold war right and cost-accounted it correctly (doubtful) it would have missed the budgetary effect of, for example, the late 1980s recession, the tech stock boom and bust, 9-11, the invasion of Iraq and consequent long run costs to the budget, the oil price drop of the 1990s, the oil price rise of the 2000s, the oil price drop of the 2010's, the global financial crisis, and the Red Sox winning two World Series.

There is simply no way this could be known in advance and all these things (apart from the Red Sox winning) have massive budgetary effects. As such, projecting out these smooth linear trend lines is negative information. We don't know what the future holds but we do know that whatever it will hold it will not be that projection. So to base policy on that projection is to politically create the future today before it comes to pass. I believe in other areas of life we call this 'bait and switch.' My favorite example of this was when the federal government unexpectedly balanced its budget in 1999 and then (and now) Whitehouse economic advisory Gene Sperling predicted, "surpluses as far as the eye can see." George Bush based his tax cuts upon that trend being true. They lasted two years.

2) *Entitlements are the problem and they need to be cut.*

I am no expert on this and defer to those that are. And I am the first person to say that any society that spends 17 percent of its GDP on healthcare has serious problems with the issue of mortality. But more seriously, but this also strikes me as economic nonsense.

First of all, if by entitlements we mean social security, it's not a part of the budget. The reason that it appears in budget projections is that the CBO assumes when the current fund gets into trouble in about 20 years, the government will put it on the budget. But there is no reason to assume that. First, it's a pay as you go system. It's not a part of the budget so it can't be a part of the deficit. Like the general budget, there is a revenue problem with social security, not a spending problem, looming very far off. The payroll tax that funds it is currently capped at $118,500. Why do that if it's a universal program? Simply lift the payroll cap completely and around 80 percent of the problem disappears.

Second, if by entitlements we mean Medicare then I lack the expertise to comment. But it is odd that when we talk about entitlements we do not talk about how US corporations, as legal persons, can legitimately transfer price their products, domicile for tax purposes in Ireland and incorporate in a subsidiary in Holland that lowers their taxes further. In 2010 I paid more taxes than Bank of America, and they had already received a bailout. If we are going to talk entitlements, then surely we should have that on the table?

3) *Interest on the debt is going to swallow every tax dollar we bring in, leaving nothing for any other program*

Again, apart from this being based upon completely unbelievable linear projections of the future, there is no evidence to support this belief. If it were even remotely likely then we should see it in our forward rates. Yet today as I write this March 9th 2014, the US 30 Bond yield sits a 2.8 percent. When you consider that this price is the market making a 30-year bet on the future, a yield of 2.8 percent doesn't even factor in inflation over that period. If the above statement is true then global financial markets seem completely unaware of it.

4) *Finally, there is a whole bunch of homespun homilies and metaphors that talk about the risk to future generations of racking up debt today. Some typical examples are:*

**It is irresponsible and immoral to kick the can down the road.**
**We cannot saddle our grandchildren with a crushing burden of debt.**
**We need a budget that is painful to all (today) in order to protect future generations.**
**Future generations are going to have an inferior standard of living because of our fiscally irresponsible behavior.**

I think it should be clear from what I have already said already that this is dubious at best. What we have is a funding crisis, not a spending crisis. The problem is too low revenues, not too high spending. The US has plenty of spare tax capacity, especially at the top. But this set of platitudes I find to be deeply offensive because I am the product of the very thing you want to cut. In fairness, as an emigrant I was raised on someone else's tax dollar (the UK's) but there as many US born citizens now paying taxes in the UK, so the point that I am about to make stands.

I was born in 1967 in a working class family on the East Coast of Scotland. My mother died when I was three weeks old and I was given up to my paternal grandmother for my care. Our income was her state retirement pension (an entitlement). I went to school (paid by taxes) and ate free meals at school (an entitlement). I went to university for free (an entitlement) and now I am a professor at an Ivy League school. As such, I will pay more in taxes over my lifetime to the US government at a much higher rate, and for longer, than I would have ever done if these entitlements had not been there. They made me what I am today and I am a fiscal net positive long asset.

So when people say "we cannot saddle our grandchildren with a crushing burden of debt," or that "we need a budget that is painful to all (today) in order to protect future generations," they are really saying "lets shrink the economy today so that the parents of today earn less money and pay more for services. That will make sure that their grandchildren grow up poorer, with a smaller economy, and a worse education." Quite how that is supposed to keep America great going forward is a mystery to me (unless it's the magic of tax cuts themselves, but they keep failing to show up too).

Far from "Future generations [having] an inferior standard of living because of our fiscally irresponsible behavior," cutting now and deeply so will produce the very outcomes that have brought Europe to the precipice. Indeed, we have been running a giant natural experiment across the world for the past several years on balanced budgets and the results are in.

The US hardly cut (apart from the sequester) and as a result it has grown and now leads the pack. Europe cut deeply and apart from Germany (which lives off other countries spending via exports) has seen their GDP shrink and their debts explode since they started cutting. The cuts lowered GDP and worsened the debt profile of the countries and the cut the most. We have all the evidence we need to make a judgment on this, so why do we keep cutting?

My explanation is that what finance types would call a 'class specific put option' has been executed on the American public, and they folks that cashed-in this contract are a bit nervous about being found out.

A put option is a contract where the seller of the contract gets a fee for offering protection against a default and the buyer gets protection. In 2007/8 the US financial system, which basically looks after the assets and incomes of (primarily) the top 30 percent of the US income distribution, went bust. It called in the option the public that had unknowingly written as taxpayers bailed out 'too big to fail' institutions. But given that the banks' assets are the investors' liabilities and vice versa, when you bail the banks you bail out the assets of the richest part of society. The result of this balance sheet transfer is the generation of massive amounts of public debt as private debt is taken onto the federal government's balance sheet via bailouts, recapitalizations, and most of all, because of the recession this bust produces. Having produced all this debt via asset bailouts and bank-induced recession, the top part of the income distribution then screams loudly about the terrible debts incurred by overspending (even if it was to save their own assets) and demand cuts to programs that they don't consume. This is why it's a class specific put option. As the old adage has it, 'a boom is when the rich get richer and a recession is when the poor get poorer.'

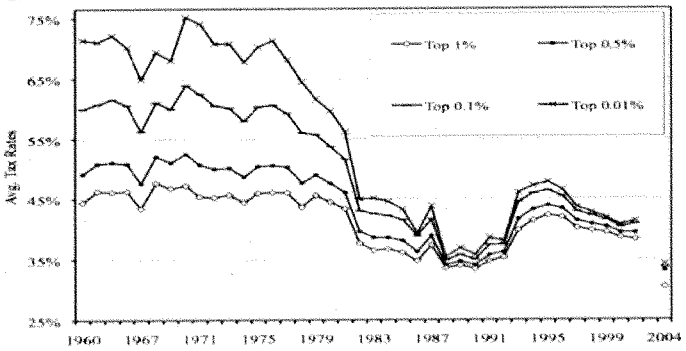
It is also of little surprise to me to find out that billionaire philanthropists and the richest CEO's in the world fund the main institutions fostering this concern, such as the Business Roundtable and the Petersen Foundation. After all, these are smart people and they know that having made off with 90 percent of the gains of the past 20 years, and then having had their assets bailed out on top of that, they are a bit worried that the public might just come after them for some of the share of the costs.

To make sure that never happens we must make sure that we all believe that China owns the US (it doesn't) that Social Security is bust (it isn't) and that the only way to grow the economy is to shrink it now (which, if it were true, would mean that if we shut down the economy from January to June every year and then opened it up again in July, the resulting boom would make the economy bigger than it would have been had it been open all year). Yes, it really is that absurd.

At the end of the day I came to the United States because it is the greatest country in the world. I sincerely believe that. My wife, who comes from East Berlin, knows that better than most. But what made the US great was that it didn't give a hoot about debt when it came to fighting fascism and communism. It invested public money in the technologies of the future 25 years out and reaped the benefits. It gave everyone a chance to be an ivy-league professor. And now we seem to want to stop all that for the sake of a false analogy between a household and a superpower's budget. Surely we are better than that? Surely one day I can dream of taking an Amtrak from Boston to New York at a speed greater than 45 miles per hour? Surely one day I will land in JFK and not think that I am in the third world? To do that, we need to stop taking nonsense about debt and start talking sense about investment. They are two sides of the same coin. Not choice we need to make between the two.

Slide One:

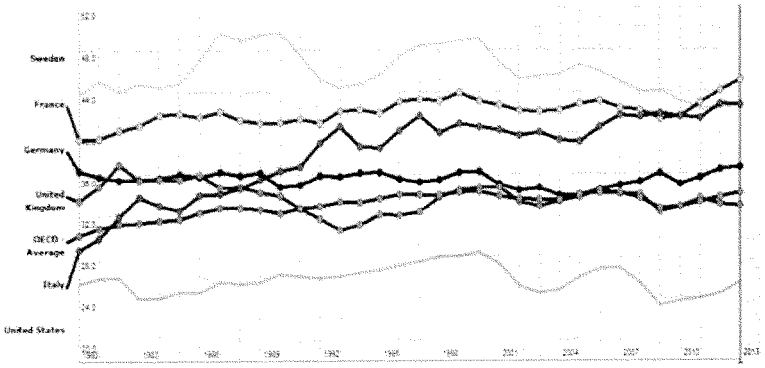
US: Average tax rates for top income groups (from Hacker and Pierson 2010)



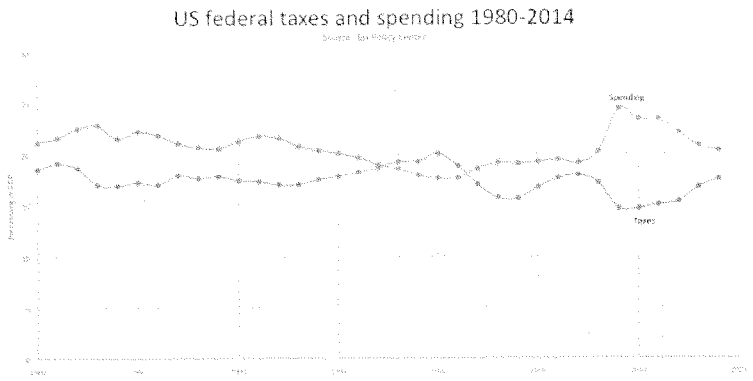

Slide Two:

Source: stats.oecd.org

**Total, Total tax revenue, Tax revenue as % of GDP**

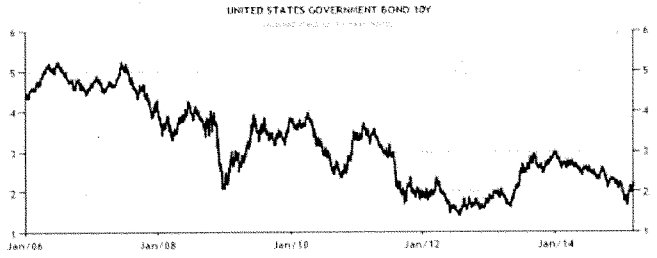


Slide Three:




Slide Four:

If the US was overspending it would show up in Bond Yields – it hasn't.



Slide Five:

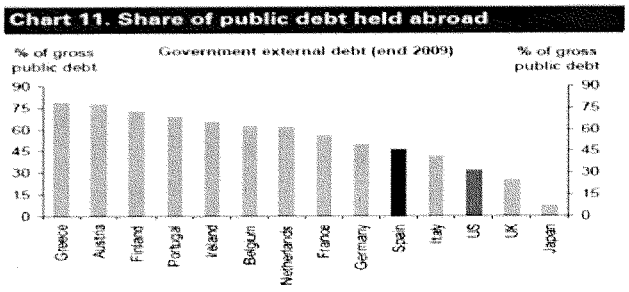
# The Global Lessons of Budget Balancing

## Lessons from History

| Years Budget Was in (e) and Debt Was Paid Down | Outcome |
|---|---|
| 1817-1821 | Depression began in 1819 |
| 1823-1836 | Depression began 1837 |
| 1852-1857 | Depression began 1857 |
| 1867-1873 | Depression began 1873 |
| 1886-1893 | Depression began 1893 |
| 1920-1930 | Great Depression 1929 |
| 1998-2001 | Recession in 2001 followed by Great Recession |

Slide Six:

## The Myth of Foreign Ownership of US Debt




*Source: OECD, Haver Analytics, DB Global Markets Research*

Chairman ENZI. Thank you.

Now, we will turn to questions. As a reminder, I will alternate recognition between the Republican and the Democratic Senators, following seniority for those who were here when the hearing gavel sounded. After that, I will recognize members based on their order of arrival. If you are not here when your name is called, I will skip you, but pencil you in at the end of the question list. Actually, I do not have to pencil you in. We have this nifty little computer here now that somebody is keeping track of all these changes for me so we will all have a chance to ask questions.

Some good presentations by all three. It will be interesting to see what Europe does now when they have the Euro where they do not have the control of their money supply, and with Greece where they are about to reverse all of their austerity. That is what their new election did.

But, I will begin with Governor Engler. You ran the State of Michigan for 12 years under the constitutional requirement that your annual budget be balanced, yet you made significant investments in education, conducted a successful economic growth plan, and you reduced income taxes numerous times. You have also successfully run large nonprofits. I have been arguing that a balanced budget requirement sharpens the priority setting process. You obviously had your priorities. Am I right in thinking that the process of writing a budget becomes more focused on priorities and what not to fund under a balanced budget requirement? Can you tell me how you did prioritization and wound up with an improvement?

Mr. ENGLER. Well, thank you, Mr. Chairman. The question of priority setting is one that is never done by a Governor alone. It is a collaborative process. In Michigan at the time, we had divided government, so we ended up having to have a consensus among legislators in both parties. In fact, one of the changes we made in the early days of the 1990s, we eliminated general assistance, which was cash assistance for single able-bodied adults without children. We had Democratic votes to do that.

We prioritized things like education, what we thought was an investment agenda. And, we tried to reduce those programs that we thought were less essential. It was not as though—we were not reducing key investments. Some went up and some went down. I mean, sort of in contrast to the sequestration process that has been used here, which is kind of a blunt tool that goes the good gets cut with bad, you try to eliminate the bad and double-down on the good is what a strategy is.

I would say that if we look across the States, because we all, for the most part as Governors, have balanced budget requirements, we do not have latitude. So, we just have to set priorities. In the case of Michigan, it actually took two years, really, to get the whole deficit gone. We could not even get it done in the first year. But, we knew that raising taxes, given the unemployment numbers in Michigan at the time, was a poor strategy, and so we averted that path and stayed on one that ultimately led to an unemployment rate that got under four percent.

Chairman ENZI. Thank you.

Ms. MacGuineas, you have served on so many budget commissions and work groups that you have provided some suggestions,

but I know you have more. Adopting a joint budget resolution might be a big step forward. We have not done that in six years. Beyond that important goal, however, what would be the two or three most important reforms to the budget process that we can assure would provide a better debate over priorities and an informed budget?

Ms. MACGUINEAS. Good. So, given where we are right now, I think one of the most important things we can do is adopting a fiscal metric. And, so, if we have a goal that is agreed upon, whether it is balancing the budget or getting the debt to a certain level of the economy by a certain amount of time. That then forces the budget process to confront trade-offs.

So, right now, fiscal responsibility is usually used as people trying to stop the other side from doing what they want to do. But, instead, if we agreed we need to get the debt to whatever goal it is, we then would put forth a variety of plans of how to get there and you look at the different kinds of trade-offs. How much comes from revenues? How much comes from spending? What is that spending like? How do we make up a budget plan? And that is the process that budgeting should confront.

Second, I do think we need to look at lot more at the long term. Right now, our budget process is overly focused on the short term when we know that the problems that are really generating our concerns deal with demographics, the aging of society, and health care, and, again, those growing interest payments. So, when you look out in the long term, even though we cannot project sort of when the business cycle will hit, demographics is destiny, as they say, and so we know that that is going to have a significant effect.

Finally, I think there is two-thirds of the budget, mandatory spending, that really is not budgeted for, and I think finding more ways to have oversight and thinking about how much you want to spend on various areas and which priorities we want to spend on will, again, go back to confronting trade-offs within the budget.

Chairman ENZI. Thank you. Fiscal metric, long-term planning, and looking at the two-thirds that is mandatory. I appreciate that.

And Governor Engler mentioned increasing the economy. It was interesting that the OMB said that if we increased the economy by one percent, that that would increase revenues by $4 trillion over ten years.

You also mentioned in your testimony $100 billion in gimmicks. We will see if we cannot reach a more honest budget.

My time has expired. I will have some questions in writing for all of you and hope you will respond. Obviously, Dr. Blyth, your questions will have a lot more to do with specific numbers, and I appreciate the presentation that you made and look forward to your answers.

Senator Sanders, followed by Senator Sessions.

Senator SANDERS. Thank you, Mr. Chairman, and let me thank all of the panelists for their excellent testimony.

Governor Engler, I want to ask you a question, and I do not want to—please trust me and understand that it is not a personal question. I have a hard time hearing a representative of an organization of the largest corporations in America, where the CEOs of these corporations will retire with about $88,000 a month, over a

million dollars a year, in retirement benefits, which is the case, coming before the Congress to recommend that we cut Social Security benefits for people who are trying to survive on $12,000, $13,000, $14,000 a year. My point here is not to argue the issue. I mean, different people have different views on Social Security. But, I just want to say, I have a problem with some of the wealthiest people in this country, who have more money than people can dream of, coming here and lecturing us about how we have to lower Social Security benefits for disabled vets and working people.

My question to you is—and let me go to Ms. MacGuineas, if I could, you used the expression, "strengthening entitlement programs." I will be introducing legislation that will strengthen Social Security. It will make it solvent until the year 2060 by lifting the cap on taxable income, which is now at $118,500. Starting at $250,000, all people would pay the 6.2 percent. That will strengthen Social Security very significantly. Are you supportive of that legislation?

Mr. ENGLER. Well, I will start with that. Who do you want to—

Senator SANDERS. Sure, either one. I was going to start—let me start with Ms. MacGuineas, then we will go to you.

Ms. MACGUINEAS. Yes. I think that that is the kind of thing that we need to do to strengthen Social Security, in that right now, what we have is promises that have been made that we cannot make good on. I think you should go the whole way. I think that—I believe that your bill closes about 80 percent, maybe. I know it gets to 2061, as you said, but again in 2021—at some point, we would have to start confronting that it will be out of balance pretty quickly. So, I would recommend putting a full package that gets to sustainable solvency, which is normally the goal.

And, the only issue—I think that looking at lifting, eliminating the payroll tax cap makes an awful lot of sense. I think there are only so many times we can tax and use that money for different places. So, the one thing I think we want to do is think about, holistically, what the biggest priorities in our country are, and I think Social Security and maintaining a strong safety net, in particular for people who depend on it, clearly is.

I do think you want to make sure those changes are targeted and you do not expand benefits for the well-off at the same time that you are making those changes.

Senator SANDERS. Okay. Governor.

Mr. ENGLER. Yes. I would certainly look at any legislation that is introduced to strengthen the system. That is why we look carefully at President Obama's recommendations to use the correct calculations on cost of living for Social Security. We are disappointed that that did not get any traction in the Congress. So, there are a number of changes.

But, when I talk about strengthening Social Security, I am also wanting to make sure the people who need it most have it there for them. So, I am not interested in protecting Warren Buffett's Social Security. I am interested in the people you talk about.

Senator SANDERS. Well, but I am not talking about Warren Buffett. I am talking—

Mr. ENGLER. Well, you are, because—

Senator SANDERS. No, I am not. I am talking about—

Mr. ENGLER. You are.

Senator SANDERS. All right. Well, we can argue. I am talking about maintaining a universal system, and I am talking about lifting the cap right now, which is at $118,500 a year, so that somebody who makes $10 billion a year contributes the same amount as somebody who makes $118,500, I think that that is pretty wrong.

All right. Let me ask, Governor, again, and then I am going to go to Ms. MacGuineas, as you well know, there are major corporations in this country, including General Electric, PG&E, the American Electric Power, Corning, who have paid zero in taxes in recent years, in fact, have received rebates from the IRS. Let me start with you, Ms. MacGuineas, and then we will go to the Governor. If we are serious about talking about deficit reduction in any way that is fair and not simply on the backs of low-income and working families, should we not end those loopholes?

Ms. MACGUINEAS. I think one of the keys to overall tax reform is broadening the tax base, which means ending many of the corporate loopholes. I would do the same thing on the individual side, as well, and I would try to do it comprehensively. But, yes, I think we have to look at all the tax breaks. Right now, you have corporations that are putting money overseas because they have a crazy tax system that they have to work within. So, we need to rationalize our tax system, allow us to be more competitive, and I believe, as part of a comprehensive debt deal, you are going to have to look at both sides of the budget, look at spending and revenues—

Senator SANDERS. I apologize. Again, my time is short. Let me just go back to you, because I am running out of time. Last question, Mr. Chairman. In, as I recall, 1952, corporations contributed over 30 percent of the revenue coming into the Federal Government. Today, that number, I believe, is around ten percent. Does that concern you, that the collective amount coming into the Federal Government from corporations, in general, have declined precipitously?

Mr. ENGLER. Well, I think corporations, as we recognize, are tax collectors. I mean, corporations collect the taxes from their customers. One of the studies—there are several studies, actually, that show that corporate tax burdens fall most heavily upon workers in America—I can provide those to the committee—about 75 percent of corporate taxes. It is one of the reasons that—that has a negative effect on wages, actually, corporate taxes. But, I—

Senator SANDERS. Is it a logical conclusion, Governor, that we should eliminate corporate taxes?

Mr. ENGLER. I would think that would be a terrific idea.

Senator SANDERS. You think we should have zero corporate taxes in America?

Mr. ENGLER. I think that there are proposals that have been in Congress to reform the tax structure that come up with very impressive ways to look at how we could make the system more progressive. Today's system is, in fact, anything but, and, more importantly, going to the point about job creation and wealth that you talked about earlier, today's system—and we released a report just today showing that in the last decade, 1,300 companies were needlessly acquired by foreign ownership because of the tax structure

that we have here. So, I think job creation and wealth creation says get that stretch much, much better. Ireland—Britain has cut theirs seven points in the last, I think, three years. Ireland is way down.

Senator SANDERS. Am I out of time, I presume?

Chairman ENZI. Yes.

Senator SANDERS. I am. Okay. Thank you.

Chairman ENZI. Senator Sessions, then Senator Stabenow. If she is not here, then it goes to Senator Johnson.

Senator SESSIONS. Thank you, Mr. Chairman. I look forward to us having a budget that passes both houses of Congress that will balance. Social Security is not within our purview, so we will not be able to lay out plans to fix that, but we will lay out a budget under Chairman Enzi's leadership, I think, that will serve the national interest.

I just would say, Dr. Blyth, that experts dealing with how to solve the fiscal debt crisis around the globe have found through careful study that spending reductions are kinder on the economy than tax increases. And, I will quote the studies of Alberto Alesina at Harvard, Valerie Ramey at UCLA, the World Bank, the European Central Bank, and the International Monetary Fund. You just do not—this idea that you can tax the economy and hammer it and it is going to produce more growth is, I do not think, defensible.

I would also note, colleagues, that under President Obama, we have already added $2.3 trillion in taxes over the decade, $1.7 on Obamacare, another $600 billion at the fiscal cliff. And, his budget that he submitted now has got another $2.4 trillion that he wants to add. So, I do not think we are going that way.

Ms. MacGuineas, thank you, and thank you to the Committee for a Responsible Budget. I was just looking at some of the names on your list of Directors: Kent Conrad, our former Chairman here, Paul O'Neill, Leon Panetta, Pete Peterson, Robert Reischauer, Alice Rivlin, former Senator Chuck Robb, Paul Volcker. So, I think you speak in a good way for the objective evaluation of where we are.

I want to say to you, first, I totally agree, and it is very important to emphasize that our debt problems have not been solved. Years ago—several years ago, we knew the deficits would decline to this year, but we also could tell then they were going to start going up again to a dangerous level. They are already at a dangerous level, almost a half-a-trillion dollars each year in debt. So, you have indicated that. Would you just briefly assert with clarity your belief that if we do not do something, that we are on an unsustainable path, as the Congressional Budget Office says, and we place our country at risk. That is a fundamental question Americans need to know.

Ms. MACGUINEAS. I absolutely believe that. I believe the fact that we are projected to have our debt growing faster than our economy is problematic from an economic perspective and it puts us at risk.

Senator SESSIONS. And we know Rogoff Reinhart studies have indicated when debt gets to the level we are at now, you can begin to slow economic growth, and the last thing we need to do is have another action that slows growth.

You also said something that is very important, and I think all of our colleagues need to hear this. You said a fiscal goal is a key part of budgeting. So, we talked with former cabinet members in New Zealand and Canada, the former Prime Minister of Canada. Both of those faced budget crises and balanced their budget. Both have told me personally that you need a clear goal for the people of your country and the goal is a balanced budget. Anything else becomes so fuzzy that you cannot call people to sacrifice to reach the goal. Now, I understood you to say, Ms. MacGuineas, that you think that we should have a goal of balancing the budget.

Ms. MACGUINEAS. Yes. I think that what we have seen in these countries that have done fiscal turnarounds is that having an understandable goal by the public is one of the key factors in success. And, I do think that balancing the budget—over the business cycle, though. I do not think it is important you balance it every year. I think when the economy is slow, you need to be running budget deficits, and when the economy is strong, you need to be saving so that you are able to. I think that is your ultimate goal. And, I think, again, what is really troubling is where we are right now, where it is projected that our debt will grow faster than the economy.

Senator SESSIONS. I understood you to say in your opening statement that balancing the budget will have economic growth benefits, too, over time. Would you share your thoughts on that.

Ms. MACGUINEAS. Yes. So, if you look at—there have been a number of studies by the Congressional Budget Office, for instance, that show putting in place a Simpson-Bowles-like plan would have short-term effects where it slows the economy, and I will talk about that in one second, and then it has longer-term growth effects, where it adds to GDP in perpetuity. That is one of the reasons that Simpson-Bowles and other comprehensive plans always did say, you need to pick when you start to phase those changes in very carefully. You should not phase them in when the economy is slow. You phase them in gradually when the economy is getting stronger.

So, I think there is a big difference between austerity and fiscal responsibility. Fiscal responsibility is putting us back on a sustainable path, and that will have effects on the economy, on jobs, on wages, and that is why fiscal responsibility—it is not a goal in and of itself. It is part of how you have a comprehensive growth plan. I do not believe our economy can be strong and that that strength and that growth can be shared across the economy, which is a really important priority, unless you have a manageable debt situation.

Senator SESSIONS. Mr. Chairman, maybe Governor Engler will give a yes or no to this. You had great success with welfare reform. Do you believe it is time for us to have additional welfare reform, and properly done, could that translate, or move workers from dependency to work and prosperity? Basically, yes or no.

Mr. ENGLER. Yes.

[Laughter.]

Senator SESSIONS. Thank you.

Chairman ENZI. In keeping with the alternating of those who were here at the sound of the gavel, Senator Merkley would be next, then Senator Johnson.

Senator MERKLEY. Thank you very much, Mr. Chairman, and thank you all for your testimony and thoughts.

Governor Engler, I understood you are making the case corporations should not pay any taxes, and in Oregon, we have a road user fee, weight per mile, that affects trucking. Essentially, it is calculated so everyone's impact on the road is reflected in the fee. So, it is a little more sophisticated than a diesel tax. You put an extra axle under a truck, you do less road damage, you pay a lower rate. If you are a smaller truck, you take up less road space, you are using less infrastructure, you pay a lower rate, so on and so forth.

That concept in which infrastructure costs are paid proportionately to the users made a lot of sense to me, and when I hear you say, or as I understood you said when I was out of the room, that corporations should not pay any tax, I think, why should a corporation not help pay for the infrastructure that it uses? Why should that burden all fall to others?

Mr. ENGLER. Well, thank you for asking this question, because what I—I certainly think corporations—they pay lots of taxes. They collect lots of taxes. But, I think all of us as Governors knew that our tax rates had an impact on business investment in our State. That is why Governor Cuomo, to clarify for our Ranking Member, he is advertising all over America, come to New York, no taxes. No taxes on business. Tax holidays. That is no corporate tax. Now, that does not mean they are not paying franchise taxes or other types of taxes, but he is talking about the income tax.

To Senator Merkley's question, I think Oregon is to be commended for their kind of innovative approach in looking at this. I, as a Governor, signed a gas tax increase, which included taxes on diesel fuel, which primarily at the time the trucks bought that. I think we are kind of at the end of the gas tax era. There is maybe one more hike in there, but I think you are looking down the road. It is going go take some—you know, we have got to work out the technology, but—

Senator MERKLEY. So, let me put it this way. If we were looking at the use of infrastructure across the country and the amount of the Federal budget that went into that, would you support a minimum corporate tax that reflected the amount that companies are utilizing that infrastructure?

Mr. ENGLER. Well, you just asked me about fuel taxes or vehicle miles traveled. I mean, those kind of user taxes. There are some who, I think, have tried to conflate the issue of the current tax law of the U.S. is, of course—

Senator MERKLEY. Okay. My time is running out. I gather I am not going to get your support for that strategy, but I just thought it would be an interesting reflection.

Let me turn to the issue of Social Security. My seniors feel that the Consumer Price Index on Social Security should reflect their actual baskets of goods, what seniors buy. Dr. Blyth, do you agree with my seniors in Oregon? Should the CPI in Social Security reflect what seniors are actually facing in terms of inflation?

Mr. BLYTH. The CPI tends to measure what we call core inflation, so it strips out a lot of more volatile items. Unfortunately, your seniors live in a volatile world, and not just your seniors. If we think about this more generally, the cost of health care and the

cost of education goods are growing far faster than the cost of inflation, and when you have stagnant real wages, that creates a real problem.

So, in terms of supporting seniors through making adjustments in the CPI more reasonable—

Senator MERKLEY. Try to give me the crisp version of this.

Mr. BLYTH. Yes.

Senator MERKLEY. Thank you.

And, Ms. MacGuineas.

Ms. MACGUINEAS. My recommendation would be to adopt what the people who do the calculation of inflation say is the best measure, which is the chained CPI, which, I think, would have effects on all parts of the budget—the budget, Social Security, and revenue. I think one of the present—

Senator MERKLEY. Let me ask you this. Are you aware that chained CPI is less accurate in reflecting the costs faced by seniors than the current price index and certainly less accurate than CPIE, which is designed directly to capture the costs faced by seniors?

Ms. MACGUINEAS. Well, what I am aware of is that the CPIE, which is experimental, has been determined by the people who are still putting it together as not being a good, accurate measure yet. So, they are continuing to work on it, and I think they should. It will be interesting, if we start breaking out inflation so that it applies differently for different groups, how that will look throughout the economy. I think we continue to develop it, but right now, chained CPI is the one they say is best.

Senator MERKLEY. Well, "they," whoever "they" is, may say that, but it is really advocating for something that is an accounting trick that is less accurate for our seniors. And, quite frankly, our seniors are onto that type of strategy, one more attack on people of low income, an attack on our seniors, attack on working America, while here I hear a panel that is saying, you know what? Wealthy Americans should not pay the same marginal tax rate that working Americans pay. Why not? Why should wealthy Americans not pay the same amount per every $1,000 they earn that working Americans earn? And, I am out of time, so if the Chair will indulge me and you want to give a crisp response, why should a working person pay a higher marginal tax rate than the rich?

Ms. MACGUINEAS. They should not.

Senator MERKLEY. Thank you.

Mr. BLYTH.

Mr. BLYTH. They should not.

Senator MERKLEY. And Governor Engler.

Mr. ENGLER. The—I thought the President made a reasonable proposal. I am surprised that it is now interpreted as an attack on seniors and poor people.

Senator MERKLEY. Well, that was not the question, actually. The question was, why should low-income or middle-income Americans pay a higher tax rate per $1,000 they earn than the rich?

Mr. ENGLER. Well, I think—I thought our tax code was progressive.

Senator MERKLEY. Well, then, you are deeply misinformed and I encourage you to read up a little on it.

Thank you, Mr. Chair.

Chairman ENZI. Next is Senator Johnson, followed by Senator Whitehouse.

Senator JOHNSON. Thank you, Mr. Chairman.

Ms. MacGuineas, you mentioned Simpson-Bowles. I just wanted, for the record, to make sure everybody understands, we have actually done about 81 percent of Simpson-Bowles. Simpson-Bowles asked for about a trillion dollars in tax increases. In our fiscal cliff deal, we got about $700 billion. They are looking for about $1.9 trillion in discretionary spending reductions. In our Budget Control Act, we got about 2.1. And, then, Simpson-Bowles also had about half-a-trillion dollars of some mandatory spending, which we have not done. So, Simpson-Bowles, before interest, was looking for about $3.4 trillion of deficit reduction. We have done about $2.8 trillion.

Now, it has been a pretty messy process, but lest anybody think that is a panacea—I mean, it certainly has helped in the short term, but we have got a long-term problem which I want to talk about.

I have certainly been trying to point out that we do not have a ten-year budget window problem. We really have a 30-year demographic problem. We have all the Baby Boom generation. We are retiring at the rate of 10,000 per day. We made all these promises and we really do not know how to pay for them.

So, if you look at the—and I see in your testimony, Ms. MacGuineas, you talked about the CBO's alternate fiscal scenario. So, we have actually turned, converted those percentages of GDP, which nobody understands, to dollars. Let me just run it by you.

In the first decade, the deficit is projected, according to CBO's alternate fiscal scenario, to be $8 trillion. The second decade, $31 trillion. The third decade, $88 trillion. I always like to point out that my little baby girl turned 31 and that kind of went by like that. Now, the net private asset base of America is $106 trillion.

So, you talked about—and you related our debt to a family. I would just kind of like to have you relate why the nation, a nation that is in debt over its head, why it is hard to grow their economy when you have this massive debt hanging over their head, massive debt service, and is that not pretty similar to a family that is in debt over its head, spending all of its money on servicing a debt, having the creditors banging on their door? It is kind of hard to grow a personal economy, as well. Can you just kind of speak to that?

Ms. MACGUINEAS. Well, I never want to overdo the comparison between the government and families, because, clearly, they are different. But, there are a number of conclusions that you can draw, and one is that you cannot borrow indefinitely. You cannot borrow beyond your means.

You also cannot borrow to spend on consumption rather than investment and have that turn out well for you. So, when families are borrowing to send a kid to college or for their worker training, that might be a good reason to borrow, whereas borrowing to spend a lot of money on consumption is not. The same for the government. And, if you look at how our government spends money right now, it is the reverse of what I would think it should be if we had a long-term strategy, to your point which you focused on so much

about the long-term, where the vast majority, probably above 80 percent of what we spend is on consumption and very little is on investment.

And, if you look at the difference between what Simpson-Bowles recommended and what happened, the area that fell short was we did not reform any of the entitlement programs. Where the squeeze has been is on the investment, the discretionary portion of our budget, and that squeeze is going to harm our growth and our economy in the long run—in the medium run.

Senator JOHNSON. Dr. Blyth, I heard your testimony talking about we have just got a revenue problem. Does that long-term projected deficit, does that not concern you?

Mr. BLYTH. It does concern me, but it concerns me in a very different way. Global financial markets, as measured by bond rates, have no issue with funding the United States. They simply do not—

Senator JOHNSON. Right.

Mr. BLYTH. —currently. But, you know, a 30-year shot at 2.8 percent is pretty good. The notion that—and the family analogy is at all useful for this, I find very problematic.

For example, three variables really matter about debt sustainability. One is positive demographics, right. Are you Italy or are you the U.S., and the U.S. is positive on this.

Are you growing? Yes, we are the leader of the pack. The IMF is celebrating us. That is kind of awesome. So, your GDP is growing, as well.

And, then the third one that matters is the rate of growth in the debt. Now, you were saying that, basically, we are on an unsustainable track. But, if we are the lead performer, I do not see how that can be. That is the assumptions built into the model, actually, that does that. So, we are actually in a pretty good place to just grow our way into a solvent situation over the long term.

Now, should we restructure the budget? This is legitimate democratic debate. What should we spend on? I am deeply troubled by the fact that the United States spends 17.7 percent of GDP on health care. That is not—it is like we are all trying to live forever. There is something very strange going on. It is twice all the other developed countries. So, we have issues, but we do not have the issues that are related to family budgets.

Senator JOHNSON. Okay. I appreciate that.

Governor Engler, you were talking about, basically, corporate tax reform. Certainly, a number of businesses report their income through individual returns, through Subchapter S-es and LLCs, and those businesses—that business income is actually taxed at those progressive tax rates, which we do have a progressive tax system. The maximum marginal tax rate is approaching 40, in some instance over 40 percent just on a Federal basis. Then tack on property tax and State tax and—

Mr. ENGLER. Sure.

Senator JOHNSON. Okay, and payroll tax. So, has the Business Roundtable at all explored potentially doing the same thing with larger corporations? In other words, rather than make employers and consumers pay the tax—because that is really who pays the

corporate tax. It is not the piece of paper that is the corporate charter—

Mr. ENGLER. Right.

Senator JOHNSON. —it is a self-inflicted wound. We are the chumps. Has the Business Roundtable explored any options of how you make the owners of the large corporations, basically as pass-through entities, and make the owners of the companies pay the corporate tax rather than the piece of paper that is the corporate charter?

Mr. ENGLER. Well, in 1986, Senator, everybody went the other way. They fled from the corporate status and went to that incorporated pass-through status.

We are—we think and we talk in terms of business tax reform. Obviously, we think we could get the corporate rate 25 percent. That would get us to average of the OECD nations. Our effective rates today are, according to a World Bank study that was done, looked at 185 countries, you know, we have the highest effective rate among the G–7 nations. There is a lot of confusion about that. You see a lot of different rates tossed around. But, we have got a very high effective rate. The 25 percent rate would, I think, make us globally competitive, and that is where we ought to be.

You know, I talk about the States. The States are the—the way to understand this, I think, and your question is an excellent one, because you look at how the States compete for jobs and we saw migration from—Michigan sure saw it from the Midwest down to the South. When Indiana went to a Right to Work State, that put pressure on your State. Michigan now moved to a Right to Work State. They are competing because States have to compete.

Well, today, unfortunately, that competition is happening among nations, and almost everybody has got a kind of a national economic strategy to go out and compete except us, and that is fundamentally the difference, and that is why we have not seen GDP growth above nine percent—above three percent in nine years. So, it is growth and that is why I was citing growth as such a contributor to solving these budget problems, and that is how people go to work and that is how they raise incomes.

Senator JOHNSON. Thank you, Governor. Thank you, Mr. Chairman.

Chairman ENZI. Senator Whitehouse, followed by Senator Crapo.

Senator WHITEHOUSE. Thank you, Chairman.

One quick question for Governor Engler. During the time that you were Governor, the national unemployment rate fell to a 30-year low of 3.8 percent. So, would you give President Clinton and his economic policies maybe even a smidgen of credit for—

Mr. ENGLER. Well, I think that President Clinton and Speaker Gingrich and Senator Dole could all take credit as the leaders of the respective chambers. But, I will tell you what I give credit to. That was a period where people worked together. You know, they worked—they got welfare reform done during that period, a Democrat President and a Republican-led House, and—

Senator WHITEHOUSE. Well, let us talk for a minute—

Mr. ENGLER. —we are not seeing that kind of cooperation today. But, I think you have got your finger on something—

Senator WHITEHOUSE. —about working together, then, because I think working together would be a good thing.

Mr. ENGLER. Yes.

Senator WHITEHOUSE. We hear folks right in this committee and out on the floor who talk a really good game on debt and on the deficit. It is like people who talk up a good game on religion, but on Sunday morning, they are not in the church pew. On Sunday morning, they are out playing softball or sitting at the tavern having a cold one and you get a sense of what their real priorities are when you see how things relate to one another. Go to church, go play softball, or go sit and have a cold one.

One of the key priorities here is what are we going to do about the $1.2 trillion that goes out the back door of the tax code through loopholes, through tax favoritism, through benefits for high-income taxpayers that lower-income taxpayers do not share, and when you come to that conversation, all the good words and good work on debt and deficit from our colleagues come to a screeching halt. And, every corporate tax loophole is sacred, and every position in the code that gives a high-income, including an amazingly high-income taxpayer, a benefit compared to regular working folks, they will defend that to the last trench.

So, if we, in fact, are going to work together, is it not just economically necessary to look at the $1.2 trillion in lost revenue that adds to the deficit and that is going out the back door of the tax code? Let me go right across, Blyth, MacGuineas, and, well, you guys are the economists—

Mr. BLYTH. I will save you some time. Yes.

Senator WHITEHOUSE. Okay.

Ms. MACGUINEAS. Absolutely. That is kind of the shadow part of the budget. It is not very good spending. It is not targeted. It is not done well. And, it is the key to tax reform. You need to broaden the base in order to make us more competitive, simplify the tax code, and raise revenues, and you want to reform the tax code. You want to bring rates down and you want to collect more revenues to close the deficit. Those tax breaks are how you are going to do it.

Senator WHITEHOUSE. I would add that, from the political perspective, if you are a lobbyist for a big special interest and you go to the Appropriations Committee to get some special deal for your client, you have got to fight for that every single year, or at least every single year that there is an appropriation. And, so, for the lobbyist, that might be good, because you are constantly employed, but for the special interest, it is not as sure a thing as if you can get something into the tax code for yourself. Then you can walk back and you are good for years.

And, when you see some of the nonsense that gets into the tax code through things like conference reports, where nobody will put a finger on how it put in there, it has no identity, it is the anonymous deal, you know who it benefits but the whole thing was done out of regular order, there is a quality of this just being a very seamy and disreputable side of the legislative business, as well. So, I hope that we can undo some of that and get to a place where we can seriously address the debt and the deficit on both sides of the aisle and assure that this conversation is not just being used as a

stalking horse for benefit cuts and sort of the traditional hobby-horses of one party.

I yield back my time.

Chairman ENZI. Thank you. The first one to finish ahead of time.

Senator Warner, followed by—

Senator WHITEHOUSE. I got good, quick answers, Mr. Chairman. Everybody agreed. It was terrific from the economists.

[Laughter.]

Senator WARNER. Well, thank you, Mr. Chairman, and with apologies to the panel, because I have got a series of points, I would like to make—surprise, surprise—I actually would wager you, Mr. Chairman, that as different the views could be from the three panelists, that they could actually come up with a coherent plan, because these are not problems that are unsolvable—

Mr. ENGLER. Right.

Senator WARNER. And, then, I have got a number of points, in my effort to be equal opportunity offender here, let me try to make a series.

One, as a Governor, as well, Governor Engler, and we worked together on things, we balanced our budget. We got a AAA bond rating. But, we also had to deal with revenues, and the States are very different. They do not have two-thirds of their budget on a mandatory basis. And, while I think the Chairman has had a long record of being responsible in terms of having a balanced approach, I do find that there are a number of members who use the notion of a balanced budget amendment as a fig leaf because they are not willing to propose a real plan that is truly balanced on both sides of the balance sheet, both in terms of how we deal with spending and how we deal with revenue.

And, candidly, for a nation that does need the opportunity to go into debt at appropriate times, I think it is not the appropriate way to go. I think we need to make the hard choices that this committee or groups like Simpson-Bowles and others have tried to make.

I think it is also important, as we talk, we have seen corporate tax levels go down at State. We have seen it go down nationally. But, I do think it is important as we think about this with intellectual honesty, as we point to countries like Ireland and others, it is not like their tax rates are lower. They may have taken the corporate tax rate down. But, I think Dr. Blyth's chart is really essential that everybody looks at. If you look at our competitors, they are all at almost ten percent higher percent of GDP in revenues than we are, including the Irelands of the world.

So, the notion that we are going to be able to solve this somehow without additional revenues, and the absurdity of people who say, you know, 17.4 percent, we need to get to, because that is our historic averages, well, the thing is, at 17.4 percent, we have never balanced the budget. And, with an enterprise that we have got now with just the demographic bulge, unless we get that revenue line up to 18.5, 19, we are just—we are not getting there, even with entitlement reform.

And, just so I can, again, make sure I am equal opportunity, I think Social Security, best program ever. But, I think when some of us do not acknowledge the math around Social Security, we make a mistake. I, for one, believe the chained CPI, something that

had been agreed on by both economists on the left and the right, makes some sense. I also think the idea that we are going to have different forms of inflation measure for different population sectors does not make sense. And, I do agree with the Ranking Member that raising the cap has to be part of the solution set.

What bothers me, because Social Security and Medicare have been so successful, we have seen poverty rates go for seniors in the 1960s from mid-20s down, and even though the Ranking Member has pointed out they are starting to creep up, thank goodness, because of good advocacy of people like him and others, they are still down at only nine percent.

What bothers the heck out of me, and should bother us all who care about America being competitive, is we have got poverty rates now amongst kids at 24 to 25 percent. And, unfortunately, all of those programs that support those children all come from the discretionary part of the budget and do not get the benefit that Senator Whitehouse mentioned, which I think is a key part of the problem, too, you get it into the tax code, you are safe. You get it onto a mandatory side, you are safe. And, the investments that we need to make for kids somehow are always first on the chopping block.

I would also make the point, and again, with apologies to the panel in terms of not asking questions, that there is, I think, sometimes—and as Governors, we know this—we become more competitive. It is not the lowest tax rate that attracts people. It is quality of workforce. It is your infrastructure. It is your universities. And, unfortunately, America's business plan right now, we have, as a percent of spend, the lowest investment in those domestic discretionary items. We have a lower percentage of spend than we had during President Eisenhower. That is not a good budget plan.

And, unfortunately, at least the Ryan budget plan—and I know, Mr. Chairman, you are going to gavel me out here—the Ryan budget plan takes already historic lows, domestic discretionary at about 16 percent, and cuts it almost in half, down to around eight percent over about a 15-year time frame. Just from your background in finance, my background as a business guy, that is not an enterprise that I would invest in.

So, I do hope that we can—I would charge this group, or, frankly, any other group to come up with a framework. And, if we are willing to come at this with both sides of the ledger, I do think we can get something done.

Again, my apologies to the panel for not asking a question, but this is something that I care very deeply about.

Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Senator Wicker, then Senator King.

Senator WICKER. Well, thank you very much, and I wondered if I would even make it for the discussion because I have had to be in two other hearings.

Let me pick up on what the Senator from Virginia said, though, about chained CPI. I think everyone is in agreement, if you are receiving a Federal retirement benefit, that benefit should not be eaten away by inflation. We all agree on that. The question is how to measure that. And, so, the reason that people like Senator War-

ner and I would be willing to embrace chained CPI is it is deemed by economists to be the most accurate measure of the inflation rate as it affects consumers and, therefore, it would simply be fair. The fact that it would help us on the revenue side and help us on the expenditure side is an added benefit. But, we would need to first make sure that it is, indeed, the most accurate measure of the Consumer Price Index, or the inflation rate, so that a cost-of-living adjustment, a COLA, is, indeed, accurate.

Now, when I came in Senator Warner was talking about making a different rate apply to different individuals. You know, it seems to me he makes a point that if we arrive at an accurate measure of inflation, that ought to be the measure. However, I will just simply say to my fellow committee members, if it would help us get somewhere on an accurate measure of the Consumer Price Index, I would be willing to start it at a certain level of higher-income earners or higher-income retirement recipients and see if it works and see how that can be made to be part of the solution.

If what we are worried about are the lower-income pensioners that might be expecting the higher Consumer Price Index, then we could take care of those people. But, try it at some level, and I am open to suggestion there. I think, and I will say that Senator Warner was on to something, but I would say that we ought to be flexible and not hide-bound if it will get us to a solution.

Let me just ask the panel this, and there is no way we can have a full discussion of this. This is about the benefits of a balanced budget. You know, when I was a freshman back in 1995 in the House of Representatives, the idea of actually getting to a balanced budget within ten years, it was just so troublesome to Chairman Kasich that, I mean, he went back to the Speaker, "Must I really do this?" And, so, we finally came up with a plan to have a balanced budget, and lo and behold, it was much earlier than ten years or seven years.

How did—somebody help me out here. How did we get to a balanced budget so quickly after we finally made up our minds to do that? Of course, we know when we lost the balanced budget, it was September 11, 2001. From that day forward, there has been no hope of a balanced budget at the Federal level since then. But, if you could talk about what were the factors that actually got us to that earlier than expected, and were we going to lose the balanced budget anyway and I am just using 9/11 as an excuse, or are there things that got put into the budget structurally after 9/11 that we just could not get around?

Mr. ENGLER. I would say that a factor that I think is important is the confidence that there was in the U.S. economy. We went through that rather catastrophic shutdown, but then after that, we got a number of things converging. We got welfare reform done. You had split—you had divided control, divided government, but people saw people working together. Decisions were being made. I think there was an easing of regulatory burden at the same time. I just think a number of things combined together. There was confidence in the economy. People were investing. And, a good deal of it came from the private sector growth, and that is one of the things I am a big advocate of.

Ms. MACGUINEAS. One of the things that we did that got us there is we had three budget deals, in 1990, 1993, and 1997, and so a number of real policy choices were made at the time that put us back on a track, and also combined with a growing economy and in some sectors of the economy bubbles, which did not turn out to sustain.

We then lost the deficit—we lost the surplus because we had a huge economic downturn that took away revenues, increased spending. There was money to deal with that. And, we also made policy choices along the way that spent the surpluses. As soon as we had surpluses, it seemed like we were putting in place all sorts of new programs, cutting taxes. Spending was growing faster than it had. And, it reminds us that surpluses kind of take us off of being fiscally more responsible.

The problem we have now is that with the growth of the—the aging of the population and the entitlement programs, it is so much harder to do than it was before. The numbers we have is that it will be about $5.5 trillion to get us to balance in ten years. And, just to put that in perspective, that is eight times the size of the fiscal cliff deal, and it is 65 times the size of the Ryan-Murray deal, which you will recall none of you—I should not say none of you, but we did not stick to for very long. So, it will entail some real policy choices to get us to balance or even on that track, and that is what it took last time. And this time, the challenges because of the growth of the population, the aging of the population, will be even more challenging.

Mr. BLYTH. Going back to what Senator Warner said, and I said in my presentation, you also have a revenue problem, and a particular one. The United States tax revenues are particularly susceptible to the economic cycle. What that means is in the late 1990s, global interest rates fell. Lots of countries did well in that period, not just the United States. And, because of that, money was cheaper and you ended up with a lot of bubbles, first of all in tech stock, and then after 9/11 and we bought them there in 2004, it went into mortgages and it went into the housing bubble. And, when we have those types of bubbles, revenues go up, but they are unsustainable revenues because the base rate of revenue collection is so low.

Senator WICKER. Thank you, Mr. Chairman.

Chairman ENZI. Thank you.

Senator KING.

Senator KING. Mr. Chairman, I have to begin with a hilarious anecdote, which people are going to find hard to believe, but I just looked it up and I was right.

John Engler, you and I sat with Alan Greenspan in January of 2001, where he told us, and I remember because I happened to sit right next to him, about the grave danger to the country of zero budget deficit and the fact that the danger was that the Federal Government, because it was running surpluses, would eventually pay off all its debt and start going into the equity markets. I just found his testimony to the committee in January, January 25, 2001. So, history is a very strange deal, because here we are talking about the danger of deficits. At that time, Alan Greenspan was—he was arguing in favor of the first round of Bush tax cuts,

saying that it was a danger to have surpluses and to balance the budget. Anyway—

Mr. ENGLER. The danger is gone.

Senator KING. Yes, long gone.

[Laughter.]

Senator KING. I agree with almost everything that has been said today, believe it or not, because I believe there is some commonality here. I think long-term debt and deficits are unsustainable and are, in fact, burdening future generations and the interest rate. What worries me is that we are in a fantasy land of interest rates right now, and if the interest rates go from 1.8 or two percent to a long-term average five or six percent, just interest on the debt will almost equal the entire discretionary budget.

What worries me—and, so, I am inclined, and I think all politicians are inclined—it is much easier to spend than it is to tax. So, deficits are almost hard-wired into the system unless there is a discipline. Every State has the discipline of requiring a balanced budget. So, sort of institutionally, I am inclined to support a balanced budget amendment, except the practicality of it—there are two practicalities that make it a problem.

One is that we have spending that is essentially—it is mandatory. That is the word. It means it is uncontrollable. And, that is where the rise is. One of you testified 85 percent of the increase in future budgets is in that area—Social Security, Medicare, Medicaid, and interest on the debt. That is where the increase is.

Discretionary spending, which is what we talk about as the budget, but it is really only a third of the Federal budget, is essentially flat or declining as a percentage of GDP, the lowest in 40 years.

Therefore, if you put a balanced budget amendment on top of that situation, with the mandatory rise caused mostly by health care and demographics, and that is all you do, you squeeze the shortfall down into the discretionary budget and essentially eliminate the Federal Government. We become a collection agent for Social Security, and it squeezes out all of the discretionary programs, whether it is defense or Head Start.

The other piece of—and, I think of it as a vice—and there is another piece that needs to be discussed, has not been mentioned here, and that is the "No Tax Pledge." If you combine a balanced budget amendment with the No Tax Pledge, the only place to go is to eliminate discretionary spending, because it just cannot work. The arithmetic does not work. And, I think of the No Tax Pledge as a kind of ratchet that only works in one direction. Taxes go down. They could never go back up under different circumstances.

So, Mr. Chairman, that is the practical problem that I have. I theoretically like the idea of a balanced budget amendment, but if it is applied in the current situation, as we see it now, with the combination of the growth of health care expenditures and the demographic bulge that is coming, it cannot work, or it can work if your goal is to eliminate Head Start and the defense budget. So, that is the problem that I see now.

We have to come to grips with this. The question is not whether we should balance the budget. I think we should. The question is how to do it and over what period of time and what is on the table in order to do it. You know, we can argue about what the right tax

will be for corporations or individuals, but the real number we ought to be debating is what is the right percentage of GDP for revenues. And, if we are stuck at 17.5 percent, then none of this is going to work unless you are going to eliminate, essentially, all the functions that we think of as essential to the operation of the Federal Government.

My final point is, Dr. Blyth, I bet you never figured you would come from Dundee and have to listen to a guy named Angus talk about economics.

[Laughter.]

Mr. BLYTH. Well, the Scots do secretly run everything, Senator.

[Laughter.]

Mr. BLYTH. We just do not want them to know.

Senator KING. I am sorry you let that out of the bag.

Mr. Chairman, thank you very much.

Chairman ENZI. Thank you.

Senator PERDUE.

Senator PERDUE. Thank you, Mr. Chairman.

I agree with my colleague from Maine, Senator King, in most respects. I differ with just two minor points. I want to get to my other point in just a minute, but I want to respond, because he has got a great point. We have another option. Let me remind people on both sides of the house, I think we all know that the fiscal irresponsibility of the last 30 years cannot continue. It just cannot. This is not a partisan question.

The issue, though, is that we have got the 800-pound gorilla in the room that we never talk about. The last time we had a balanced budget in this country, we had a Democratic President and we had a Republican Congress. We also had something called a dot-com bubble and ten years of good interest rates, but I will not go there, either.

I will say this. It was not our fiscal responsibility in Washington that caused that surplus. It was an economy that was growing like crazy, and I was participating in that. We have that opportunity again, but we are doing so many things in this city to thwart that growth to give us an opportunity to dig out of here, because he is right. The math does not work. You are not going to solve the future unfunded liabilities unless we get this economy going, and even then it is going to take tough, tough decisions up here.

I would argue that the balanced budget is not the issue. I mean, I know that is sort of a first step. I get it. It is sort of the phrase of the day. I love the word "surplus." We do not talk a lot about surplus around here, but we have got to have it if you are going to pay down $18 trillion. And, by the way, if we get to a balanced budget in ten years, we are going to grow the debt by $8 trillion minimally between now and 2025, by most estimates. So, at $25 trillion of debt, if interest rates, as Senator King alluded to just a minute ago, go back to their 30-year historic average, that is untenable. We cannot manage that. There is no way to pay for that. You cannot tax your way out of here. You cannot cut your way out of here, in my view.

Yes, I think Social Security and Medicare and pension benefits for Federal employees all have to be amended, but not by current beneficiaries. The numbers have changed dramatically since peo-

ple—since these systems were developed back in the 1930s, most of them. Life expectancies have gotten longer. The financial balance here of people working versus people in retirement and the demographic slide that we are talking about here, or the growth in the retirement-age population.

So, I just have a question for Ms. MacGuineas. I know you have dedicated a lot of years to this, and I have watched your work. I hope you will stay involved with this, because I think this is the quintessential challenge of our generation. Help me understand the long-term implications of this debt. I understand what the benefits are of a balanced budget, but we have got to get to a surplus situation so we can start paying down this debt to a certain level.

And, I want to take just a second real quick. I absolutely believe that talking—I disagree on one thing, and this is both sides—I think talking about debt and the size of government as a percentage of GDP is an absolute fallacy. Let me give you an example.

In business, you have fixed expenses. We have fixed expenses in the Federal Government. Just because the economy grows three percent over ten years does not mean the Federal Government needs to grow ten percent over three years. So, I think if we start looking at what the real needs are, what the missions are of each of our departments and what money we need to spend, we will end up developing a more realistic and more financially responsible long-term plan.

I am sorry to take so much time, but I want to get to the question, and that is, Ms. MacGuineas, what is your position relative—how do you see the long-term potential, not just getting to a balanced budget in ten years, but past it, because in year 11 to year 20, Social Security quadruples, Medicare quadruples. I just do not—unless we have some type of serious conversation about the long-term implications of this demographic issue, I do not see how we are going to solve this debt crisis.

Ms. MACGUINEAS. Yes, Senator. I agree with you. The key to helping get us out of this, in addition to the policy choices, is growing the economy, and that is true in the short, medium, and long term. And the long term, if we do not get control of the debt, that makes growing the economy all the more challenging.

I also want to add that I agree with Ranking Member Sanders that the other key to this is making sure that when we grow the economy, that growth is shared in a way that we have not been seeing in our economy, and we cannot thrive as a country unless we have a thriving, vibrant middle class and we get rid of some of the poverty that has been taking—

Senator PERDUE. I agree.

Ms. MACGUINEAS. —moving along. So, when I always come here and encourage everybody to compromise and work together on the budget and the fiscal situation, that is to—I think the economy calls for that identical kind of cooperation. That growth and shared growth need to be worked out together. I just think taking the debt as a separate issue is the wrong way to look at it. I think getting control of the debt is an absolutely central component of growing the economy and ensuring that it grows in a way that works for all of us.

Senator PERDUE. Thank you, Mr. Chairman. Thank you.

Chairman ENZI. Thank you.

I really appreciate the comments by the witnesses, the questions by the members of the committee. There is still a chance for people to submit questions, usually of the more technical nature that would just bore any audience out there, but that are essential to making the kinds of decisions that we need to make. So, questions for the record are due no later than 6:00 p.m. today, and hopefully, the witnesses will respond within seven days.

A word of caution to all members of the committee. Chained CPI is a nasty word across America. Now, if you ask seniors what chained CPI is, they have no idea. They just know it is bad. So, I really like the way that it was phrased here, that we need a realistic basket of purchases to come up with that Consumer Price Index or cost-of-living add-on or whatever. So, think about that. Share any other terminology that we can use for that that will not generate the kind of instant hate that we have with chained CPI, and the reason the President left it out of his last budget. I will be around if somebody wants to ask questions about that afterwards.

But, with no further business to come before the committee, we stand adjourned.

[Whereupon, at 12:10 p.m., the committee was adjourned.]

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

We previously reported that fully addressing all the remaining actions identified in GAO's annual duplication and cost savings reports could lead to tens of billions of dollars of additional savings. The following tables include areas identified through the annual reports that could potentially result in cost savings or revenue enhancements. Where possible, we relied on estimates from the Congressional Budget Office and the Joint Committee on Taxation. We also developed estimates based on agencies' data and used agencies' developed estimates.

The totals reflect a summary of these estimates, which relied on different data sources and methodologies and considered different time periods, and represent a rough estimate of financial benefits (and may or may not result in direct budget savings). These estimates may understate the eventual savings that will accrue, as we used a conservative approach in aggregating these data.[1] Further, these estimates represent GAO's work when each estimate was created, and actual savings will vary due to factors associated with inflation, changes in costs, and due to the timing and degree of agency and congressional action.

- **Table 1** includes areas with actions that have specific cost savings or revenue enhancement estimates. Based on available data, these areas, if fully addressed, could potentially provide financial benefits to the government ranging from roughly $45 billion to $50 billion.

- **Table 2** includes areas where GAO's work has included more general estimates of potential cost savings or revenue enhancements. Based on available data, these areas, if fully addressed, could potentially provide roughly $30 billion in financial benefits.

  These estimates have a higher degree of uncertainty because they may rely on more limited data, be sensitive to the timing of congressional and executive-branch agencies' actions, and may reflect greater uncertainty about agencies' approach to implementing our recommendations and congressional direction. For example, in 2013, we reported that federal agencies could achieve significant cost savings annually by expanding and improving their use of strategic sourcing—a contracting process that moves away from numerous individual procurement actions to a broader aggregated approach. In particular, in fiscal year 2011, the Departments of Defense (DOD), Homeland Security, Energy, and Veterans Affairs accounted for 80 percent of the $537 billion in federal procurement spending, but reported managing about 5 percent or $25.8 billion through strategic sourcing efforts. In contrast, leading commercial firms leverage buying power by strategically managing 90 percent of their spending—achieving savings of 10 percent or more of total procurement costs. While strategic sourcing may not be suitable for all procurement spending, we reported that a reduction of 1 percent in spending from large procurement agencies, such as DOD, would equate to over $4 billion in savings annually.[2]

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[1]In particular, we used the bottom of individual estimate ranges and the shortest time period associated with each estimate.

[2]In December 2014, the Office of Management and Budget (OMB) issued a memorandum on category management that, among other things, identifies federal spending categories suitable for strategic sourcing. These categories cover some of the government's largest spending categories, including information technology and professional services. According to OMB, these categories account for $277 billion in fiscal year 2013 federal procurements. This level of spending suggests that by using smarter buying practices the government could realize billions of dollars in savings. However, until OMB sets government-wide goals and establishes metrics, the government may miss opportunities for cost savings through strategic sourcing.

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

- **Table 3** includes areas with potential cost savings or revenue enhancements for which the available estimates are descriptive estimates of savings magnitude (e.g., millions or billions in savings). For these estimates, the minimum of the descriptive estimate was used. For example, "billions" is counted as $1 billion, "millions" is counted as $1 million, and "hundreds of millions" is counted as $100 million. Based on this information, these actions, if fully addressed, could potentially provide roughly $9 billion in financial benefits.

- **Table 4** identifies additional areas from GAO's work that could help avoid future federal costs, including reducing cost growth in the $1.5 trillion invested in major defense acquisition programs, narrowing the $385 billion net tax gap, and reducing the almost $125 billion in government-wide improper payments, including in the areas of Medicare, Medicaid, and the Earned Income Tax Credit. Given the scope of these issues, even modest gains in efficiency and effectiveness would result in significant savings.

- **Table 5** identifies areas with actions taken by Congress or executive branch agencies that include financial benefits that are accruing as a result of our work. We reported on these financial benefits in our 2015 annual report, stating that executive branch and congressional efforts to address suggested actions resulted in roughly $20 billion in financial benefits from fiscal years 2011 through 2014, with another approximately $80 billion in additional benefits projected to be accrued through 2023. These estimates of totals were rounded down to the nearest $10 billion.

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

**Table 1: Areas with Dollar Savings Estimates (in millions)**

| Year | Area # | Area | Source of estimate | Estimated financial benefit |
|---|---|---|---|---|
| **Income Security** | | | | |
| 2011 | 80 | **Social Security Offsets**: Social Security needs data on pensions from noncovered earnings to better enforce offsets and ensure benefit fairness, estimated to result in **$2.4-$6.5 billion savings over 10 years** if enforced both retrospectively and prospectively. If Social Security only enforced the offsets prospectively, the overall savings would be less as it would not reduce benefits already received. | CBO/OMB | $2,400-6,500 |
| 2014 | 8 | **Disability and Unemployment Benefits**: Congress should consider passing legislation to prevent individuals from collecting both full Disability Insurance benefits and Unemployment Insurance benefits that cover the same period, which could save **$1.2 billion over 10 years** in the Social Security Disability Insurance program according to the Congressional Budget Office. | CBO | 1,200 |
| 2015 | 21 | **Children's Disability Reviews**: To prevent **an estimated $3.1 billion** in potential overpayments **over 5 years**, the Social Security Administration needs to conduct timely disability reviews to better ensure that only eligible children receive cash benefits from the Supplemental Security Income program. | GAO | 3,100 |
| **Tax Policies and Enforcement** | | | | |
| 2014 | 15 | **Collection of Unpaid Federal Taxes**: The federal government could increase tax revenue collections by **$500 million over a 5-year time period**, according to a 2012 Congressional Budget Office estimate, by identifying and taking actions to limit issuance of passports to applicants with unpaid federal taxes. *Savings may also be realized from addressing the other two actions in this area—levying payments to Medicaid providers and identifying security-clearance applicants with unpaid federal taxes—but no estimate of savings is available for these actions.* | CBO | 500 |
| 2011 | 56 | **Simple Tax Return Errors**: Congress could grant the Internal Revenue Service broader authority, with appropriate safeguards against misuse of that authority, to correct math errors during tax return processing. In March 2015, the Joint Committee on Taxation estimated that this change could result in **$133 million in savings over 10 years**. | JCT | 133 |
| **Information Technology** | | | | |
| 2011 | 15 | **Federal Data Centers**: Consolidating federal data centers would provide an opportunity to improve government efficiency and achieve cost savings and avoidances of **about $7.5 billion** by fiscal year 2017. | GAO/Agencies | 7,450 |
| **Energy** | | | | |
| 2014 | 13 | **Advanced Technology Vehicles Manufacturing (ATVM) Loan Program**: Unless the Department of Energy can demonstrate demand for new ATVM loans and viable applications, Congress may wish to consider rescinding all or part of the remaining **$4.2 billion** in credit subsidy appropriations. | GAO | 4,200 |
| 2015 | 16 | **U.S. Enrichment Corporation Fund**: Congress may wish to consider permanent **rescission of the entire $1.6 billion balance** of the U.S. Enrichment Corporation Fund—a revolving fund in the U.S. Treasury—because its purposes have been fulfilled. | GAO | 1,600 |
| 2015 | 15 | **Strategic Petroleum Reserve (SPR)**: By reducing the SPR to 90 days, DOE may be able to reduce its operating costs by **about $25 million per year**. *The potential revenues from selling the reserve depend on the amount and price of crude oil sold; the potential magnitude of that estimate is captured in table 3.* | GAO | 25 |
| 2011 | 45 | **Oil and Gas Resources**: Improved management of federal oil and gas resources could result in approximately **$2 billion in additional revenue over 10 years.** | Agency | 2,000 |

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

| Year | Area # | Area | Source of estimate | Estimated financial benefit |
|---|---|---|---|---|
| **Agriculture** | | | | |
| 2013 | 19 | **Crop Insurance**: To achieve **up to nearly $2 billion per year** in cost savings in the crop insurance program, Congress could consider limiting the subsidy for premiums that are provided on behalf of individual farmers, reducing the subsidy, or some combination of limiting and reducing these subsidies. *Savings would depend on the option selected.* | GAO | 2,000 |
| 2013 | 1 | **Catfish Inspection**: Repealing provisions of the 2008 Farm Bill that assigned U.S. Department of Agriculture's (USDA) Food Safety and Inspection Service responsibility for examining and inspecting catfish and for creating a catfish inspection program would avoid duplication of federal programs and could save taxpayers millions of dollars annually without affecting the safety of catfish intended for human consumption. USDA estimated that implementation of its catfish inspection program would cost the federal government and industry **an additional $14 million annually**. The Food and Drug Administration estimated that its annual cost for inspecting catfish-processing facilities was about $700,000. | Agency | 14 |
| **Health** | | | | |
| 2012 | 46 | **Medicare and Medicaid Fraud Detection Systems**: The Centers for Medicare & Medicaid Services would need to ensure widespread use of its fraud detection systems to better position itself to determine and measure progress toward achieving the **$21 billion in financial benefits** that the agency projected as a result of implementing these systems. | Agency | 21,000 |
| 2015 | 19 | **Medicare Payments to Certain Cancer Hospitals**: To achieve **almost $500 million per year** in program savings, Congress should consider modifying how Medicare pays certain cancer hospitals. | GAO | 500 |
| **Homeland Security** | | | | |
| 2013 | 28 | **Checked Baggage Screening**: By reviewing the appropriateness of the federal cost share the Transportation Security Administration (TSA) applies to agreements that finance modification projects related to the installation of checked baggage screening systems at airport facilities, TSA could, if a reduced cost share were deemed appropriate, achieve cost efficiencies and be positioned to install a greater number of optimal baggage screening systems than currently anticipated. According to TSA, as of March 2015, their data show that lowering the cost share from 90 percent to 75 percent could result in **roughly $140 million in cost efficiencies during the fiscal year 2015 to 2030 timeframe**. | Agency | 140 |

Source: GAO.

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

**Table 2: Areas with Dollar Savings Estimates Involving Assumptions with Higher Levels of Uncertainty**

| Year | Area # | Area | Estimated financial benefit |
|---|---|---|---|
| 2014 | 21 | **Medicaid Demonstration Waivers**: Federal spending on Medicaid demonstrations could be reduced by billions of dollars if the Department of Health and Human Services were required to improve the process for reviewing, approving, and making transparent the basis for spending limits approved for Medicaid demonstrations. GAO estimated the federal share of savings **could have been up to $21 billion over 5 years** for two states' recent demonstrations that GAO reviewed. | $21,000 |
| 2013 | 23 | **Agencies' Use of Strategic Sourcing**: Selected agencies could better leverage their buying power and achieve additional savings by directing more procurement spending to existing strategically sourced contracts and further expanding strategic sourcing practices to their highest-spending procurement categories—savings of 1 percent from selected agencies' procurement spending alone would equate to over **$4 billion annually**. | 4,000 |
| 2012 | 51 | **Domestic Disaster Assistance**: The Federal Emergency Management Agency (FEMA) could reduce the costs to the federal government related to major disasters declared by the President by updating the principal indicator on which disaster funding decisions are based and better measuring a state's capacity to respond without federal assistance. For fiscal years 2004 through 2011, had FEMA adjusted the indicator for increases in inflation or personal income since 1986, fewer jurisdictions would have met the primary criterion FEMA uses to determine whether to recommend that the President declare a major disaster, which **could have reduced federal cost by as much as $3.59 billion**. | 3,590 |
| 2013 | 31 | **Tobacco Taxes**: Federal revenue losses ranged from as much as **$615 million to $1.1 billion between April 2009 and 2011** because manufacturers and consumers substituted higher-taxed smoking tobacco products with similar lower-taxed products. To address future revenue losses, Congress should consider modifying tobacco tax rates to eliminate significant tax differentials between similar products. | 615-1,100 |
| 2014 | 12 | **Combatant Command Headquarters Costs**: If the Department of Defense (DOD) applied the 20 percent reduction in management headquarters spending to the $1.7 billion the department used to operate and support the five geographic combatant commands in fiscal year 2012, DOD could potentially achieve up to an estimated **$340 million in annual savings**. | 340 |
| 2013 | 18 | **Agricultural Quarantine Inspection Fees**: The United States Department of Agriculture's Animal and Plant Health Inspection Service could have achieved as much as **$325 million in savings** (based on fiscal year 2011 data, as reported) by more fully aligning fees with program costs; although the savings would be recurring, the amount would depend on the cost-collections gap in a given fiscal year and would result in a reduced reliance on U.S. Customs and Border Protection's annual Salaries and Expenses appropriations used for agricultural inspection services. | 325 |
| 2012 | 49 | **Immigration Inspection Fee**: The user fee for immigration inspection of air and sea passengers should be reviewed and adjusted to fully recover the cost of the air and sea passenger immigration inspection activities conducted by the Department of Homeland Security's U.S. Immigration and Customs Enforcement and U.S. Customs and Border Protection rather than relying on general fund appropriations; in 2012 this could have resulted in reduced reliance on general fund appropriations used for inspection services by **about $175 million**. | 175 |

Source: GAO.
Note: GAO developed the estimated financial benefits identified in this table.

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

**Table 3: Areas with Notional (i.e., estimated millions of dollars, billions of dollars) Financial Benefits**
As previously noted, these areas involve rough descriptive estimates, and the minimum of that estimate was used. For example, "billions" is counted as $1 billion, "millions" is counted as $1 million, and "hundreds of millions" is counted as $100 million. Action status for the 2011-2014 areas vary within the area—i.e., a mix of fully, partially, or not addressed actions. The status of 2015 actions is pending.

| Year | Area # | Area | Estimated financial benefit (in millions) |
|---|---|---|---|
| **Defense and Contracting** | | | |
| 2011 | 6 | **Tactical Wheeled Vehicles**: A departmentwide acquisition strategy could reduce the Department of Defense's risk of costly duplication in purchasing Tactical Wheeled Vehicles. Reducing the number of joint light tactical vehicles DOD procures could result in *billions of dollars in cost savings*. | $1,000 |
| 2015 | 14 | **DOD Headquarters Reductions and Workforce Requirements**: The Department of Defense could potentially achieve *hundreds of millions of dollars in cost savings* and help to ensure that headquarters organizations are properly sized to meet their assigned missions by re-evaluating its ongoing headquarters-reductions efforts and conducting periodic reassessments of workforce requirements. | 100 |
| **Energy** | | | |
| 2015 | 15 | **Strategic Petroleum Reserve** (for potential revenues from selling some of the reserve): The Department of Energy could potentially *realize savings* by reexamining the appropriate size of the Strategic Petroleum Reserve—which was *valued at about $45 billion* as of December 2014—and depending on the outcome of the analysis, selling crude oil from the reserve and using the proceeds to fund other national priorities. | 1,000 |
| **Health** | | | |
| 2011 | 71 | **Medicaid Improper Payments**: *Preventing billions in Medicaid improper payments* requires sustained attention and action by the Centers for Medicare & Medicaid Services. | 1,000 |
| 2013 | 26 | **Medicaid Supplemental Payments**: To improve the transparency of and accountability for certain high-risk Medicaid payments that annually total tens of billions of dollars, Congress should consider requiring the Centers for Medicare & Medicaid Services to take steps that would facilitate the agency's ability to oversee these payments, including identifying payments that are not used for Medicaid purposes or are otherwise inconsistent with Medicaid payment principles, which could lead to cost savings. GAO's analysis of providers for which data are available suggests that *savings could be in the hundreds of millions, or billions, of dollars*. | 100 |
| 2015 | 6 | **DOD US Family Health Plan**: To potentially *save millions of dollars* and eliminate duplication within the Department of Defense's health care system, Congress should terminate the statutorily required US Family Health Plan because it offers military beneficiaries the same health care benefit offered by other Department of Defense health care contractors. | 1 |
| **Information Technology** | | | |
| 2014 | 24 | **Information Technology Investment Portfolio Management (PortfolioStat)**: The Office of Management and Budget and multiple agencies could help the federal government realize *billions of dollars in savings* by taking steps to better implement PortfolioStat, a process to help agencies manage their information technology investments. | 1,000 |
| 2013 | 30 | **Information Technology Operations and Maintenance**: Strengthening oversight of key federal agencies' major information technology investments in operations and maintenance would provide an opportunity for *savings on billions in information technology investments*. | 1,000 |
| 2015 | 23 | **Federal Software Licenses**: In order to achieve *hundreds of millions of dollars in government-wide savings*, federal agencies should apply better management of software licenses and the Office of | 100 |

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

| Year | Area # | Area | Estimated financial benefit (in millions) |
|---|---|---|---|
| | | Management and Budget should issue a directive to assist agencies in doing so. | |
| **Tax Policies and Enforcement** | | | |
| 2011 | 17 | **Tax Expenditures**: Periodic reviews could help identify ineffective tax expenditures and redundancies in related tax and spending programs, potentially *reducing revenue losses by billions of dollars*. | 1,000 |
| 2013 | 22 | **Additional Opportunities to Improve Internal Revenue Service Enforcement of Tax Laws**: The Internal Revenue Service can realize *cost savings and increase revenue collections by billions of dollars* by, among other things, using more rigorous analyses to better allocate enforcement and other resources. | 1,000 |
| 2012 | 44 | **Internal Revenue Service Enforcement Efforts**: Enhancing the Internal Revenue Service's enforcement and service capabilities can help reduce the gap between taxes owed and paid by *collecting billions in tax revenue* and facilitating voluntary compliance. | 1,000 |
| 2015 | 17 | **Tax Policies and Enforcement**: By more effectively using data to manage various enforcement programs, the Internal Revenue Service could bolster tax compliance and potentially collect *hundreds of millions of dollars in additional revenue*. | 100 |
| 2011 | 63 | **S Corporations**: Congress and the Internal Revenue Service can help S corporations and their shareholders be more tax compliant, potentially increasing tax revenues by *hundreds of millions of dollars each year*. | 100 |
| 2014 | 17 | **Online Taxpayer Services**: The Internal Revenue Service could potentially realize *hundreds of millions of dollars in cost savings and increased revenues* by enhancing its online services, which would improve service to taxpayers and encourage greater tax law compliance. | 100 |
| 2011 | 59 | **Real Estate Tax Deductions**: Better information and outreach could help *increase revenues by tens or hundreds of millions of dollars annually* by addressing overstated real estate tax deductions. | 10 |
| **General Government** | | | |
| 2013 | 24 | **Opportunities to Help Reduce Government Satellite Program Costs**: Government agencies could achieve considerable cost savings on some missions by leveraging commercial spacecraft through innovative mechanisms such as hosted payload arrangements and sharing launch vehicle costs. Selected agencies have *reported saving hundreds of millions of dollars* to date from using these innovative mechanisms. | 100 |
| **Social Services** | | | |
| 2014 | 25 | **Better Data to Mitigate Foreclosures**: The Department of Housing and Urban Development's Federal Housing Administration and the Departments of Veterans Affairs and Agriculture could improve outcomes and better manage the costs associated with foreclosure mitigation efforts with additional data collection and analysis, potentially *saving taxpayers millions of dollars on an annual and recurring basis*. | 1 |
| 2014 | 26 | **Housing Choice Vouchers Rent Reform**: By improving data collection and analysis efforts under the Moving to Work demonstration program, the Department of Housing and Urban Development would provide Congress with information to determine which rent reform option should be implemented program-wide and thereby potentially *reduce program funding by millions of dollars* or extend housing assistance to additional low-income households or some combination of these outcomes. | 1 |

Source: GAO.

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

**Table 4: Select Areas that Could Help Reduce Future Costs**
In addition to the areas noted in the other tables, GAO's work has identified opportunities to help avoid future federal costs, including reducing cost growth in the $1.5 trillion invested in major defense acquisition programs, narrowing the $385 billion net tax gap, and reducing the almost $125 billion in government-wide improper payments, including in the areas of Medicare, Medicaid, and the Earned Income Tax Credit. Given the scope of these issues, even modest gains in efficiency and effectiveness would result in significant savings.

| |
|---|
| **Reduce Cost Growth in Defense** |
| **Weapon Systems Acquisition Programs** (2011, Area 38): Employing best management practices could help the Department of Defense (DOD) achieve significant cost savings on the $1.4 trillion (fiscal year 2015 dollars) it expects to invest in the development and procurement of its portfolio of 78 major defense acquisition programs. |
| **Military Health Care Costs** (2012, Area 36): To help achieve significant projected cost savings and other performance goals, DOD needs to complete, implement, and monitor detailed plans for each of its approved health care initiatives |
| **Military Personnel Costs (2011, Area 37)**: A total compensation approach would be needed to manage military personnel costs—which grew 31 percent from fiscal year 2001 to fiscal year 2014. |
| **Narrow the Tax Gap** |
| **Tax Policies and Enforcement** (2014, Area 20): The Internal Revenue Service (IRS) can realize cost savings and increase revenue by, among other things, identifying continued offshore tax evasion and evaluating whether the agency's streamlined corporate audit process is meeting its goals. |
| **Sole Proprietors** (2011, Area 61): Many options could improve the tax compliance of sole proprietors and begin to reduce their $68 billion portion of the tax gap. |
| **Businesses Not Filing Tax Returns** (2011, Area 62): The Internal Revenue Service could find additional businesses not filing tax returns by using third-party data, which show such businesses have billions of dollars in sales. |
| **Reduce Medicare and Medicaid Improper Payments and Improve Program Integrity** |
| **Improving use of automated edits.**[4] In November 2012, GAO reported that use of prepayment edits saved Medicare at least $1.76 billion in fiscal year 2010, but savings could have been greater if prepayment edits had been more widely used.[5] |
| **Monitoring postpayment claims reviews.** To improve the efficiency and effectiveness of Medicare program integrity efforts, GAO recommended in July 2014 that CMS reduce differences between contractor postpayment review requirements, when possible, and monitor the database used to track recovery audit activities to ensure that all data were submitted, accurate, and complete.[6] |
| **Removing Social Security numbers from Medicare cards.** The health insurance claims number on Medicare beneficiaries' cards includes as one component the Social Security number of the beneficiary (or other eligible person, such as a spouse). This introduces risks that the beneficiaries' personal information could be obtained and used to commit identity theft.[7] To better position the agency to efficiently and cost-effectively identify, design, develop, and implement a solution to address this issue, GAO recommended that CMS direct the initiation of an IT project for identifying, developing, and implementing changes that would have to be made to CMS's affected systems. |
| **Implementing actions authorized by the Patient Protection and Affordable Care Act (PPACA).** GAO reported in the February 2015 update to its high-risk series that CMS should fully exercise its PPACA authority related to strengthening its provider and supplier enrollment provisions.[8] The following summarizes additional open recommendations and procedures authorized by PPACA that CMS should implement to make progress toward fulfilling the four outstanding criteria to remove Medicare improper payments from GAO's high-risk list. CMS should<br>• require a surety bond for certain types of at-risk providers and suppliers;<br>• publish a proposed rule for increased disclosures of prior actions taken against providers and suppliers enrolling or revalidating enrollment in Medicare, such as whether the provider or supplier has been subject to a payment suspension |

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

from a federal health care program;

- establish core elements of compliance programs for providers and suppliers;
- improve automated edits that identify services billed in medically unlikely amounts;
- develop performance measures for the Zone Program Integrity Contractors who explicitly link their work to the agency's Medicare FFS program integrity performance measures and improper payment reduction goals; and
- require Medicare administrative contractors to share information about the underlying policies and savings related to their most effective edits.

**Improving third-party liability efforts.** Congress generally established Medicaid as the health care payer of last resort, meaning that if enrollees have another source of health care coverage—such as private insurance—that source should pay, to the extent of its liability, before Medicaid does. This is referred to as third-party liability. However, there are known challenges to ensuring that Medicaid is the payer of last resort. While CMS has issued guidance to states, GAO recommended additional actions that could help to improve cost-saving efforts in this area, such as monitoring and sharing information on third-party liability efforts and challenges across all states and providing guidance to states on oversight of third-party liability efforts related to Medicaid managed care plans.[7]

**Increasing oversight of managed care.** Most Medicaid beneficiaries are in managed care, and managed care expenditures have been growing at a faster rate than fee-for-service expenditures. In May 2014, GAO reported that most state and federal program integrity officials GAO interviewed stated that they did not closely examine managed care payments, focusing on fee-for-service claims instead.[8] To help improve the efficiency and effectiveness of program integrity efforts, GAO recommended that CMS require states to conduct audits of payments to and by managed care organizations, update managed care guidance on program integrity practices, and provide states with additional support in overseeing managed care program integrity.

**Strengthening program integrity.** Although CMS has taken positive steps to oversee program integrity efforts in Medicaid, other actions remain, such as improving reporting of key data, strengthening its efforts to calculate return on investment for its program integrity efforts, and using knowledge gained from its comprehensive reviews of states to better focus audit resources and improve recovery of improper payments.

**Reduce Earned Income Tax Credit (EITC) Improper Payments**

**Regulating Paid Tax Preparers.** In August 2014, IRS reported that 68 percent of all tax returns claiming the EITC in tax years 2006 and 2007 were prepared by paid tax preparers—most of whom were not subject to any IRS regulation—and that from 43 percent to 50 percent of the returns overclaimed the credit.[9] Similarly, in GAO's undercover visits to randomly selected tax preparers, a sample that cannot be generalized, GAO found errors in EITC claims, resulting in significant overstatement of refunds.[1] Based in part on GAO's recommendation, in 2010, IRS initiated steps to regulate certain preparers through testing and education requirements; however, the courts ruled that IRS lacked such regulatory authority.[2] In 2014, GAO suggested that Congress consider granting IRS the authority to regulate paid tax preparers, if it agrees that significant paid preparer errors exist. In September 2015, the Joint Committee on Taxation estimated that regulating tax preparers would raise $135 million in revenue through 2025.

**Accelerating W-2 filing deadline.** IRS estimates that it paid $5.8 billion in fraudulent identity theft refunds during the 2013 filing season.[3] While GAO does not know the extent to which improper EITC payments are the result of identity theft, IRS has reported that improper payments are a mix of unintentional mistakes and fraud. IRS issues most refunds months before receiving and matching information returns, such as the W-2 "Wage and Tax Statement," to tax returns. In August 2014, GAO recommended that IRS estimate the cost and benefits of options to implement pre-refund matching using W-2 data.[7] Given that any change could impose burdens on employers and taxpayers as well as create additional costs to IRS for systems and process changes, Congress and other stakeholders need information on this impact to fully assess any potential changes. In September 2015, the Senate Committee on Finance scheduled a committee markup of a bill to prevent identity theft and tax refund fraud, including a provision to modify due dates for filing Forms W-2. The Joint Committee on Taxation estimated that the provision would raise $151 million in revenue through fiscal year 2025.

Source: GAO.

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

[a]To help ensure that payments are made properly, CMS uses controls called edits that are programmed into claims processing systems to compare claims data with Medicare requirements in order to approve or deny claims or flag them for further review.
[b]See GAO, *Medicare Program Integrity: Greater Prepayment Control Efforts Could Increase Savings and Better Ensure Proper Payment*, GAO-13-102 (Washington, D.C.: Nov. 13, 2012).
[c]GAO, *Medicare Program Integrity: Increased Oversight and Guidance Could Improve Effectiveness and Efficiency of Postpayment Claims Reviews*, GAO-14-474 (Washington, D.C.: July 18, 2014). GAO suggests actions related to monitoring postpayment claims reviews in the 2015 Annual Report Area 7: Medicare Postpayment Claims Reviews.
[d]See GAO, *Medicare Information Technology: Centers for Medicare and Medicaid Services Needs to Pursue a Solution for Removing Social Security Numbers from Cards*, GAO-13-761 (Washington, D.C.: Sept. 10, 2013).
[e]See GAO, *High-Risk Series: An Update*, GAO-15-290 (Washington, D.C.: Feb. 11, 2015).
[f]See GAO, *Medicaid: Additional Federal Action Needed to Further Improve Third-Party Liability Efforts*, GAO-15-208 (Washington, D.C.: Jan. 28, 2015).
[g]See GAO, *Medicaid Program Integrity: Increased Oversight Needed to Ensure Integrity of Growing Managed Care Expenditures*, GAO-14-341 (Washington, D.C.: May 19, 2014).
[h]*Internal Revenue Service, Compliance Estimates for the Earned Income Tax Credit Claimed on 2006- 2008 Returns*, Publication 5162 (8-2014) (Washington, D.C.: August 2014).
[i]GAO, *Paid Tax Return Preparers: In a Limited Study, Preparers Made Significant Errors*, GAO-14-467T (Washington, D.C.: Apr. 8, 2014), and Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Significant Errors, GAO-06-563T (Washington, D.C.: Apr. 4, 2006).
[j]*Loving v. IRS*, 917 F. Supp. 2d 67 (D.D.C. 2013), *aff'd* 742 F.3d 1013 (D.C. Cir. 2014).
[k]GAO, *Identity and Tax Fraud: Enhanced Authentication Could Combat Refund Fraud, but IRS Lacks an Estimate of Costs, Benefits and Risks*, GAO-15-119 (Washington, D.C.: Jan. 20, 2015).
[l]GAO, *Identity Theft: Additional Actions Could Help IRS Combat the Large, Evolving Threat of Refund Fraud*, GAO-14-633 (Washington, D.C.: Aug. 20, 2014).

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

**Table 5: Areas with Actions Taken by Congress and Executive Branch Agencies that Resulted In or Are in the Process of Leading to Financial Benefits**

| Year | Area # | Area | Estimated financial benefit, 2011-2014 (in millions) | Estimated financial benefit, 2015-2023 (in millions) |
|---|---|---|---|---|
| **Energy** | | | | |
| 2011 | 13 | **Domestic Ethanol Production**: Congress allowed the Volumetric Ethanol Excise Tax Credit to expire at the end of 2011, which eliminated duplicative federal efforts directed at increasing domestic ethanol production and reduced revenue losses by **$4.5 billion in fiscal year 2012 and $6.1 billion in fiscal year 2013.** | $16,500 | $9,000 |
| **Agriculture** | | | | |
| 2011 | 35 | **Farm Program Payments**: The Agricultural Act of 2014 eliminated direct payments to farmers and should save approximately **$4.9 billion annually** from fiscal year 2015 through fiscal year 2023, according to the Congressional Budget Office (CBO). | - | 44,100 |
| **Homeland Security** | | | | |
| 2012 | 48 | **Passenger Aviation Security Fees**: The Bipartisan Budget Act of 2013 modifies the passenger security fee from its current per enplanement structure ($2.50 per enplanement with a maximum one-way-trip fee of $5.00) to a structure that increases the passenger security fee to a flat $5.60 per one-way-trip, effective July 1, 2014.[a] Pursuant to the act, collections under this modified fee structure will contribute to deficit reduction as well as to offsetting TSA's aviation security costs.[b] Specifically, the act identifies **$12.6 billion** in fee collections that, over a 10-year period **beginning in fiscal year 2014 and continuing through fiscal year 2023**, should contribute to deficit reduction.[c] Fees collected beyond those identified for deficit reduction are available, consistent with existing law, to offset TSA's aviation security costs. According to the House of Representatives and Senate Committees on the Budget, and notwithstanding amounts dedicated for deficit reduction, collections under the modified fee structure will offset about 43 percent of aviation security costs, compared to the approximate 30 percent currently offset under the existing fee structure.[d] | 1,260 | 11,340 |
| 2012 | 47 | **Border Security**: To limit future program funding for the Arizona Border Surveillance Technology Plan (Plan) as GAO suggested in February 2012, legislation was enacted for fiscal years 2013 and 2014. Specifically, the Department of Homeland Security Appropriations Act for **fiscal year 2013** rescinded **$73.2 million** from funds appropriated for the Plan in fiscal years 2011 and 2012. In addition, the enacted rescission under the Consolidated Appropriations Act for **fiscal year 2014** was approximately **$67.5 million** from unobligated prior-year balances for the U.S. Customs and Border Protection's border security fencing, infrastructure, and technology account, under which the Plan is funded. | 140.7 | - |
| 2011 | 78 | **Baggage Screening Systems**: The Transportation Security Administration estimated that the agency saved a cumulative **$104.5 million** in personnel costs **from fiscal years 2011 through 2013** from its efforts to replace or modify older checked baggage screening systems with more efficient in-line systems, as GAO suggested. | 104.5 | - |

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

| Year | Area # | Area | Estimated financial benefit, 2011-2014 (in millions) | Estimated financial benefit, 2015-2023 (in millions) |
|---|---|---|---|---|
| 2011 | 79 | **Customs Fee Collections**: U.S. Customs and Border Protection (CBP) officials told us that in September 2012, CBP transferred $639.4 million into an unavailable treasury receipt account. This action, according to these officials, effectively removed **$639.4 million** from CBP's financial reports and addressed the House Committee on Appropriation's request to provide a status of the funds and a path forward for eliminating these funds from CBP financial reports. | 639.4 | - |
| **Defense** | | | | |
| 2013 | 2 | **Combat Uniforms**: Consistent with GAO's recommendation, the Army chose not to introduce a new family of camouflage uniforms into its inventory, resulting in a cost avoidance of about **$4.2 billion over 5 years**. | - | 4,200 |
| 2012 | 37 | **Overseas Defense Posture**: The United States Forces Korea conducted a series of consultations with the military services to evaluate the costs and benefits associated with tour normalization, as GAO suggested, and decided not to move forward with the full tour normalization initiative because it was not affordable. The Department of Defense's (DOD) decision to not move forward with this initiative resulted in a cost avoidance of **$3.1 billion from fiscal years 2012 through 2016**. | 1,860 | 1,240 |
| 2011 | 36 | **Overseas Military Presence**: In February 2012, the Army announced its decision to permanently reduce the number of U.S. ground forces in Europe by: inactivating two of the four brigade combat teams stationed there, the first to occur in fiscal year 2013, and the second to occur in fiscal year 2014; inactivating its Germany-based V Corps headquarters in fiscal year 2013; and reducing the number of combat support and combat service support positions in Europe by approximately 2,500 positions. Based on the Army's analysis, the closure and consolidation of facilities in Europe presently being used by the forces earmarked for inactivation could result in cost savings of **$2 billion over 10 years**. In addition, the overall savings to DOD could be substantially more when the units are taken out of the force structure since the Army will no longer incur the equipping and other costs associated with those units. | 400 | 1,600 |
| 2012 | 34 | **Defense Headquarters**: DOD announced that the military services, combatant commands, and other headquarters within the department were finalizing their reviews and plans to meet the headquarter budget reduction. The fiscal year 2015 President's budget request stated that DOD's efforts to reduce management headquarters staffs will result in savings of **$5.3 billion through fiscal year 2019**. In February 2015, the fiscal year 2016 President's budget request for DOD was submitted to Congress, including the department's initial headquarters reductions. DOD stated that the specific reduction plans have been identified in the Future Years Defense Program and it is still on track to achieve $5.3 billion in headquarters reductions, but DOD did not include its specific reduction plans for future years in the budget request. According to DOD officials, the largest savings will occur in fiscal year 2019, and DOD will continue to refine its plans for headquarters reductions during future President's budget submissions. | - | 5,300 |

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

| Year | Area # | Area | Estimated financial benefit, 2011-2014 (in millions) | Estimated financial benefit, 2015-2023 (in millions) |
|---|---|---|---|---|
| 2011 | 2 | **DOD's Military Medical Command**: DOD has taken action to further assess alternatives for restructuring the governance structure of its Military Health System in order to reduce duplication within the command structure and eliminate redundant processes that add to growing defense health care costs. This effort could result in projected savings ranging from **$281 million** to $460 million annually. | 281 | - |
| 2012 | 38 | **Navy's Information Technology Enterprise Network**: The Navy has completed various plans and analyses, including an official life-cycle cost estimate that has **decreased the amount** it planned to spend on the Next Generation Enterprise Network **from about $15.6 billion to $13.0 billion** between fiscal years 2013 and 2017. | - | 1,560 |
| 2012 | 33 | **Air Force Food Service**: In 2011, the Air Force issued a memorandum to the Major Commands directing a review of existing food service contracts. As a result, according to Air Force officials, the Air Force reviewed and renegotiated the food service contracts at eight installations for a total savings of over **$2.5 million per year**. In addition, according to Air Force officials, all food service contracts were validated again during fiscal year 2012 for additional savings of over **$2.2 million per year**. Air Force officials said that the Air Force will review contracts annually for areas where costs can be reduced. | 7.2 | - |
| **Health** | | | | |
| 2011 | 74 | **Medicare's Health Care Payments**: The Patient Protection and Affordable Care Act requires that the Secretary of Health and Human Services identify potentially misvalued codes by examining multiple codes that are frequently billed in conjunction with furnishing a single service. In implementing this provision in 2011, CMS expanded the imaging multiple procedure payment reduction (MPPR) to the technical component of additional imaging services (i.e., the portion of the payment that covers the actual performance of the service) and implemented a 25 percent MPPR for the practice expense component for certain therapy services. The Physician Payment Therapy and Relief Act of 2010 subsequently reduced the MPPR for these therapy services from 25 to 20 percent. However, under the American Taxpayer Relief Act of 2012, Congress increased the MPPR for therapy services to 50 percent for services provided on or after April 1, 2013. The Congressional Budget Office has estimated that this MPPR increase will save **$1.8 billion over 10 years.** | 360 | 1,440 |
| 2012 | 45 | **Medicare Advantage Payment**: Consistent with GAO's finding that the adjustment made for differences in diagnostic coding patterns between Medicare Advantage plans and traditional Medicare providers was too low for 2011 and 2012 and likely resulted in excess payments to Medicare Advantage plans, Congress has taken steps to increase the adjustment prospectively. The Health Care and Education Reconciliation Act of 2010 required minimum increases in the annual adjustment for coding differences starting in 2014 and required CMS to continue making adjustments in subsequent years until the agency implements risk adjustment based on diagnostic, cost, and use data from Medicare Advantage plans, which is important for helping ensure an accurate payment adjustment for Medicare Advantage diagnostic coding patterns. The American Taxpayer Relief Act of 2012 subsequently increased the statutory minimum for the annual adjustment. Specifically, for 2014, the annual adjustment was required to be not less than the adjustment factor applied | 250 | 2,250 |

Potential Estimated Financial Benefits if 2011-2015 Actions Were Fully Addressed

| Year | Area # | Area | Estimated financial benefit, 2011-2014 (in millions) | Estimated financial benefit, 2015-2023 (in millions) |
|---|---|---|---|---|
| | | for 2010, plus 1.5 percentage points, totaling 4.9 percent in 2014, and to be a minimum of 5.9 percent for 2019 and subsequent years. For 2015, CMS has applied a 5.16 percent adjustment. CBO has estimated that the American Taxpayer Relief Act's amended statutory minimum will save **$2.5 billion over 10 years.** | | |
| **Federal Property** | | | | |
| 2014 | 18 | **Real-Estate Owned Properties**: By calculating the lower rate of losses on troubled mortgages that are resolved without the Federal Housing Administration (FHA) taking ownership of the real estate as compared to those where FHA does take ownership and sells the property through the traditional REO process, GAO determined the agency saved as much as **$1.6 billion** in the 12 months from **July 2013 to June 2014** and **almost $1.2 billion** in the 12 months **from July 2014 to June 2015**. | 1,600 | 1,170 |

Source: GAO.

[a]See Pub. L. No. 113-67, § 601(b), 127 Stat. 1165, 1187 (2013), amending 49 U.S.C. § 44940(c).

[b]In addition, the first $250 million in fees collected each fiscal year are, consistent with existing law, to be deposited in the Aviation Security Capital Fund for use in supporting aviation security-related airport capital improvement projects or for other purposes specified in statute. See 49 U.S.C.§§ 44923(h), 44940(i).

[c]See 49 U.S.C. § 44940(i) (identifying, among other things, the specific amount to be credited as offsetting receipts and deposited in the general fund of the U.S. Treasury each fiscal year, 2014 through 2023).

[d]The Bipartisan Budget Act further revoked TSA's authority to collect the Aviation Security Infrastructure Security Fee, which TSA had been collecting from air carriers pursuant 49 U.S.C. § 44940(a)(2). See Pub. L. No. 113-67, § 601(a), 127 Stat. at 1187.

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