Senate Budget Committee
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Hearing on Bipartisan Proposals for Long Term Fiscal Sustainability

Speaker: Hon. David M. Walker, President and CEO of the Peter G. Peterson Foundation
and Former Comptroller General of the United States (1998-2008)

Chairman Conrad, Ranking Member Gregg and other members of the Senate Budget Committee, it is truly a pleasure to appear before you again, this time in my new capacity as President and CEO of the Peter G. Peterson Foundation. Thank you for the opportunity to appear before you today.

First and foremost, I would like to commend Chairman Conrad and Senator Gregg for their public calls for action to ensure the long-term stability and sustainability of our nation's finances. They are right to be concerned regarding the need to address the federal government's deteriorating financial condition. They are also correct in recognizing that a special process will be necessary to achieve the types of actions needed to put our country on a more prudent and sustainable fiscal path.

We are all well aware of the economic and other non-business cycle challenges that our country has faced during the past fifteen months. During this period the housing bubble burst. We also experienced crises in the financial services sector and an adverse ripple effect on the automotive and other sectors of our economy. As a result, we experienced a serious recession and a significant increase in unemployment and under-employment levels. The federal government took a number actions designed to address these challenges and prevent an even deeper recession or depression.

Given the above, federal deficits and debt levels escalated dramatically in fiscal 2009 to record post World War II levels both in dollar and percentage of GDP terms. Specifically, the fiscal 2009 unified deficit was $1.42 trillion or approximately 9.9 percent of GDP. This was almost nine times the size of the federal deficit just two years ago!

While a large increase in the unified deficit and related debt levels in fiscal 2009 is understandable given the recession and our other major challenges, the federal government did not provide clearly defined objectives, criteria and conditions for the TARP bill and the $787 billion "stimulus bill". Therefore, only time will tell if appropriated funds were applied in an economic, efficient, and effective manner.

We need to learn lessons from these experiences and take steps to do a better job in the future. Even more importantly, we also need to recognize the reality that the U.S. Government's financial condition is worse than advertised and that we face a large and growing fiscal imbalance that is driven primarily by rising health care costs, known demographic trends and a growing gap between projected spending and revenues over time. We faced these conditions before the current recession and recent federal bailouts and assistance programs; however, our situation is worse now and we are closer to reaching a possible "tipping point".

This past weekend total federal debt passed the $12 trillion mark which is almost 85 percent of GDP. Federal debt almost doubled during President George Walker Bush's (43) presidency, and it could double again within the next 10 years unless we change course. Doing so will require elected officials to make tough choices in connection with federal budget policy, social insurance programs, tax policies, health care practices, defense spending and other key areas—choices that may not be popular; but ones that are necessary if we want to avoid a much bigger crisis and ensure that our collective future will be better than our past.

While our escalating deficits and debt levels are a major challenge, they are part of the broader federal financial challenge. Another key challenge is that our nation has become increasingly dependent on foreign lenders to finance our federal deficits. Today, over 50 percent of our nation's public debt is held by foreign lenders and that percentage is growing. Believe it or not, we had virtually no foreign debt at the end of World War II and only 19 percent in 1990. Yes, the truth is that America is being mortgaged and increasingly that mortgage is being held by foreign lenders. That is not in our economic, foreign policy, national security and even domestic tranquility interests over time.

Our federal government also faces a federal financial sink hole that is growing at a rapid rate. At the end of fiscal 2000, the federal government had about $20.4 trillion in total liabilities, commitments and unfunded promises for Social Security and Medicare. That number rose to $56.4 trillion at the end of fiscal 2008—a 176 percent increase in just eight years! While the final numbers won't be in until late 2009, it is likely to be at least $63 trillion due to the record deficit in 2009, growing unfunded promises for Social Security and Medicare, and trillions in additional commitments and contingencies associated with various government bailouts and other assistance efforts. Shockingly, given this number, our total federal financial hole is about $10 trillion more than the current estimated net worth of all Americans and the gap has been growing.

Irrespective of this fact, many in Washington want to grow government even more despite the fact that the federal government has already promised more than it can afford, especially in the area of health care. The truth is that Medicare is already underfunded by over $38 trillion and growing. At the same time, Congress is currently debating making more federal health care promises, without adequately addressing the tens of trillions in unfunded health care promises that we already have.

Let me be clear, we need to ultimately achieve comprehensive health care reform, including some level of universal coverage that is appropriate, affordable and sustainable over time. We should, however, focus first and foremost on gaining control over health care costs or else we risk putting millions more Americans into a health care system that is fundamentally flawed and financially unsustainable over time.

For any health care reform effort to be deemed to be fiscally responsible, it must meet at least four key tests. First, it should pay for itself over 10 years. Second, it should not add to federal deficits past 10 years. Third, it should result in a significant reduction (e.g., 20 percent or more) in the tens of trillions in federal unfunded health care promises that we already have. Finally, it should result in a reduction in the total health care costs as a percentage of the economy as compared to the status quo.

In achieving the above four tests, we must be realistic regarding the assumptions that are used to meet them. Specifically, relying on historically unsuccessful and unsustainable approaches to control provider payments or generate additional revenues may make the numbers work on paper but they are not likely to be sustained over time. Such approaches are also unlikely to pass a "straight face test" in the real world. My extensive travels and participation in town halls and other meetings with many thousands of Americans in 45 states over that past four years have helped me to see firsthand that Americans are tired of creative accounting approaches, unrealistic promises, government bailouts, and partisan bickering.

While we are awaiting the final results of a study that we are funding, it seems pretty clear that the House bill that was passed this weekend does not meet these four tests of fiscal responsibility. It also relies on unrealistic approaches to pay for its proposed expansion of coverage. Health care reform must help improve our nation's financial condition and long-term outlook in order to be prudent and sustainable.

Meeting these four key tests of fiscal responsibility for health care reform is critical but, even if they are met, we will need to do a lot more in order to ensure that this nation has a successful health care system that can be sustained over time. In addition, it is already pretty clear that the current health care reform effort is punting on most of the tough choices that need to be made to really control health care costs. For example, we need to impose a budget for federal health expenditures, we must move away from the current fee for service payment system, we must pursue evidence-based medical approaches, we must address end-of-life issues, we must better target existing tax preferences for employer provided and paid health care, and we must better target taxpayer subsidies under the current voluntary Medicare Part B and D programs.

Irrespective of how the current health care reform debate ends, we must recognize the reality that key factors that contributed to the recent mortgage-related sub-prime crisis also exist in connection with the federal government's own finances. These factors are: first, a disconnect between the parties who benefit from prevailing policies and practices and those who will pay the price and bear the burden for today's fiscal irresponsibility; second, a lack of adequate transparency and public understanding regarding the related risks; third, too much debt, not enough focus on cash flow and an over reliance on current credit ratings; and finally, a failure of existing risk management, regulatory and oversight functions to act until a crisis is at our doorstep.

There are, however, two big differences from the mortgage related sub-prime crisis. First, the numbers and stakes in connection with the federal government's finances are much larger. In addition, no one will "bailout America", we must solve our own problems.

We must take concrete steps to address of this structural fiscal challenge before we face a possible super sub-prime crisis. That could result if foreign lenders lose confidence in our ability to put the federal government's financial house in order. We must recognize that if our foreign lenders lose confidence or if they otherwise decide to significantly reduce their appetite for financing our deficits, we could experience a dramatic decline in the dollar and a dramatic increase in interest rates. This would have a devastating impact on America and Americans. It could also result in a global depression. We must not allow this to happen.

With all of the above as background, let me now move to the primary subject of this hearing—namely, whether the Congress should move to enact a special process to address this nation's large and growing fiscal challenge? My answer to this question is a resounding and unequivocal, YES!

Why do I say this? Because America currently suffers from three societal afflictions—namely: myopia, tunnel vision and self-interest. These factors cause many Americans to focus primarily on today and not enough on what needs to be done to create a better tomorrow. These maladies also affect the work of United States Congress and have grown to epidemic proportions during the past decade or so.

These maladies combined with problems with our current Congressional redistricting process, campaign finance system, special interest lobbying, and a rise in the percentage of members who seek to be "professional politicians", have resulted in our current dysfunctional democracy. One way this is evidenced is by the Congress' unwillingness and/or inability to address large, known and growing challenges that threaten our collective future absent a crisis. Importantly, we must not allow a crisis to occur in connection with our nation's finances because the consequences to our country, American families and the global economy would be severe. We must find a way to act before a crisis occurs.

Clearly, escalating federal deficits and debt levels, combined with our growing dependency on foreign lenders and the deepening federal financial hole represent challenges that must be addressed. Candidly, the American people get it, but the Congress represents a laggard in connection with these critical issues. That must change and soon.

Based on my extensive travels across the U.S. to discuss the issue of federal fiscal responsibility with the American people, it is now abundantly clear that a majority of Americans have grown tired of too much talk and not enough action from Washington in connection with our nation's deteriorating financial condition. Furthermore, The Peter G. Peterson Foundation, which I have the privilege to head, periodically conducts statistically valid public opinion surveys to assess the views of the American people on a range of critical issues facing our nation. Our last survey, conducted in the spring of this year, showed that the number two issue of concern to the American people was our nation's escalating deficit and debt levels. This subject was only exceeded by the need to get the economy on track.

Interestingly, the public was much more concerned with our escalating deficits and debt levels than health care reform, Iraq and Afghanistan, climate change, proliferation of weapons of mass destruction, and other key issues of public concern. Furthermore, by nearly a two to one margin Americans felt that a special commission was needed to help put our financial house in order. In addition, by an almost two to one margin, they also felt that such a commission should include a number of capable and credible non-government experts.

We currently have another survey in the field and expect to receive the results soon. We fully expect that Americans are likely to be even more concerned about our deteriorating financial condition today than the last time we polled on these issues. I will be happy to provide the results of our last survey and the new survey, once it is completed, for the record should the committee so desire.

These growing public concerns were manifested in various protests during the August Congressional recess. In addition, China and other foreign lenders have publicly expressed their concerns regarding the U.S. Government's current fiscal policy and path. They have also taken certain actions to hedge against the possibility of much higher inflation and a much lower dollar once the global economy turns around.

When will Washington recognize the reality that we must act to defuse our ticking fiscal time bomb? And how can we best proceed to address our growing fiscal challenge before a crisis is at our doorstep?

In my view, the Congress and the President should take action in early 2010 once the current health care reform effort has come to a conclusion, or even possibly as part of that reform effort. Specifically, we need to put a process in place that will accomplish two key goals. First, to educate and engage representative groups of the American people on the serious fiscal challenge that we face, the range of tough choices that need to be made, the pros and cons of various options, the prudence of acting sooner rather than later, and the potential consequences to our country and families if we don't do so. This will require the involvement of several respected, non-government professionals who have the ability and the credibility to make the case and engage the public around the country and on the Internet in an independent, objective, fact-based, non-partisan and non-ideological manner. Second, we must also create a process that will set the table and provide the needed political cover for one or more tough votes in Congress. Therefore, the commission should be able to make recommendations in connection with needed statutory budget controls, social insurance programs reforms, tax reforms, defense spending, additional health care reforms, and other appropriate areas.

How can we best accomplish these two key goals? In my view, the best way to do so is by creating a new type of commission. This commission would not be the typical Washington commission. It would be designed to accelerate action rather than to punt the ball down the field once again. To do so, it would need to be created by law, be properly designed, and adequately funded and staffed. Its efforts should also result in a range of recommendations that will be guaranteed a vote in the Congress.

Importantly, everything must be on the table for any commission to be credible and to have a real chance of success. This includes acknowledging the need to modernize the current social insurance programs, constrain federal spending and raise additional revenues. In the final analysis, this special process should be designed to facilitate achieving a significant reduction in the over $60 trillion in federal liabilities and unfunded promises, and to create a climate and momentum to do more over time. This process could also enable achievement of the so-called "grand bargain" that President Obama spoke of in January 2009 in an interview with George Stephanopoulos.

The composition of the Commission is important. For example, such a commission could include twelve members of Congress, including six representatives from each House and from each side of the political aisle, two representatives from the Administration, and six highly qualified non-governmental experts, including two Democrats, two Republicans and two Independents. After all, a significant and growing minority of Americans have become political independents, including myself. These people need to be represented and traditional bipartisan approaches have typically left this important segment of the electorate out in the cold. This should not happen, especially in connection with a commission as significant as this one. Importantly, having some experts who are political independents can also help to enhance the credibility of any "outside the Beltway" and Internet related public education and engagement efforts.

Such a commission should be able to make recommendations either in installments or all at once. For example, the commission could be asked to report in a timelier manner on certain issues where a super majority agreement might be able to be reached more expeditiously (e.g., statutory budget controls that would be imposed after the economy has clearly turned around, Social Security reform). Alternatively, the commission could report its recommendations all at once and as a single package. Importantly, any recommendations supported by a predetermined super-majority of the full commission should be guaranteed hearings and a vote in both houses of the Congress. In addition, while any proposals should be subject to possible amendments, any amendment should be required to be both deficit and debt neutral as compared to the commission's recommendations.

Some have argued that using a commission to address these important issues is the wrong way to go since the Congress should handle these matters through the regular order. This ignores the reality that the regular order is badly broken.

Some argue that the Congress should not turn over so much power to a special commission. However, this argument ignores that fact that, in the final analysis, elected members of Congress and the President must act on any commission recommendations before they can become the law of the land. Therefore, they have the final say as it should be under our constitutional form of government.

I am aware that several legislative proposals have already been introduced in the Congress to create special fiscal commissions. They have varying scopes, compositions, life spans and other features. They all, however, have one thing in common. Each one properly recognizes that the regular order is not likely to generate the type of transformational reforms on the multiple fronts that we need to within a reasonable time frame. This is the cold hard truth and we must act accordingly.

In closing, our current fiscal path is irresponsible, immoral and downright un-American. We are mortgaging the future of our children and grandchildren while reducing relative investments in their future. At the same time, they are facing increasing competition in a global economy.   Yes, our nation is at a critical crossroads. We must take steps to address our large, known and growing fiscal challenge soon. We owe it to our country and to our families to do no less.