PRESIDENT'S FISCAL YEAR 2006 BUDGET WITH OMB DIRECTOR BOLTEN

HEARING

BEFORE THE

COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED NINTH CONGRESS

FIRST SESSION

FEBRUARY 9, 2005

Serial No. 109–2

Printed for the use of the Committee on Ways and Means

U.S. GOVERNMENT PRINTING OFFICE

23–913 WASHINGTON : 2005

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2250 Mail: Stop SSOP, Washington, DC 20402–0001

COMMITTEE ON WAYS AND MEANS

BILL THOMAS, California, *Chairman*

E. CLAY SHAW, JR., Florida
NANCY L. JOHNSON, Connecticut
WALLY HERGER, California
JIM MCCRERY, Louisiana
DAVE CAMP, Michigan
JIM RAMSTAD, Minnesota
JIM NUSSLE, Iowa
SAM JOHNSON, Texas
ROB PORTMAN, Ohio
PHIL ENGLISH, Pennsylvania
J.D. HAYWORTH, Arizona
JERRY WELLER, Illinois
KENNY C. HULSHOF, Missouri
RON LEWIS, Kentucky
MARK FOLEY, Florida
KEVIN BRADY, Texas
THOMAS M. REYNOLDS, New York
PAUL RYAN, Wisconsin
ERIC CANTOR, Virginia
JOHN LINDER, Georgia
BOB BEAUPREZ, Colorado
MELISSA A. HART, Pennsylvania
CHRIS CHOCOLA, Indiana

CHARLES B. RANGEL, New York
FORTNEY PETE STARK, California
SANDER M. LEVIN, Michigan
BENJAMIN L. CARDIN, Maryland
JIM MCDERMOTT, Washington
JOHN LEWIS, Georgia
RICHARD E. NEAL, Massachusetts
MICHAEL R. MCNULTY, New York
WILLIAM J. JEFFERSON, Louisiana
JOHN S. TANNER, Tennessee
XAVIER BECERRA, California
LLOYD DOGGETT, Texas
EARL POMEROY, North Dakota
STEPHANIE TUBBS JONES, Ohio
MIKE THOMPSON, California
JOHN B. LARSON, Connecticut
RAHM EMANUEL, Illinois

Allison H. Giles, *Chief of Staff*
Janice Mays, *Minority Chief Counsel*

Pursuant to clause 2(e)(4) of Rule XI of the Rules of the House, public hearing records of the Committee on Ways and Means are also published in electronic form. **The printed hearing record remains the official version.** Because electronic submissions are used to prepare both printed and electronic versions of the hearing record, the process of converting between various electronic formats may introduce unintentional errors or omissions. Such occurrences are inherent in the current publication process and should diminish as the process is further refined.

CONTENTS

	Page
Advisory of February 2, 2005 announcing the hearing	2
WITNESS	
Office of Management and Budget, Hon. Joshua B. Bolten, Director	5
SUBMISSION FOR THE RECORD	
Embassy of Peru to the United States, Eduardo Ferrero, statement	70

PRESIDENT'S FISCAL YEAR 2006 BUDGET WITH OMB DIRECTOR BOLTEN

WEDNESDAY, FEBRUARY 9, 2005

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
Washington, DC.

The Committee met, pursuant to notice, at 2:06 p.m., in room 1100, Longworth House Office Building, Hon. Bill Thomas (Chairman of the Committee) presiding.

[The advisory announcing the hearing follows:]

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

FOR IMMEDIATE RELEASE
February 02, 2005
No. FC–2

CONTACT: (202) 225–1721

Thomas Announces Hearing on President's Fiscal Year 2006 Budget with OMB Director Bolten

Congressman Bill Thomas (R–CA), Chairman of the Committee on Ways and Means, today announced that the Committee will hold a hearing on President Bush's budget proposals for fiscal year 2006 within the jurisdiction of the Committee on Ways and Means. **The hearing will take place on Wednesday, February 9, 2005, in the main Committee hearing room, 1100 Longworth House Office Building, beginning at 2:00 p.m.**

In view of the limited time available to hear witnesses, oral testimony at this hearing will be from invited witnesses only. The witnesses will be the Honorable Joshua Bolten, Director, Office of Management and Budget. However, any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

BACKGROUND:

Since his reelection to a second term in office, President George W. Bush has outlined several budget and tax proposals. The details of these proposals are expected to be released on February 7, 2005, when the President is scheduled to submit his fiscal year 2006 budget to the Congress.

In announcing the hearing, Chairman Thomas stated, "I look forward to Director Bolten's appearance before the Committee and discussing details of the President's budget and policy initiatives."

FOCUS OF THE HEARING:

Office of Management and Budget Director Bolten will discuss the details of the President's budget proposals that are within the Committee's jurisdiction.

DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

Please Note: Any person(s) and/or organization(s) wishing to submit for the hearing record must follow the appropriate link on the hearing page of the Committee website and complete the informational forms. From the Committee homepage, *http://waysandmeans.house.gov*, select "*109th Congress*" from the menu entitled, "*Hearing Archives*" (*http://waysandmeans.house.gov/Hearings.asp?congress=17*). Select the hearing for which you would like to submit, and click on the link entitled, "*Click here to provide a submission for the record*." Once you have followed the online instructions, completing all informational forms and clicking "submit" on the final page, an email will be sent to the address which you supply confirming your interest in providing a submission for the record. You ***MUST REPLY*** to the email and ***ATTACH*** your submission as a Word or WordPerfect document, in compliance with the formatting requirements listed below, by close of business Wednesday, February 23, 2005. **Finally**, please note that due to the change in House mail policy, the U.S. Capitol Police will refuse sealed-package deliveries to all House Office

Buildings. For questions, or if you encounter technical problems, please call (202) 225–1721.

FORMATTING REQUIREMENTS:

The Committee relies on electronic submissions for printing the official hearing record. As always, submissions will be included in the record according to the discretion of the Committee. The Committee will not alter the content of your submission, but we reserve the right to format it according to our guidelines. Any submission provided to the Committee by a witness, any supplementary materials submitted for the printed record, and any written comments in response to a request for written comments must conform to the guidelines listed below. Any submission or supplementary item not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All submissions and supplementary materials must be provided in Word or WordPerfect format and MUST NOT exceed a total of 10 pages, including attachments. Witnesses and submitters are advised that the Committee relies on electronic submissions for printing the official hearing record.

2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.

3. All submissions must include a list of all clients, persons, and/or organizations on whose behalf the witness appears. A supplemental sheet must accompany each submission listing the name, company, address, telephone and fax numbers of each witness.

The Committee seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202–225–1721 or 202–226–3411 TTD/TTY in advance of the event (four business days notice is requested). Questions with regard to special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

Chairman THOMAS. Good afternoon. Today's hearing is the second in a series examining the President's fiscal year 2006 budget. We are honored to have the Office of Management and Budget (OMB) Director Joshua Bolten once again testifying before our Committee. Thank you for coming and we look forward to your testimony and to your responses to Members' inquiries. The President has presented a budget blueprint that funds the Nation's priorities while reigning discretionary spending and cutting the deficit in half by 2009. It will be difficult work, but it is our responsibility to ensure taxpayer dollars are spent wisely. To that end, Congress must work to eliminate duplicative and ineffective programs while continuing to pursue policies that enhance individual Americans and economic growth. Last year, the economy, as I said yesterday, created 2.2 million jobs, and aftertax income increased nearly 9 percent. Today, the unemployment rate has declined to 5.2 percent. This growth is, I think, to a very great extent directly the result of Republican tax policies. Our strengthened economy has resulted in higher than anticipated Federal revenue, which has helped lower the deficit.

While being mindful of deficits, we must also think about the economy of tomorrow, which, of course, is going to be increasingly competitive and the battlefield will be trade. Currently, we have a government that in many respects was built for the past. The President has provided Congress a rare opportunity to fundamentally examine key elements of our governmental structure, including Social Security and the Tax Code, and we should take this op-

portunity to develop solutions that meet the needs of our aging society and take the opportunity to also address the challenges of the 21st-century economy. Our Nation can emerge stronger and healthier if we approach this assignment responsibly. We can ensure government is prepared to meet its obligations to today's and tomorrow's workers and as they retire. We can produce changes that ensure America is the most attractive place to do business and that each American is treated fairly by a simpler tax system. The opportunity is ours to address crucial changes to government systems that can move America forward. This Committee should be in a place where these great challenges can be discussed and debated in a constructive environment. The Chair hopes that that is where the Committee will be. Prior to recognizing the gentleman from New York, Mr. Rangel, for any comments he may wish to make, the Chair wishes to thank the Members for their willingness to participate in the orderly fashion that we did yesterday which allowed us to be able to have every Member of the Committee an opportunity to inquire of our witness. The Chair hopes that will be possible again today. With that, the gentleman from New York.

Mr. RANGEL. Thank you, Mr. Chairman. I really welcome you to the Committee. After yesterday's hearing, you have no idea how badly we need you to explain how the budget was put together and what is in and what is out, because quite frankly, some of us were unable to follow the explanations given by the Secretary of the U.S. Department of the Treasury. But, since it is your job for the Nation and our job to try to fit into the President's budget what we think is a priority, your presence here is so important. So, during the questioning, I hope that you will be able to explain why a nation at war would not see fit to put into a budget the cost of that war, or in addition, why when the President says that his number one domestic priority is Social Security and every economist says that there are going to be tremendous transitional costs even up to trillions of dollars, why that is not in the budget, and also where there are provisions in the Tax Code to try to make certain that everybody that is wealthy pay a minimum tax and to find out through no fault of their own they get caught up in this complicated Tax Code and pay over $600, $700 billion over 10 years and that relief is not in the tax code. We know that there is an explanation for this, but we have to be able to explain to our constituents what makes this budget so different from a family budget, that if you don't see money for what you want or what you have to get in the budget, that you are not going to get it. So, rather than say the war has ended, that Social Security is dead on arrival, or to forget about it for middle-income voters, we hope you will be able to find the language to help us to have a better understanding of where the compassion is in this budget. Thank you.

Chairman THOMAS. With that, Director Bolten, if you have a written statement, it will be made a part of the record, without objection, and the Committee is anxious to hear from you in any way you see fit for the time you have.

STATEMENT OF THE HONORABLE JOSHUA B. BOLTEN, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

Mr. BOLTEN. I do have a statement, Mr. Chairman, and thank you for your hospitality, Mr. Rangel, other distinguished Members of the Committee. The President's 2006 budget, which was transmitted to this Congress on Monday, meets the priorities of the Nation and builds on the progress of the last 4 years. We are funding our efforts to defend the homeland from attack. We are transforming our military and supporting our troops as they fight and win the global war on terror. We are helping to spread freedom throughout the world. We are promoting the pro-growth policies that have helped to produce millions of new jobs and restore confidence in our economy. Over the past 4 years, the President and Congress rose to meet historic challenges—a collapsing stock market, a recession, the revelation of corporate scandals, and, of course, the attacks of September 11. To meet the economy's significant challenges, in each year of the President's first term, Congress and in particular this Committee and the President enacted major tax relief that fueled recovery, business investment, and job creation. The chart that is on the screen right now shows the strong economic growth unleashed by the tax relief that you enacted. Since the recession year of 2001, economic growth has increased in each of the following 3 years. A primary goal of this 2006 budget is to assure that our economic growth continues.

A strengthening economy produces rising tax revenue. Last year, after declining 3 years in a row, Federal revenue grew by nearly $100 billion. Reflecting strong continued growth, we project that Federal revenues will grow by an even larger figure this year. The President and Congress have also devoted significant resources to rebuild and transform our military and to protect our homeland. In the first term, the defense budget grew by more than a third, the largest increase since the Reagan Administration. To make our homeland safer, the President worked with Congress to create the U.S. Department of Homeland Security and nearly tripled funding for homeland security government-wide. While committing these necessary resources to protecting America, the President and Congress have focused on spending restraint elsewhere in the budget. Working together, we have succeeded in bringing down the rate of growth in non-security discretionary spending each year of the President's first term. In the last budget year of the previous Administration, non-security discretionary spending grew by 15 percent. That is the green bar shown on your screens. In 2005, such spending will rise only about 1 percent, reflected by the small yellow bar at the right of the screen.

Because of this increased spending restraint, deficits are below what they otherwise would have been. In order to sustain our economic expansion, we must exercise even greater spending restraint than in the past. When the Federal government focuses on its priorities and limits the resources it takes from the private sector, the result is a stronger, more productive economy. The President's 2006 budget proposes that enhanced restraint. As you can see from this chart, the 2006 budget proposes a reduction in the non-security discretionary category of the budget. It is reflected in the purple bar right there. This is the first proposed cut in non-security

spending since the Reagan Administration. The budget proposes more than 150 reductions, reforms, and eliminations in non-defense discretionary programs, saving about $20 billion in 2006 alone. As a result of this enhanced restraint, overall discretionary spending, even after significant increases in defense and homeland security, will grow by only about 2.1 percent, less than the projected rate of inflation in 2006 of 2.3 percent. In other words, under the President's 2006 budget, overall discretionary spending will see a reduction in real terms. In addition, the budget also proposes savings from an additional set of reforms in mandatory programs, saving about $137 billion over the next 10 years. As this Committee well knows, both mandatory and discretionary categories of spending are inherently difficult to control, but mandatory programs are especially difficult because of their auto-pilot feature. The Administration looks forward to working with the Congress on a package of mandatory savings.

We will also work with Congress on budget process reforms. Last year, I transmitted to Congress on behalf of the Administration proposed legislation to establish statutory budget enforcement controls. We plan to transmit a similar set of proposals this year. In addition, the Administration proposes other enforcement and budget process reforms, such as the line-item veto, a results commission, and a sunset commission. These reforms will put in place the tools we need to enforce spending restraint and will bring greater accountability an transparency to the budgeting process. This budget restrains spending in a responsible way by focusing on priorities, principles, and performance. We were guided by three major criteria in evaluating programs. First, does the program meet the Nation's priorities? Second, does the program meet the President's principles for the use of taxpayer resources? Is there a real Federal role? Third, does the program produce the intended results? The Bush Administration is comprehensively measuring the effectiveness of the government's programs and the results are helping us make budgeting decisions. As part of the President's management agenda, the Program Assessment Rating Tool (PART) was developed to measure the performance of all Federal programs. Roughly 60 percent of all Federal programs have undergone the PART and those scores figured into our budgeting process.

By holding government spending to these accountability standards, by focusing on priorities, and by maintaining pro-growth economic policies, we are making progress in bringing down the size of the deficit in 2006 and beyond. Last year's budget initially projected a deficit of 4.5 percent of gross domestic product (GDP) in 2004, or $521 billion. The President set out to cut this deficit in half by 2009. Largely because economic growth generated stronger revenues than originally estimated, the 2004 deficit came in $109 billion lower than originally estimated. At 3.6 percent of GDP, the actual 2004 deficit, while still too large, was well within historical range and smaller than the deficits in 9 of the last 25 years. We project the 2005 deficit to come in at 3.5 percent of GDP, or $427 billion. If we maintain the policies of economic growth and spending restraint reflected in the budget, the deficit is expected to decline in 2006 and each of the next 4 years. By 2009, the deficit is projected to be cut by more than half from its originally estimated

2004 peak, to just 1.5 percent of GDP. This is well below the 40-year historical average deficit of 2.3 percent of GDP and lower than the deficit level in all but seven of the last 25 years. The Administration intends to submit shortly a supplemental appropriations request of approximately $81 billion, primarily to support operations in Iraq and Afghanistan for the remainder of the fiscal year. The 2006 budget spending and deficit projections fully reflect the outlay effects of this supplemental request. They also fully reflect the prior $25 billion supplemental bill passed by the previous Congress. However, the budget does not reflect the effect of undetermined but anticipated supplemental requests for ongoing operations in Iraq and Afghanistan beyond 2006.

The published version of the 2006 budget also does not reflect the effects of transition financing associated with the President's proposal to create personal retirement accounts as part of a comprehensive plan to permanently fix Social Security. As the Administration announced last week, the type of personal accounts the President is proposing will require approximately $664 billion in transition financing over the next 10 years with an additional $90 billion in related debt service. This transition financing would result in a deficit in 2009 and 2010 of 1.7 percent of GDP. If I can get the next chart, you will see that reflected on this chart. This is still consistent with the President's goal of cutting the deficit in half by 2009 and still well below the 40-year historical average deficit. It is important to remember that this transition financing does not have the same impact on national savings, and thus on the economy, as does traditional government borrowing. Every dollar the government borrows to fund the transition to personal accounts is fully offset by an increase in savings represented by the accounts themselves. In addition, the transition financing of retirement benefits does not represent new debt to the government. These are obligations that the government already owes in the form of future benefits. Perhaps most important, comprehensive Social Security reform that includes personal accounts can eliminate the system's current $10.4 trillion in unfunded obligations. Those of us who devote our time to thinking about fiscal policy all share a common interest in averting this danger. There is no task as vital to fiscal policy makers this year than removing these unfunded obligations by enacting comprehensive Social Security reform. Confronting these long-term obligations, combined with our near-term deficit reduction efforts, will help assure a strong economy both now and in the future. I look forward to working with the Committee and the full Congress on this budget, which meets the priorities of the Nation in a fiscally responsible way. Thank you very much, Mr. Chairman. I would be happy to take questions.

[The prepared statement of Mr. Bolten follows:]

Statement of The Honorable Joshua B. Bolten, Director, Office of Management and Budget

Chairman Thomas, Ranking Member Rangel, and distinguished members of the Committee, the President's 2006 Budget, which was transmitted to the Congress on Monday, meets the priorities of the Nation and builds on the progress of the last four years.

We are funding our efforts to defend the homeland from attack. We are transforming our military and supporting our troops as they fight and win the Global War on Terror. We are helping to spread freedom throughout the world. We are pro-

moting high standards in our schools, so that our children gain the skills they need to succeed. We are promoting the pro-growth policies that have helped to produce millions of new jobs and restore confidence in our economy.

Over the past four years, the President and Congress rose to meet historic challenges: a collapsing stock market, a recession, the revelation of corporate scandals and, of course, the terrorist attacks of September 11th.

To meet the economy's significant challenges, in each year of the first term, Congress and the President enacted major tax relief that fueled recovery, business investment, and job creation.

Recent economic indicators support the case for tax relief. Since the recession year of 2001, economic growth has increased in each of the following three years. A primary goal of this Budget is to assure that our economic growth continues.

A strengthening economy produces rising tax revenues. Last year, after declining three years in a row, federal revenue grew by nearly $100 billion. Reflecting strong continued growth, we project that federal revenues will grow by an even larger figure this year.

The President and Congress have also devoted significant resources to rebuild and transform our military, and to protect our homeland. In the first term, the defense budget grew by more than a third, the largest increase since the Reagan Administration. To make our homeland safer, he worked with Congress to create the Department of Homeland Security and nearly triple funding for homeland security government-wide.

While committing these necessary resources to protecting America, the President and Congress have focused on spending restraint elsewhere in the Budget. Working together, we have succeeded in bringing down the rate of growth in non-security discretionary spending each year of the President's first term. In the last Budget year of the previous Administration, non-security discretionary spending grew by 15 percent. In 2005, such spending will rise only about 1 percent. Because of this increased spending restraint, deficits are below what they otherwise would have been.

In order to sustain our economic expansion, we must exercise even greater spending restraint than in the past. When the Federal government focuses on its priorities, and limits the resources it takes from the private sector, the result is a stronger, more productive economy.

The President's Budget proposes that enhanced restraint. The 2006 Budget proposes a reduction in the non-security discretionary category of the Budget. This is the first proposed cut in this non-security spending since the Reagan Administration.

The Budget proposes more than 150 reductions, reforms, and eliminations in non-defense discretionary programs, saving about $20 billion in 2006 alone.

As a result of this enhanced restraint, overall discretionary spending, even after significant increases in defense and homeland security, will grow by only 2.1 percent—less than the projected rate of inflation, which is 2.3 percent. In other words, under the President's 2006 Budget, overall discretionary spending will see a reduction in real terms.

In addition, the Budget also proposes savings from an additional set of reforms in mandatory programs, saving about $137 billion over the next 10 years.

As you well know, both mandatory and discretionary categories of spending are inherently difficult to control, but mandatory programs are especially difficult because of their "auto-pilot" feature. The Administration looks forward to working with the Congress on a package of mandatory savings.

We will also work with Congress on budget process reforms. Last year, I transmitted to Congress, on behalf of the Administration, proposed legislation to establish statutory budget enforcement controls. We plan to transmit a similar set of proposed statutory controls to establish caps on discretionary spending, a pay-as-you-go requirement for mandatory spending only, and a new enforcement mechanism to control long-term unfunded obligations. The President's Budget also proposes that Congress include these budget enforcement mechanisms and associated reforms in the FY 2006 Budget resolution.

In addition, the Administration proposes other enforcement and budget process reforms, such as the line-item veto, a Results Commission, and a Sunset Commission. These reforms would put in place the tools we need to enforce spending restraint and would bring greater accountability and transparency to the budgeting process.

This Budget restrains spending in a responsible way by focusing on priorities, principles, and performance. We were guided by three major criteria in evaluating programs:

First: Does the program meet the Nation's priorities? The Budget increases funding to strengthen our Armed Forces, improve the security of our homeland, promote economic opportunity, and foster compassion.

Second: Does the program meet the President's principles for the use of taxpayer resources? If an appropriate Federal role could not be identified in a program's mission, the Budget generally proposes to reduce or eliminate its funding.

Third: Does the program produce the intended results? The Bush Administration is comprehensively measuring the effectiveness of the government's programs—and the results are helping us make budgeting decisions. As a part of the President's Management Agenda, the Program Assessment Rating Tool, or PART, was developed to measure the performance of Federal programs. Roughly 60 percent of all Federal programs have undergone the PART, and those scores figured into the budgeting process.

By holding government spending to these accountability standards, by focusing on our priorities, and by maintaining pro-growth economic policies, we are making progress in bringing down the size of the deficit in 2006 and beyond.

Last year's Budget initially projected a deficit of 4.5 percent of Gross Domestic Product (GDP) in 2004, or $521 billion. The President set out to cut this deficit in half by 2009. Largely because economic growth generated stronger revenues than originally estimated, and because the Congress delivered the spending restraint called for by the President, the 2004 deficit came in $109 billion lower than originally estimated.

At 3.6 percent of GDP, the actual 2004 deficit, while still too large, was well within historical range and smaller than the deficits in nine of the last 25 years.

We project the 2005 deficit to come in at 3.5 percent of GDP or $427 billion. If we maintain the policies of economic growth and spending restraint reflected in this Budget, the deficit is expected to decline in 2006 and each of the next four years. In 2006, we project the budget deficit to fall to 3.0 percent of GDP, or $390 billion. In 2007, the deficit is projected to fall further to 2.3 percent of GDP, or $312 billion.

By 2009, the deficit is projected to be cut by more than half from its originally estimated 2004 peak-to just 1.5 percent of GDP, which is well below the 40-year historical average deficit of 2.3 percent, and lower than the deficit level in all but seven of the last 25 years.

The Administration intends to submit shortly a suppl emental appropriations request of approximately $81 billion, primarily to support operations in Iraq and Afghanistan for the remainder of the fiscal year. The 2006 Budget's spending and deficit projections fully reflect the outlay effects of this supplemental request, as well as the prior $25 billion supplemental bill already enacted by the Congress. However, the Budget does not reflect the effect of undetermined but anticipated supplemental requests for ongoing operations in Iraq and Afghanistan beyond 2005.

The published version of the 2006 Budget also does not reflect the effects of transition financing associated with the President's proposal to create personal retirement accounts as part of a comprehensive plan to permanently fix Social Security. As the Administration announced last week, the type of personal accounts the President is proposing will require approximately $664 billion in transition financing over the next ten years, with an additional $90 billion in related debt service. This transition financing would result in a deficit in 2009 and 2010 of 1.7 percent of GDP, which is still consistent with the president's goal to cut the deficit in half by 2009, and still well below the 40-year historical average.

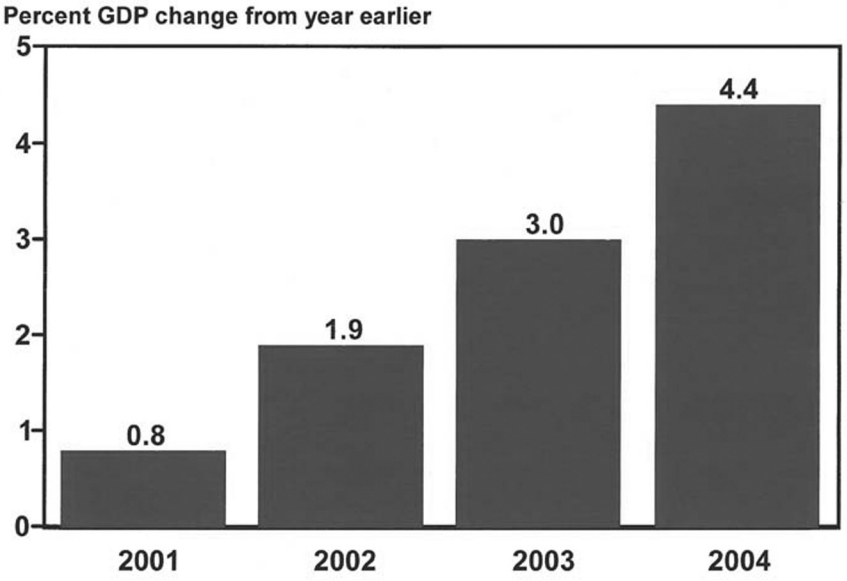
It's important to remember that this transition financing does not have the same impact on national savings, and thus on the economy, as does traditional borrowing. Every dollar the government borrows to fund the transition to personal accounts is fully offset by an increase in savings represented by the accounts themselves. In addition, the transition financing of retirement benefits does not represent new debt-these are obligations that the government already owes in the form of future benefits.

Perhaps most important, comprehensive Social Security reform that includes personal accounts can eliminate the system's current $10.4 trillion in unfunded obligations. Those of us who devote our time to thinking about fiscal policy all share a common interest in averting this danger. There is no task as vital to fiscal policymakers this year than removing those unfunded obligations by enacting comprehensive Social Security reform.

Confronting these long-term obligations, combined with our near-term deficit reduction efforts, will help assure a strong economy both now and in the future.

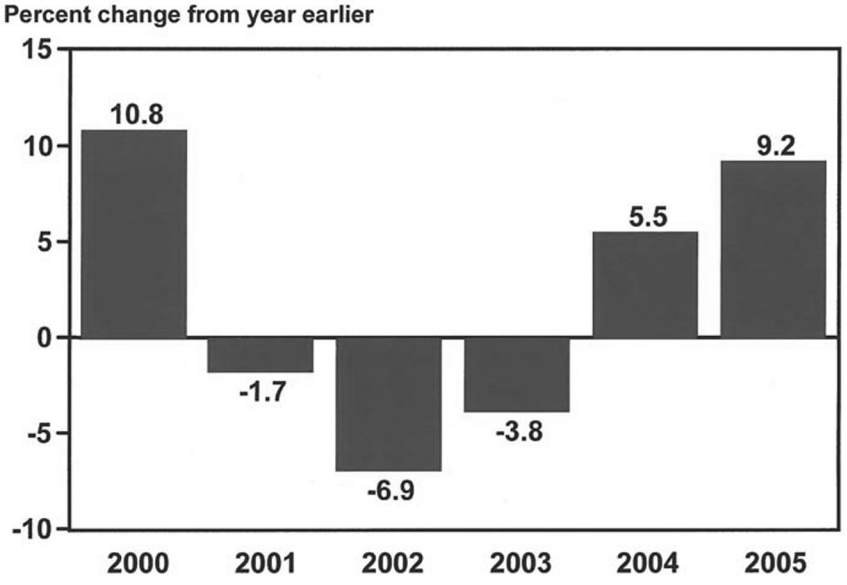
I look forward to working with the committee and Congress on this Budget, which meets the priorities of the Nation in a fiscally responsible way.

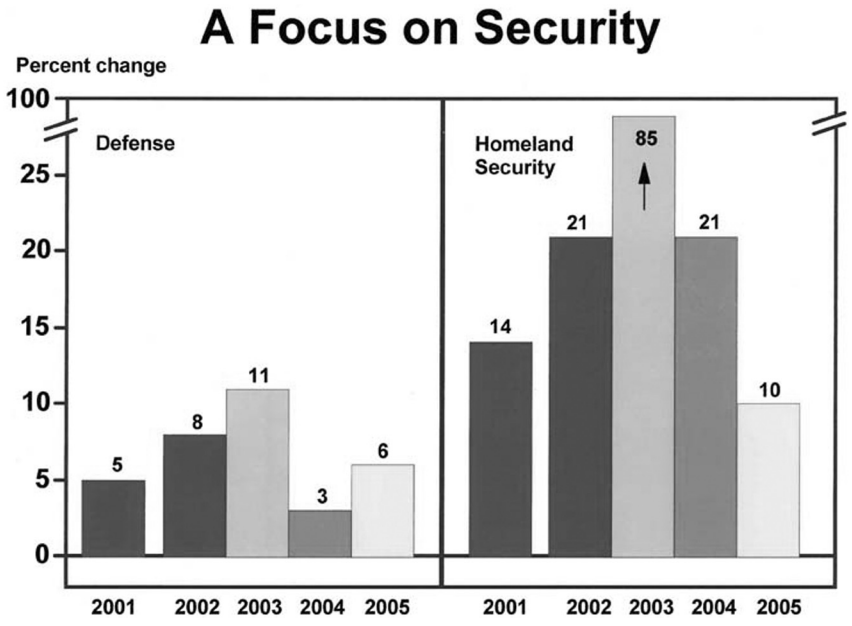
Strong Sustained Economic Growth

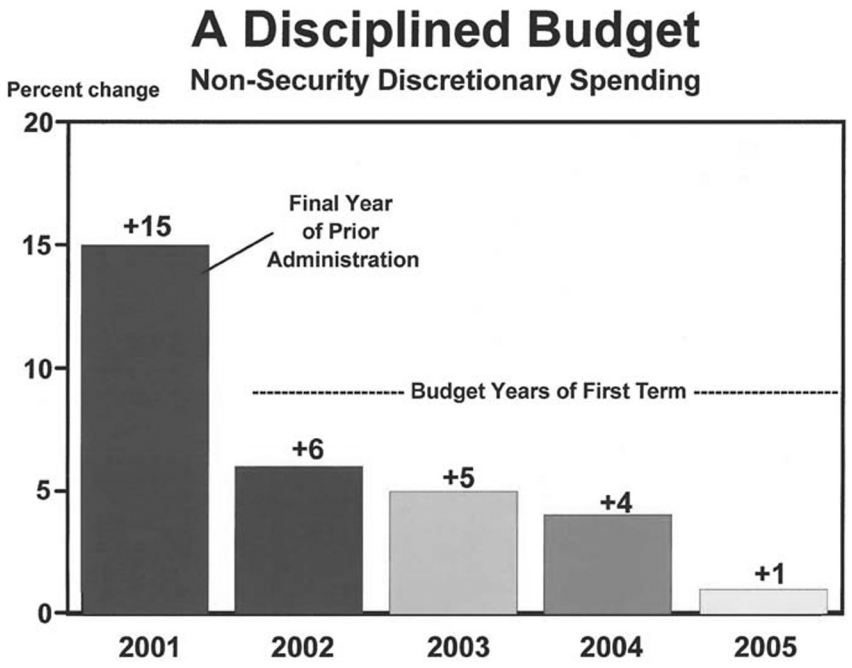


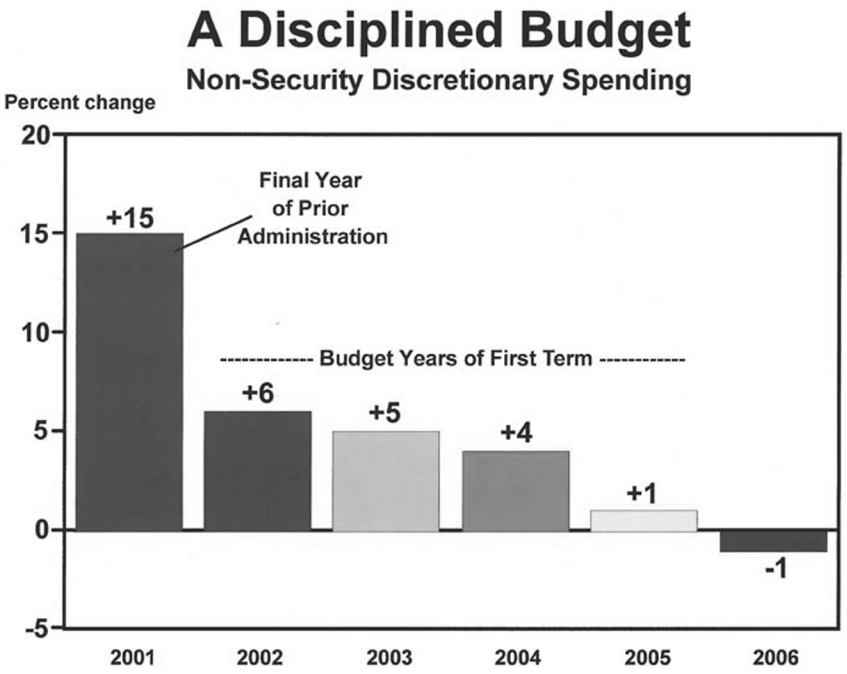
Note: GDP growth for 2004 is an estimate.

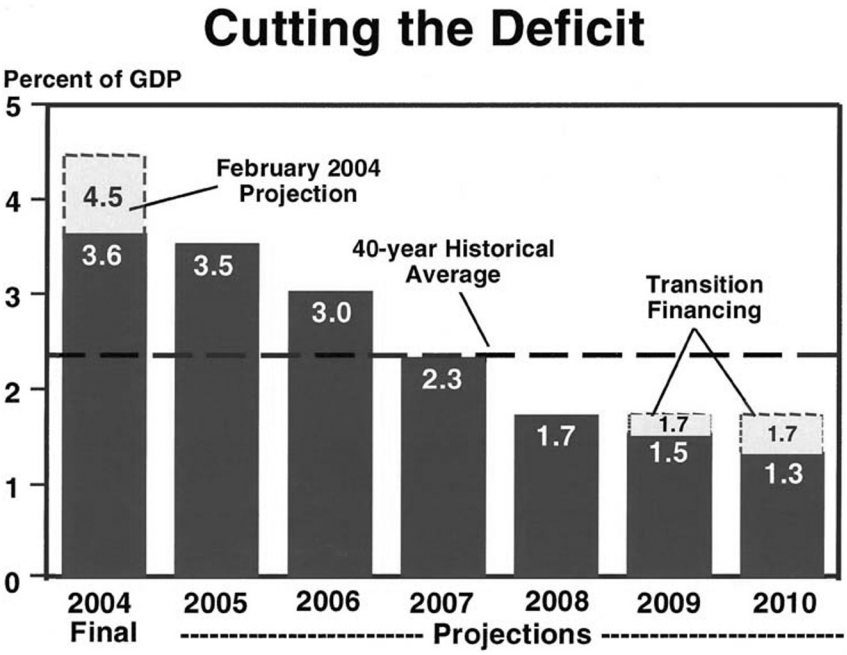
Recovering Economy = Rising Receipts

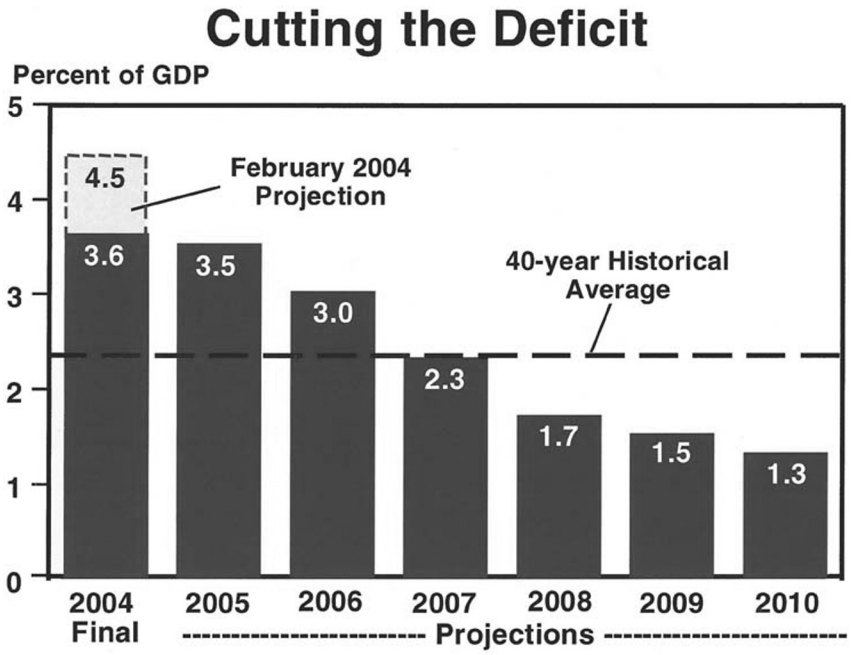



A Focus on Security
Percent change
100
25
20
15
10
5
0
Defense
5
8
11
3
6
2001
2002
2003
2004
2005
Homeland Security
14
21
85
21
10
2001
2002
2003
2004
2005


A Disciplined Budget
Non-Security Discretionary Spending
Percent change
20
15
10
5
0
+15
Final Year of Prior Administration
Budget Years of First Term
+6
+5
+4
+1
2001
2002
2003
2004
2005


A Disciplined Budget
Non-Security Discretionary Spending
Percent change
20
15
10
5
0
-5
+15
Final Year
of Prior
Administration
---------- Budget Years of First Term ----------
+6
+5
+4
+1
-1
2001
2002
2003
2004
2005
2006


Cutting the Deficit
Percent of GDP
5
4
3
2
1
0
4.5
3.6
February 2004
Projection
3.5
3.0
40-year Historical
Average
2.3
1.7
Transition
Financing
1.7
1.5
1.7
1.3
2004
Final
2005
2006
2007
2008
2009
2010
---------- Projections ----------



Chairman THOMAS. Thank you very much. As you might expect, much of the discussion with Secretary Snow was over the President's Social Security provisions. You have touched on them and we will focus questions, as well. The Chair, however, believes that there are some other provisions that if not directly relating to retirement, at least tangentially assist individuals in retirement that are in the President's budget that if I don't ask the question in the way I am asking it, probably will not come up in the course of this hearing. Frankly, the Chair has said in a number of forums that we want to look at an aging society and the question of retirement in a broader way, but clearly, Social Security being one of the key factors. So, if the Director would indicate briefly, and Members will be asking questions that the Director will not be able to fully answer in the timeframe that we have, written responses will be circulated among other Members. So, if you would merely begin to set the tone of getting Members to understand the full impact of the President's focus on retirement and assistance near retirement in the budget, I believe it would be helpful to the discussions.

Mr. BOLTEN. Mr. Chairman, there are a number of provisions in the President's budget that relate to retirement security. We have proposed long-term savings accounts, retirement savings accounts. All of those are reflected in our budget estimates and reflected in the proposals. These are important measures that can be taken to assure that people are able to keep more of their own money and save it responsibly for their retirement. There are a variety of other measures that have already been adopted, in part through your efforts, Mr. Chairman, and this Committee. Health

Savings Accounts are in law. We have proposed enhancements for them through additional tax benefits for Health Savings Accounts to make sure that all of our citizens are able to control more of their own health care and make responsible health decisions on their own. There are a whole variety of other mechanisms in the budget, and you are absolutely right, Mr. Chairman, that don't get much attention but that relate to individual citizens' ability to control their own finances and to control their own retirement in ways that I think are helpful to be brought into the Social Security conversation.

Chairman THOMAS. One of the directions that I hope the debate takes at various times is that as we are looking for ways of addressing health care, both in terms of an immediate or acute need or chronic and long-term, that as we try to stress within the premier government program for seniors, Medicare, it is something that shouldn't be initiated at retirement, and that is preventive and wellness. Without a health program, either through a health savings account or assistance with small employers through new structures that I believe are also in the budget, it is very difficult for individuals to begin to prepare a lifelong health relationship which, in fact, would significantly enhance retirement, as well. We won't go into those details. But, if you begin to look at the budget in that fashion there are a number of areas that coordinate together that we hopefully believe will produce an aging society that will age even older, but in a comfort level heretofore unseen with the finances necessary to have that comfortable retirement. The Chair would indicate to the Members that the Chair intends to follow the Gibbons' Rule. Most of you would be familiar with that. Some of the freshmen would not. The former Member from Florida initiated a procedure in which the order that the Chair would call on Members to question witnesses was based on who was present at the fall of the gavel. I can't believe it was designed to encourage attendance. However, there is a secondary effect in which it actually does. As I go down the list of names, if you weren't called when it should have been called, in your opinion, from a seniority point of view, it is because I am following the Gibbons' Rule, and almost always the Committee will function by the Gibbons' Rule and that is if you were here when the gavel fell, you will be called in order of seniority. With that, the Chair would——

Mr. BECERRA. Mr. Chairman, is that something that was articulated by you prior to the commencement of——

Chairman THOMAS. It has been the rule for every Congress that has been announced and utilized. I almost want to say decades, but I don't want to claim the gentleman from New York and I are that old. At least for the last several Congresses that we can remember. The gentleman recognizes the gentleman from New York.

Mr. MCDERMOTT. Mr. Chairman, may I ask a question?

Chairman THOMAS. Certainly.

Mr. MCDERMOTT. Would it not be fair to say that the next hearing, you would start with that rule, and then go by seniority today, since it was not—you didn't expressly state that prior——

Chairman THOMAS. The Chair would have assumed the senior Member would have dealt with that, knowing that that is the way the Committee has proceeded both under Democratic Chairs and

Republican Chairs. However, to move forward in a reasonable fashion in which the Chair hopes those Members of the Committee who were anticipating being called on sooner than would otherwise have been the case need to focus on the gentleman from Washington as the one responsible for that not occurring. The Chair is willing to say that for this hearing, we will not follow the Gibbons' Rule, notwithstanding the fact Members were here and ready at the time the gavel fell. So, with the understanding that if the sky falls, it is on the gentleman from Washington, Mr. McDermott——

[Laughter.]

Mr. RANGEL. It sounds like it is Gibbons.

Mr. MCDERMOTT. I am going to put my hands up over my head.

Mr. RANGEL. Okay.

Chairman THOMAS. The Chair would indicate that is one place they could be.

[Laughter.]

The gentleman from New York.

Mr. RANGEL. Thank you, Mr. Chairman, and thank you again, Mr. Director. Now, would you say that elimination of these entitlements will make your budget problems a lot easier? Are entitlements good for budgets or bad, entitlements, Medicare, Social Security——

Mr. BOLTEN. I am sorry, Mr. Rangel. I didn't follow the question.

Mr. RANGEL. Do you believe that the elimination of entitlements would have a positive effect on our budget if we just didn't have the Social Security entitlement, the Medicare——

Mr. BOLTEN. The elimination——

Mr. RANGEL. Just, yes, to have it done by the private sector. Would it help?

Mr. BOLTEN. I am not sure what you mean by the elimination of the entitlements. What I can tell you is that the——

Mr. RANGEL. I mean wipe them out, eliminate, gone. Private sector. Let the free market work its will. Wall Street. Prescription—that is what I mean.

Mr. BOLTEN. Entitlements are, by far, the biggest fiscal challenge this country faces.

Mr. RANGEL. You would——

Mr. BOLTEN. It is the unfunded liabilities that—I am sorry.

Mr. RANGEL. You would like to get rid of these big fiscal challenges, wouldn't you?

Mr. BOLTEN. I would like to get rid of the unfunded liabilities in the entitlements, certainly.

Mr. RANGEL. Okay.

Mr. BOLTEN. Not the programs themselves.

Mr. RANGEL. You have to be better than yesterday, but you are getting close already. Now, if, indeed, the Social Security program was one of—you have got some dramatic language here, biggest saving yet. Anyway, it is a big deal. There is no task as vital to fiscal policy makers this year than removing those unfunded obligations by enacting comprehensive Social Security reform. Now, how do you expect Americans to believe that this is so important when for whatever reason, nothing is included in the budget? You

would have to be the first to admit that no matter what the President gives us, it is going to have fiscal implications, is that not correct, of hundreds of billions of dollars if not trillions of dollars, and yet not one mention is in the budget that is presented to us. Is that true?

Mr. BOLTEN. There are fiscal implications, Mr. Rangel, and they are reflected in the last chart that I had up in my presentation, which——

Mr. RANGEL. Sir——

Mr. BOLTEN. I will put it back on the screen——

Mr. RANGEL. Sir, we are not going to vote on your chart. I am talking about a budget. Will you submit something—submit it in writing. Social Security—is there a dollar next to the cost of this dramatic change in Social Security? Is the dollar amount there at all? I thought you said it was not.

Mr. BOLTEN. It is not reflected in the prepared documents that you have.

Mr. RANGEL. That is all I am asking. I would assume, then, that it doesn't appear to be as serious as you said if dollars are not there. The other thing that I am concerned about is the Alternative Minimum Tax (AMT). Would you admit that the middle-income taxpayer has gotten caught into this, people that you and I and the President want to have relief, and the President has said that over and over?

Mr. BOLTEN. Sure. The AMT is a——

Mr. RANGEL. Very important.

Mr. BOLTEN. A very complex mechanism for collecting taxes.

Mr. RANGEL. Yet you know that it costs. There is going to be a cost to that, right? We are going to have to borrow money in order to give this relief, is that correct?

Mr. BOLTEN. What the President has called for is fundamental tax reform and we believe that the AMT can be reformed in the context of overall revenue-neutral fundamental tax reform.

Mr. RANGEL. Oh, so it won't cost anything?

Mr. BOLTEN. In the context of fundamental tax reform, we believe it can be done in a revenue-neutral fashion.

Mr. RANGEL. You are saying that we, over 10 years, can find $700 billion to provide this relief for the American people without any lost revenue, to make it revenue neutral?

Mr. BOLTEN. I think in fundamental tax reform——

Mr. RANGEL. That is good by me.

Mr. BOLTEN. That can all be done.

Mr. RANGEL. We are moving, then. This is better than yesterday. Now, how about the war? I cannot find anyplace in this budget where anyone is making any sacrifice except our brave fighting men and women and veterans. The war has to cost money and sooner or later, we will be asked to vote on the cost of the war. Some people think the whole thing is going to cost $400 billion. Is there anything, any page in the budget that you are presenting to the Congress where we can find out what the President or you will be asking us to fund? Is the war cost in the budget?

Mr. BOLTEN. The costs for 2005 are included in the budget figures that are contained in these volumes. They are also included in the charts I just presented. That supplemental request has not

come forward yet to the Congress. It will be coming forward shortly. It is $81 billion.

Mr. RANGEL. Okay. Now, in a normal family household——

Mr. BOLTEN. Mr. Rangel, it is reflected in the documents here.

Mr. RANGEL. If you are going to ask for something, normally, it is in the budget. Here, the war cost is not in the budget.

Mr. BOLTEN. I think, Mr. Rangel, what I was just trying to say is that the $81 billion that the Administration will be requesting shortly is reflected in the budget numbers that are contained in the documents before you and in the charts I just showed you.

Mr. RANGEL. Okay. I am running out of time. You would agree that we need to have this done in a bipartisan way, Republicans and Democrats?

Mr. BOLTEN. I would hope so, sir.

Mr. RANGEL. Are you included in the formulation of the Social Security plan that we have not received but the President has?

Mr. BOLTEN. Am I a part——

Mr. RANGEL. Yes.

Mr. BOLTEN. You mean, am I a participant in the internal policy debate?

Mr. RANGEL. Yes.

Mr. BOLTEN. Not the principal one, but I am one of the participants.

Mr. RANGEL. Do you know of any alive Democrat in the House or the Senate that is working with you and the President on this issue?

Mr. BOLTEN. Mr. Rangel, I am sure there are many Democrats in both Houses that are prepared to work with the Administration. The Administration is certainly prepared to work with you or anybody else that is interested in fundamental Social Security reform.

Mr. RANGEL. But, you don't know of anyone now? Thank you.

Mr. BOLTEN. That is not my role, sir.

Mr. RANGEL. I understand.

Chairman THOMAS. The Chair believes the gentleman from New York did not intend to imply that there were other than alive Democrats in the House and the Senate.

[Laughter.]

Mr. RANGEL. No, I am talking about Pat Moynihan. Pat Moynihan is a great American, a great Senator——

Chairman THOMAS. I understand that.

Mr. RANGEL. Obviously he has worked very closely with the President, however the President communicates with him. But, it doesn't help us in the bipartisanship.

Chairman THOMAS. The record will reflect that the gentleman from New York said, does he know any live Democrats in the House or the Senate.

Mr. RANGEL. As opposed to dead ones.

[Laughter.]

Chairman THOMAS. But, the Chair is trying to indicate we don't believe there are any dead Democrats in the House or the Senate.

Mr. RANGEL. I thought the President——

Chairman THOMAS. We believe they are all alive.

Mr. RANGEL. Thought that Pat Moynihan was still in the Senate.

Chairman THOMAS. Boy, the current Senators from New York would be interested in learning that one.

Mr. RANGEL. I yield.

Chairman THOMAS. Does the gentleman from Florida wish to inquire?

Mr. SHAW. Yes. I am reminded of the old-time Louisiana politics, where if you put in Huey Long, it says when he dies, if he dies, he would like to be buried in Southern Louisiana so he can stay active in politics.

[Laughter.]

That was Louisiana. In New York, they keep voting, I am sure. I am not positive of that.

Mr. MCCRERY. I am from North Louisiana.

[Laughter.]

Mr. SHAW. Reclaiming my time, I would like to continue this discussion that you are having with Mr. Rangel regarding the input from Democrats. As I pointed out yesterday to Secretary John Snow, the President certainly did put out the invitation. He said he wants to work with all the Members of Congress. Any idea that comes in with regard to saving Social Security is tremendously important. As to date, I asked the Secretary, I said, what Democrat have you been able to work with, and he could come up with Alan Boyd and that was the only name that he could come up with. So, I would like to tell my friend from New York that the door is open to all, you, Mr. Levin, anybody on this Committee, as well as anyone on our side of the aisle and your side of the aisle in the U.S. Congress.

Mr. RANGEL. If the gentleman would yield——

Mr. SHAW. We are looking for good ideas. I will yield briefly.

Mr. RANGEL. I met with the President on this and the President told me and a number of other people that what he wanted us to do is to wait until he got his Social Security plan together. Now, we Democrats want to be cooperative, but we can't until we find out what he and the Republicans are going to bring to us.

Mr. SHAW. Reclaiming my time——

Mr. RANGEL. We are anxious to work with you.

Mr. SHAW. Reclaiming my time, for the last 6 years that I was Chairman of the Subcommittee on Social Security, I was looking and reaching out and asking for ideas from your side that never came. The only thing that came was criticism. Mr. Bolten, I appreciate your mentioning something that we hear too seldom up here, and that is talking about the unfunded liability to today's workers tomorrow for their retirement benefits because that doesn't show up in our budget and that we are on a cash basis here in this country. I think we should start looking more toward capital budgeting in many areas that we can start reflecting the obligations that we are piling up on tomorrow's generation, and if we were to do that, I think perhaps we might be more responsible. I think we should start thinking about going down a dual—two roads, one with the accrual type of accounting as businesses do and the other cash, which is traditional to municipal accounting. I think this would be very, very helpful to a lot of us, not only on how we spend the money, whether we lease buildings whether buy buildings or build buildings, and a lot of the decisions that we make seem to be

skewed with the archaic budget process that we have. Have you looked into anything like that, of going toward capital budgeting or what we should do as to the disclosure of unfunded liabilities, which has been going on from the first day of our country?

Mr. BOLTEN. We have looked at some things, but I have to agree with you, Mr. Shaw, that one of the big surprises I had when I took over this job a year and a half ago was the extent to which we are bound by the accounting conventions on which government operates and how that tends to, I think, distort good decision-making. I think a move toward capital budgeting would be very helpful. We have a couple of proposals in this budget to try to make sure that we are not expanding unfunded liabilities outside the budget window because that is—when we operate outside the 5-year, or it used to be 10-year, budget window, you can do things that escape the notice of congressional rules. But, we have proposed some things in the budget that would try to capture the outside the budget window unfunded liabilities, as well, and prevent those from growing at the same time.

Mr. SHAW. I would like to follow up on another thing Mr. Rangel was discussing with you, and that is the question of the AMT. It is a growing problem. Of course, the size of the problem, and it continues to grow, makes it very difficult for us to find the revenue in which to put that it. It is a dinosaur. It should be done away with. Charlie threw out the figure of $700 billion. I think he is about right on that. But, it is going to be very difficult to find the revenue or the adjustments. I know I had the Joint Committee on Taxation do a study for me last year in which it was looking at the various brackets, how much would you have to raise in the bracket to make up the revenue that was lost within that particular bracket, and I was astounded by the figure that came up or the percentage that we would have to adjust the tax rate. Thank you, Mr. Chairman. I yield back.

Chairman THOMAS. I thank the gentleman. Does the gentlewoman from Connecticut wish to inquire?

Mrs. JOHNSON. Thank you very much. Welcome, Mr. Bolten. First of all, let me congratulate you on including in what must be in these days a very tight budget about $125 billion to help us address the problem of the uninsured. Indeed, the system is beginning to be unworkable because not everyone has equal access to affordable health insurance. I congratulate you on protecting that interest that the President has long stood by and was eloquent in defense of during the campaign and we intend to present you with very good ideas about how to carry through on his commitment.

Mr. BOLTEN. Congresswoman, we have had a chance to talk about that, I know, in person and I know how strongly you feel about it. We are glad of your interest in the President's proposals for tax credits and other elements for the uninsured and look forward to working with you.

Mrs. JOHNSON. Thank you. I also want to say that I am very, very proud of the fact that we experienced in 2004 a 4.4-percent growth in our GDP, that the last 3 months have seen the fastest growth in small business income, the fastest rise in that income over the past 10 years, that aftertax income rose 8.9 percent. I could go on, but your leadership, this President's leadership and

the Administration's leadership has given the economy greater strength. One area in which you have done that is in the health services area, where as a result of the leadership of the President and Secretary Thompson, with the close collaboration, I will have to say, of the House and Senate, we have put in place resources that will, for the first time, enable us to restructure delivery of health care services to improve quality and control costs. My question to you is, in your estimates of the cost of Medicare, did you anywhere take into account the impact of technology in reducing the cost of medical errors, the impact of disease management, and the extraordinary capability it gives us to control health care costs? Just Pacific Care saved $244 million on disease management, implementing disease management for its Medicare beneficiaries. McKesson saved $3,089 per person annually through disease management, reduced emergency room visits 61 percent, reduced hospitalization 66 percent. We have embedded now in Medicare and through what Dr. Brailler is doing and the administration is doing, are working to embed throughout the health care delivery system of America both the technology and most advanced medical knowledge to both improve quality and reduce cost. Is any of that reflected in your estimates?

Mr. BOLTEN. Congresswoman, I can't speak for the Medicare actuaries of the U.S. Department of Health and Human Services who have responsibility for doing the estimates, but I do have a strong conviction that whatever estimates we have used have not adequately taken account of the kinds of innovations you are talking about. Those are extremely important. Our fiscal crisis is really just a reflection of a broader health care financing problem in this country, and one of the best ways that we can get a hold of it is through the advancing use of technology that you are so interested in, health information technology that you worked with Dr. Brailler on. I think that we are amply funding those initiatives in this budget and we are anxious to work with you to make sure we promote those initiatives because that really is one of the key answers to bringing health care costs under control in this country.

Mrs. JOHNSON. I thank you for in your supplemental for reprogramming the money to Dr. Brailler's office. It is terribly, terribly important. But, the answer to my question is, no, neither your actuaries nor the Congressional Budget Office's (CBO's) actuaries are taking one penny of these reductions into account and they are simply of extraordinary dimensions. I thank you for sticking by them and making sure that we will have the resources to do what the American people need as well as what Medicare recipients need, which is to have access to high-quality health care at an affordable dollar. Thanks.

Chairman THOMAS. Would the gentlewoman yield briefly with the remaining time?

Mrs. JOHNSON. Yes.

Chairman THOMAS. I would tell the gentleman, I was pleased to see the President has made a very strong statement on electronic medical recordkeeping. He has almost 4 years left on his second term. The disappointing point of reading that section was that he hopes that he could achieve this by 2014. Our goal will be to hopefully have each of the next 4 years multiplied by two or pos-

sibly three so that we can accomplish this in a much faster time. That is, I think, the basis for a significant change in everything that the gentlewoman was discussing. That would be a terrific improvement. Does the gentleman from California wish to inquire?

Mr. STARK. Yes. Thank you, Mr. Chairman. I would like to deal with issues here that deal with credibility of the information that we in the Congress receive from the Administration, and I think it is important because we are asking a lot of American people to rely on the information, particularly empirical information. When you cannot depend on the accuracy or the integrity of that information—just a few minutes ago, Mr. Bolten told Mr. Rangel that the budget did include the war costs, but his testimony, whoever wrote his testimony forgot to point this out, but you said in your testimony, Mr. Bolten, that the budget does not reflect the effect of undetermined but anticipated supplemental requests for ongoing operations in Iraq and Afghanistan beyond 2005. Now, I want to talk about Medicare and the drug benefit because I just recall that back in February of 2003, at the budget hearing, Chairman Nussle asked Secretary Thompson whether his proposal would cost no more than $400 billion over the 10-year period. Secretary Thompson said, "That is correct," and the giant share of it is the prescription drugs. Then in our own club here, Chairman Thomas and the debate on June 27 said that the program stays within the reasonable bounds of the $400 billion that we are proposing, and my colleague, Mr. Shaw, said we are putting, in that same debate, $400 billion into Medicare. Chairman Nussle said we are increasing Medicare by $400 billion. It goes on. Congresswoman Johnson said that we are going to strengthen Medicare with a $400 billion plan that adds prescription drugs and preventive chronic care benefits. That was in the press release on February 3. Congressman Dreier from California said the program scores at $395 billion—he was more accurate—which is within the budget.

Now, we all know that those numbers were subject to change and there was a $534 billion number that the OMB was working with and they had it all along. They never mentioned it to anybody during the debate, but they knew that it was $534 billion, according to their experts, not $395 billion. They probably also knew that the bill might have failed if they let that information out of the box. I wouldn't suggest for a minute that my good friends on the other side of the aisle were lying, but I would suggest that they are awfully gullible if they keep believing the budget projections that the Administration brings to us, and that embarrasses all of us, not just one side of the aisle or the other, because if we don't have proper information and decent numbers that we can rely on, we are apt to make mistakes. If we can't rely, for instance, on the Social Security numbers, which aren't in the budget, we may ruin Social Security just the way we started to ruin Medicare in the Medicare bill. What we are really doing is giving a blank check from the Treasury to the pharmaceutical companies and insurance plans, and so we built up special interests at the expense of the beneficiaries and taxpayers, and that is an expensive way to deliver a lousy benefit, which it is, much less than a good benefit. When you break the market into small chunks and use private plans with higher overhead than Medicare and you prohibit specifically the

Secretary from negotiating a better price, you have just given the key to the Treasury to the pharmaceutical industry, and that is what we did, being reassured time after time after time by the OMB, by the Administration, by the CBO, that it was only going to cost $400 billion. Well, guess what, yesterday we learned that hidden in Mr. Bolten's budget—hidden, mind you—was the number of $913 billion. It is just a projection of the $534 billion, but he never mentioned the $534 billion before. So, now the $534 billion just creeps into the OMB budget and you have projected out to $913 billion and they have got some cockamamie way to bring it down to $720 billion, which CBO says they can't do in theirs. I guess the question is, ladies and gentlemen, how can we trust you, the Administration, on Social Security when you have got such a bad record of hiding the truth on Medicare?

Chairman THOMAS. The time of the gentleman has expired and the Chair would indicate that that response is probably one that would be appropriate as a written response. However, the Chair recognizes the gentleman from——

Mr. STARK. I have one for the record, Mr. Chairman. I would submit it. I anticipated——

Chairman THOMAS. Without objection, the gentleman has a question for the record.

Mr. STARK. Thank you very much.

Chairman THOMAS. The gentleman from California is recognized.

Mr. HERGER. I thank the gentleman.

Chairman THOMAS. Would the gentleman from California yield to the Chair?

Mr. HERGER. I will.

Chairman THOMAS. I thank the gentleman for yielding. The Chair wishes to place in the record a letter from the CBO dated February 9, 2005. It says, "Dear Mr. Chairman, as per your request, this letter discusses the Congressional Budget Office's current projection of spending for the Medicare Part D benefit. That estimate, which was published in the January 2005 Budget and Economic Outlook, is nearly identical to the cost estimate for Part D that we prepared in 2003." As far as the CBO is concerned, those numbers are virtually the same. As far as the numbers that you utilized in terms of the Administration's position, the Chair would ask unanimous consent to place in the record two documents of this Committee's creation based upon numbers that are in the President's budget. I will briefly go over them and then I would ask Director Bolten to briefly respond as to their accuracy and what they really mean. The Chair is very grateful to the gentleman from California for the time.

On this sheet, it says, cost projections for the Medicare drug benefit from 2006 to 2015. If you will recall, the last budget was over the previous 10-year period. That is, you pick up last year and you eliminate the out year of 2015 to 2014. The drug program in the Medicare Program had a 2-year ramp-up. It is extremely complicated, difficult. So, last year, the first year, was zero, in essence, zero cost. Then you added a last year, which is now a full benefit cost. What is missing from the $1.191 trillion figure, which is the gross spending, is apparently the failure on the part of our col-

leagues to remember that this is a voluntary program in which people choose to sign up, and if so, are subject to beneficiary premiums, unless, of course, they are low-income. That is anticipated over the same period of time to bring in $145 billion of revenue, which you then subtract from the gross spending. We also for the first time elevated seniors as seniors first and low-income second, as opposed to the historical pattern of the former majority, and that instead of having uneven treatment of seniors at the State level through the Medicaid program, we now have a uniform senior program that will, in fact, provide us with $134 billion of State Medicaid payback for the Federal assumption of that. Since Medicaid is a matching 50 cents or a dollar program between the Federal government and the State program, we have a Federal Medicaid savings of $188 billion from which you subtract from the $1.191 trillion. That provides the net spending drug benefit of $724 million that the gentleman referred to.

To really compare apples to apples, you then have to examine the effect of 2 years of the budget window of a fully functioning program that wasn't in the previous 10-year period. I am sure the gentleman didn't intend to assume that 2 years at zero would be compared to 10 years at full cost. If you subtract that figure, which is $206 billion, you wind up with a figure of net spending over the 2004–2013 period of $518 billion, virtually identical to the $511 billion that had been stated by the Administration last year. The point being, these are the Administration's figures, which always had different assumptions which produced the differing numbers between the CBO and the Office of the Director of OMB. If you did the same thing to the CBO numbers, which the CBO has not yet done but will do for us in March, I think you will find they will have the same discrepancy window, very close to $400 billion. The point is, the exercise takes you nowhere, notwithstanding headlines that seem quite interesting and anticipatory of a major coup on the part of my colleagues on the other side of the aisle. The numbers are the same if you do the math fairly and accurately. I apologize to the Director. Maybe another Member will give him additional time to respond, and the Chairman thanks the gentleman from California for his courtesies and will find ways to make it up to him. The Chair would then recognize the gentleman from Michigan, Mr. Levin, if he wishes to inquire.

Mr. LEVIN. Welcome. Why aren't the Social Security costs of the proposed private account plan in the budget?

Mr. BOLTEN. The President's proposals are still in the formulation process. He has announced some portion of it, the early years of a private account, which he announced last week. That was announced after the budget was put to bed. Because he has announced those, I did include those in my comments and in the charts I put before you just now. So, we can now show you at least the short-run deficit effect of the President's proposals for private accounts.

Mr. LEVIN. Those should be—you amended the chart, and by the way, the Secretary yesterday was unaware that you were going to amend your chart from 1.5 to 1.7, because it is not in the chart that is in the budget book, right? You have since amended the chart?

Mr. BOLTEN. That is correct.

Mr. LEVIN. Okay. So, to be truthful about budgeting, surely the first year costs should be added to the deficit, right?

Mr. BOLTEN. If the President's plans were adopted, and I think we have to wait and see what the full plan is, but what I wanted to reflect here was the short-term deficit effect of the creation of personal accounts. These would be the accurate numbers from what we know now. It would be a 1.7 percent deficit——

Mr. LEVIN. That should be reflected in the budget. What is that number for the first year that it would be operative, do you know?

Mr. BOLTEN. You mean the cost of personal accounts in the——

Mr. LEVIN. The $740 billion over 10. What is the first——

Mr. BOLTEN. It ramps up. My recollection is about $23 billion in 2009, about $56 in 2010.

Mr. LEVIN. Then it goes up the last years to what?

Mr. BOLTEN. I don't have those numbers.

Mr. LEVIN. According to——

Mr. BOLTEN. We can provide that to you, and I think they were actually on sheets of presentation when the President made the announcement about his Social Security—the short-term elements of it.

Mr. LEVIN. Yes, because according to the Social Security Administration (SSA), it goes up—this is on a calendar basis—$34 billion, and then in the two, four, six, seventh year, $176 billion, and then if you add, in increased costs, we are talking about $1 trillion $400 billion the first 10 years of the plan. I think if we are going to be honest, and you are going to be honest about budgets, you should include those figures, surely those that are within your budget window. You should revise not only your chart, you should revise the budget.

Mr. BOLTEN. Mr. Levin, we will be glad to provide you revised charts when——

Mr. LEVIN. How about a revised budget?

Mr. BOLTEN. I think that all that would need to be reflected is the costs in the out years. I think that would provide——

Mr. LEVIN. Why don't you send us a letter saying the dollar figure that should be added.

Mr. BOLTEN. I would be glad to do that when the President's plan is fully formulated.

[The information follows:]

Mr. LEVIN. Well, look, it isn't formulated fully by any means, but that part of it has been discussed by the White House, by some unnamed official. I take it that wasn't you.

Mr. BOLTEN. No.

Mr. LEVIN. Look on the last part of your testimony, if you would, where you say comprehensive Social Security reform—I question that word—that includes personal accounts, private accounts, can eliminate the system's current $10.4 trillion in unfunded obligations. By the way, that $10.4 trillion is based on infinity. Let me ask you this point blank. Do the private accounts, by themselves, would they do anything to reduce the shortfall projected for 2042 or 2052?

Mr. BOLTEN. In and of themselves, the personal accounts do not solve the solvency problem——

Mr. LEVIN. It does not solve it. Does it reduce the solvency—what is called insolvency—one dollar?

Mr. BOLTEN. If they are part of—I believe they are an integral part of a comprehensive plan.

Mr. LEVIN. No, no, no. Why don't you want to answer, no? Why do you then talk about integralness? When you are asked a straightforward question, would the private accounts by themselves address the shortfall projected for 2042 and 2052, is the answer yes or no?

Mr. BOLTEN. Personal accounts in and of themselves don't address the solvency issue, but they are part of a comprehensive plan that does address the solvency issue.

Mr. LEVIN. I know you have been told to put another clause on, but if you put a period before "but," the answer is no, right?

Mr. BOLTEN. Mr. Levin, we wouldn't be proposing the personal accounts in the absence of a comprehensive plan, so I don't—I think trying to cut the sentence off before you get to talk about the overall plan doesn't make any sense.

Mr. LEVIN. There is no comprehensive plan yet.

Mr. BOLTEN. There will be and I hope we can attract some support.

Chairman THOMAS. The gentleman's time has expired.

Mr. LEVIN. Not on this side.

Chairman THOMAS. Does the gentleman from Louisiana, Chairman of the Social Security Subcommittee, wish to inquire?

Mr. MCCRERY. Thank you, Mr. Chairman. Yes. Mr. Bolten, just a quick follow-up on Mr. Levin's question. I believe the right answer is, as designed and proposed by the President, the personal accounts do, in fact, have a salutary effect on trust fund payout in the out years, isn't that correct?

Mr. BOLTEN. Again, Congressman, we need to see the full development of the plan, but the important part about the personal accounts from our budget perspective is that although there are these short-term financing requirements, it is not a new cost to the government.

Mr. MCCRERY. Right.

Mr. BOLTEN. This is money the government already owes in the form of future benefits. Letting people keep it sooner, keep it for themselves sooner, is essentially neutral to the government but gives the individuals a chance to get a much better return on that money than the Social Security system can possibly promise.

Mr. MCCRERY. Okay. Well, let us talk a little more about that aspect, the financing of the accounts. Can you explain why borrowing, why the government borrowing money to fund the personal accounts is different from the government borrowing money to pay for—let me be careful which subject I pick——

Mr. BOLTEN. Unwarranted spending of some non-identified nature.

Mr. MCCRERY. Yes. Pork-barrel spending. Yes. Can you explain the difference?

Mr. BOLTEN. Yes. Mr. McCrery is raising a very important point here, and that is that—in fact, it is why I prefer to refer to transition financing rather than transition costs. First is the point that I have just alluded to, which is that in creating these personal

accounts, we allow people to keep more of their money now, so it is not a new cost to the government. We are just taking the benefits we need to pay later on, letting people keep it now. Second, government borrowing, usually for additional spending, has a net negative effect on national savings. There is no net negative effect on national savings from borrowing for people to use for personal accounts because there is an equality between the borrowing that the government does and the money that people set aside in their personal accounts, which is itself savings. So, the effect on the economy is at worst neutral, and in my judgment, the creation of the personal accounts is overwhelmingly positive for the economy.

Mr. MCCRERY. I understand what you just said and it is, I think, perfectly clear. But, why—go one step further. Why is net national saving important to the economy?

Mr. BOLTEN. Well, I am not an economist and I am sure I will prove that many times during the course of this hearing, but the economists will tell you that the savings rate in the country, that the national savings in the country is very important for assuring the continued growth that we have seen over the last few years. To keep that growth growing, we need to have a good savings rate so that investment can carry on and the fruits of investment can be properly realized.

Mr. MCCRERY. So, when you borrow to put money in a personal account, you are not affecting the national savings rate. But, if you borrow to pay for some spending by the Federal government, then you are, in fact, affecting—you are reducing the national savings rate.

Mr. BOLTEN. Correct.

Mr. MCCRERY. Now let us go to taxes for just a moment, and I want to preface this by saying that as a result of 9/11 and the recession, going back to Mr. Rangel's question of who is sacrificing, actually, quite a few people sacrificed in that scenario—those who lost their jobs, their families, so there were sacrifices made by Americans in that. What we try to do as a Congress, and I think the President, we have tried to create an economic atmosphere that was conducive to creating jobs so those folks who lost their jobs could get them back or could get other jobs and their families could feel better about their station in life and all those things. How important is it for us to extend the tax cuts that are already in place? Particularly, I want you to touch on the dividend and capital gains tax relief.

Mr. BOLTEN. Mr. McCrery, I think it is absolutely crucial that we extend the tax cuts that you all have put in place to continue the kind of strong growth we are getting in the economy. It is especially important for those at the bottom end of the income spectrum because those are the people that suffer the most when we have an economic downturn, as they did during the economic downturn that greeted the President when he came into office. Dividends and capital gains, economists will tell you, are at the top of the list in promoting economic growth.

Chairman THOMAS. The Chair believes that is an excellent first paragraph in a written response.

Mr. BOLTEN. Thank you, Mr. Chairman.

Chairman THOMAS. Does the gentleman from Michigan, Mr. Camp, wish to inquire?

Mr. CAMP. I do. Thank you, Mr. Chairman. Director Bolten, clearly, the economy is on strong ground. When you look at average GDP growth last year at over 4 percent, more than two million jobs created last year, wages and salaries increased, small business income up, aftertax income increased, what role do you believe that tax policy enacted in recent years had on this economic growth in terms of our economy and our budget?

Mr. BOLTEN. The Council of Economic Advisors at the White House and the Treasury Department did a study recently in which they tried to isolate the effects of the tax cuts that had been enacted over the course of the President's first term and their conclusion was—I think using cautious estimates—their conclusion was that last year, we had three million more jobs and 3.5 percent larger GDP than we would have had without the tax cuts. I think the tax cuts have been crucial in bringing us back out of a recession and I think they remain crucial for our projections of continued strong economic growth out over the rest of the budget window.

Mr. CAMP. Can we afford to make the 2001 tax cuts on individual rates, capital gains, dividends, permanent and at the same time reform Social Security? Can we afford to do that?

Mr. BOLTEN. My own judgment is that we can't afford not to do that, that the most important thing for our fiscal position is a strong and growing economy. What put us in a fiscal hole at the start of this administration was primarily a weak economy. We now have a strong economy and we have revenues recovering. I think the continuation of the tax cuts that you all have put in place is crucial for our fiscal position going into the future and it is crucial if we are going to address issues like issues of our unfunded liabilities in our entitlement programs like Social Security.

Mr. CAMP. Do you believe we can do that and still fulfill the President's goal of cutting the deficit in half by 2009?

Mr. BOLTEN. I believe we can. The last chart I had up there showed the deficit declining even with the Social Security financing elements included, declining to about 1.7 percent of GDP. That is well below the 40-year historic average of 2.3 percent. The estimates that I showed on that chart include an assumption that the President's tax cuts will be continued. Now, we don't do 10-year budgeting any more, but I think if you look out over the next five years in a budget window, you will see that trajectory continuing, that even with the Social Security financing elements included, we can and should have a continuing declining deficit as a percentage of our GDP if we have the strong economic growth that the tax cuts have helped generate.

Mr. CAMP. If Congress does nothing to reform Social Security, as some of my Democrat friends suggest, how much will it cost ultimately the taxpayer if we delay acting on fixing the program, not to mention denying a whole generation of workers choice in their retirement options?

Mr. BOLTEN. The actuaries have estimated that the overall present value of the unfunded liability on a permanent horizon is $10.4 trillion. That is a hard number for anybody to grasp, I think. But, an important element that you have just raised for this ad-

ministration and this Congress is that that huge number grows by at least $600 billion a year and more each year that we delay in addressing the problem. So, it is crucially important to our fiscal position that we address this unfunded liability as soon as possible.

Mr. CAMP. Ultimately, what effect will that have on the economy if we do nothing?

Mr. BOLTEN. I think the economy will be in serious difficulty—it is hard to say when, when the difficulty would come. But, we would face a serious financial crisis in this government if we did not address these long-term unfunded liabilities. Exactly when the crisis would hit us is uncertain because we now enjoy very low interest rates because there is a great deal of investor confidence in our economy. If we demonstrated that we were unwilling to take on these unfunded liabilities out into the future, I don't know whether that confidence would be sustained, and if the confidence goes, so also go the low interest rates. That is why it is very important to act promptly to deal with the unfunded liabilities.

Mr. CAMP. Thank you. Thank you, Mr. Chairman.

Chairman THOMAS. I thank the gentleman. Does the gentleman from Maryland, Mr. Cardin, wish to inquire?

Mr. CARDIN. Thank you, Mr. Chairman. Mr. Bolten, it is a pleasure to have you before the Committee.

Mr. BOLTEN. Thank you, sir.

Mr. CARDIN. I take it that you are in agreement with the Social Security actuaries in that there is enough revenue coming into the Social Security trust funds and their assets to be able to pay for benefits without any reductions for 37 years?

Mr. BOLTEN. I believe the Social Security actuaries' estimate was through 2042, yes.

Mr. CARDIN. That is right. In fact, the CBO, I believe, is 10 years later, that they believe there are enough assets and revenues coming in to actually take us to 2052. Of course, in 1996, the actuaries actually told us 2029, so it has improved 13 years solvency in the last 8 years without any change in law. The only reason I mention that, as I said yesterday to Secretary Snow, I don't think we should rush to make a mistake. I think we have got to get this right. Has there ever been a Budget Director who has been able to predict 37 years into the future? Are you the first?

[Laughter.]

Mr. BOLTEN. If they were my own projections, I would be more hesitant about them. They are not. They are the Social Security actuaries' projections.

Mr. CARDIN. Right. Okay. Have we ever had an actuary who has been accurate that long? I would like to see that. I guess my concern, again, is that the administration is very reluctant to go beyond 5 years in the budget, and I understand that, even though Congress likes to do a little bit further. I just am concerned about the decisions that we are trying to make today based upon circumstances so far in the future with so many changes that could take place.

Mr. BOLTEN. Congressman, may I comment on that, and that is that, of course, 2042, 2052, it might be 2032, but there is no doubt about the direction in which it is headed.

Mr. CARDIN. There is one part of your testimony that I take issue with that I think you could have been more helpful to us in this debate, where you talk about the projected deficit for 2005 under your budget being $427 billion. I think that is wrong because you are counting Social Security trust funds. I think every Member of this Congress has said and made a commitment that these are trust funds and they shouldn't be commingled with on-budget spending. So, why don't we just get that out of our vocabulary and be transparent to the American people, let them know that the trust funds are trust funds and we are not going to commingle them as we present the budget deficit numbers. We are not going to mask the size of our spending. I think that would help us all in trying to get a handle on current spending.

Mr. BOLTEN. Well, what we use our budget deficit figures for are to determine what are the current borrowing needs of the government. But, we are not masking it. There is even a table at the back of our book which shows exactly what the off-budget and on-budget liabilities are. Budget Directors before me have consistently referred to the overall budget, including the Social Security surplus that we are now enjoying, and I suspect when the Social Security system goes into deficit in the next decade, those numbers will have to be included, as well.

Mr. CARDIN. I would suggest to you that when we were heading toward a surplus, in fact, had a surplus in the operating budgets, it is a lot easier to be able to do that. Now, when you are bragging that you are reducing the deficit by a certain amount over time, you are using Social Security surplus funds to equal that number and I just think it is wrong to do that because we have a growing surplus in Social Security over the next 5 years, whereas you are claiming we are having a reduced budget deficit when in reality you are using Social Security to mask the size of the deficit. I just would urge us all, those of us who believe that we should be paying for our current needs today, don't keep using those Social Security trust funds because it is making it more difficult to deal with a budget as well as the solution to Social Security.

Now, the private accounts in Social Security, I am one of those who strongly supports encouraging Americans to save more. But, by taking the money out of Social Security, I am glad that you acknowledge that that alone hastens insolvencies, does not improve the solvency of the system. In order to do that, in order to bring about the long-term needs of Social Security, you have got to cut benefits, and I think the President has made it clear we are not going to increase taxes, so we have got to cut benefits.

If you could help us with how much we are going to have to cut benefits for those who are in private accounts and those who are not in private accounts, I know the CBO has estimated that there would be as much as an 80-percent reduction in the private accounts when your Social Security benefits, if we get to the expected return. If you could provide us with some numbers here today or by letter, I would appreciate it. How much of a reduction in benefits individuals who are 54 years old today or 27 years old today can expect if they enter a private account or if they don't enter a private account.

Mr. BOLTEN. Congressman, if you will—I think you should await the full articulation of the President's plan, but the one thing I can tell you is that whatever the full details of that plan are, they will be able to pay beneficiaries in the future, those, for example, who are retiring after 2042, a better benefit than the current Social Security system can now pay.

Mr. CARDIN. Thank you, Mr. Chairman.

Chairman THOMAS. We will, of course, rely on those same actuaries for those projections. Does the gentleman from Minnesota wish to inquire?

Mr. RAMSTAD. Thank you, Mr. Chairman. Director Bolten, it is good to see you here. I think we need to set the record straight. There is a lot of hyperbole, as you know, and downright falsehoods as to the President's proposal. There is an attempt that I have seen to scare seniors. My 85-year-old father received a mailing that alleged or that stated the voluntary personal accounts would jeopardize his benefits and the benefits of other seniors, retirees and near-retirees. I think that is loathsome, that critics are resorting to those tactics, those falsehoods, those scare tactics to scare seniors. As I said, I think we need to set the record straight. Let me just ask you straight out. For any and all Americans 55 years of age or older, will the Social Security system change in any way their benefits by adding the option of personal accounts for younger workers?

Mr. BOLTEN. The President has been clear, for that group, no change.

Mr. RAMSTAD. So, the President's voluntary personal retirement accounts would not change benefits one iota, one penny, for any retiree or near-retiree, is that correct?

Mr. BOLTEN. That is correct, sir.

Mr. RAMSTAD. I think we need to, as I said, be honest in our discourse, and the level of discourse, I have never seen lower as far as Social Security is concerned with these, as I said, attempts to scare seniors. I think they are very, very unfortunate. Let us at least be honest, intellectually honest, as we argue the merits or lack thereof of the proposal. I also have seen the critics and heard the critics say, with reference to personal accounts, that Social Security voluntary personal accounts will not boost retirement income, but rather reduce it. The critics have described the President's personal account proposal as workers borrowing against their Social Security benefits and then repaying government in the form of an automatic benefit reduction at retirement. Certainly, this is not an accurate portrayal of the President's proposal, is it, Director Bolten?

Mr. BOLTEN. I don't believe it is.

Mr. RAMSTAD. Would workers be borrowing payroll taxes they contribute to Social Security to be repaid with interest later?

Mr. BOLTEN. I don't believe that is—I am having trouble actually following what the idea there would be.

Mr. RAMSTAD. Well, I mean——

Mr. BOLTEN. That certainly is not the President's plan.

Mr. RAMSTAD. Which underscores my point. Some of these attacks are absolutely ludicrous, they are so preposterous and absurd. Certainly, we need, though, I think, to clarify that the Presi-

dent's proposal for voluntary accounts is designed to boost retirement income, not to reduce it, as alleged by some critics.

Mr. BOLTEN. That is correct, certainly well above what the current system now has an ability to pay.

Mr. RAMSTAD. Given the time value of money and the principle of compound interest, I think that should be readily apparent to most honest critics, people working on this proposal. Thank you, Director Bolten. I will yield back.

Chairman THOMAS. I thank the gentleman for the contribution of time. The Chair recognizes, if he wishes to inquire, the gentleman from Washington, Mr. McDermott.

Mr. MCDERMOTT. Thank you, Mr. Chairman. Welcome, Director Bolten. Listening to you and Secretary Snow yesterday reminded me that we had been transported back to the days of the Delphi Oracle and we were listening to the wizard try and figure out what was going on here. Yesterday before the Budget Committee, you said the President is planning on coming forward with a proposal to address the funding shortfall that faces Social Security. But, I have a Reuters story this morning that says the White House has told lawmakers it has no immediate plans to submit its own detailed proposal to Congress for overhauling Social Security. A senior Bush Administration official said no final decision has been made. If there comes a point where the President needs to spell out a specific legislation, he won't hesitate. Now, I am sure you can understand our feeling of being a little at sea about what it is you are up here trying to sell. But, you are, I am sure, familiar with this article, which was printed in the Wall Street Journal. It is a memo from Peter Wehner, one of your friends up in the White House, and you are familiar with that memo, are you?

Mr. BOLTEN. I am not, sir.

Mr. MCDERMOTT. Well, let me read a little bit for you. I can't imagine you don't realize what is in here. "We simply cannot solve the Social Security problem with personal retirement accounts alone. If we borrow $1.1 to $2 trillion to cover transition costs for personal saving accounts and make no changes in wage indexing to price indexing, we will have borrowed trillions and will still have to confront more than $10 trillion in unfunded liability." Now, my colleague, Mr. Cardin, asked you, will there be benefit cuts? Mr. Rangel says, why don't you ask him if he is as clear about people under 55 as you are above 55. You say if you are above 55, there will be no cuts. Are you saying, or are you willing to say that if you are under 55 years of age, there will be no cuts?

Mr. BOLTEN. Mr. McDermott, you need to wait for the full articulation of the President's plan——

Mr. MCDERMOTT. Well, but when? How long are we going to sit up here and discuss ideas that float around? We can all have ideas. When are you going to write it down and make a law out of it? Franklin Delano Roosevelt brought it up to the Congress.

Mr. BOLTEN. Well——

Mr. MCDERMOTT. Actually, Mrs. Clinton brought up a health care plan to the Congress. So, you see, if you bring it up here, you might run into some problems, and you can't use this dodge, well, we have to wait until. We are having a hearing on Social Security and we know from what is going on in the White House—now, let

me give you an answer, because I know my time will run out and I think you have got a copy, or somebody is going to give you a copy of this. It is from the Budget Committee and it shows that permanent tax cuts are $11.6 billion, if we extend them. That is what it is going to cost over the next 10 years—the next 75 years. The tax cut to the top 1 percent is $3.4 trillion—billion—trillion, excuse me. Social Security shortfall is $3.7 trillion. Now, if you made one simple change in your tax cuts and took it away from the top 1 percent, there would be no problem for 75 years in the Social Security fund. So, it isn't hard to solve this if you want to make the program solvent, stable. If you want to borrow $2 trillion and put us out into the stock market and hope that we can claw back enough from people that they will ultimately get some benefit—you can't tell people what they are going to get under your plan because there is no plan. Reuters says it right out of the White House. How do you keep selling this to the people?

Mr. BOLTEN. Mr. McDermott, if what you are proposing is that we raise taxes in order to try to cover the Social Security——

Mr. MCDERMOTT. No, I just said let the law expire like it is. That is not raising taxes. That is just not getting in the way of it. You wrote the law that way. That is the way the President wanted it, with an expiration date out there 10 years.

Mr. BOLTEN. Well, however——

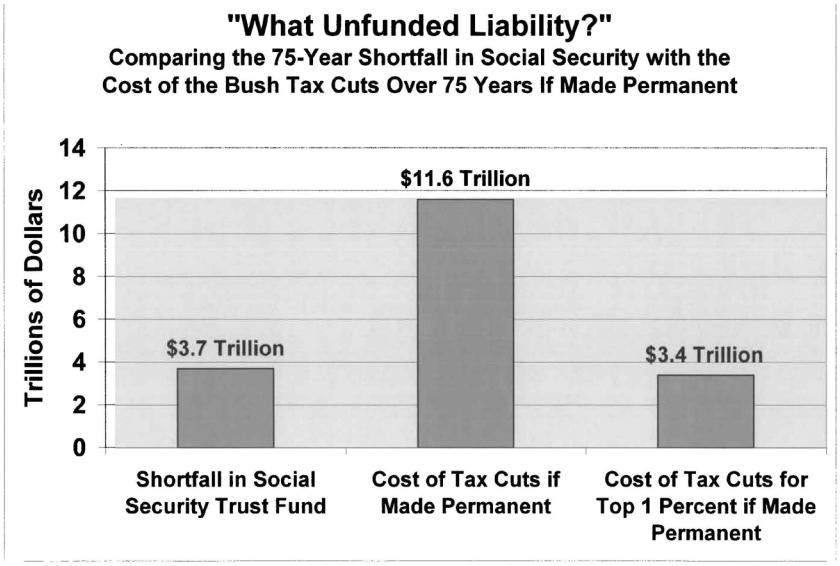
Mr. MCDERMOTT. We always knew he was lying. He really wanted a permanent tax cut, but he couldn't get it, so he said, let us let it go, right?

Mr. BOLTEN. However you want to characterize it, Mr. McDermott, I don't think tax increases are the answer for solving the Social Security problem, particularly within the Social Security——

Mr. MCDERMOTT. What is your financing plan, then? There is nothing in this budget.

Chairman THOMAS. The gentleman's time has expired and the Chair would ask unanimous consent that the chart that the gentleman from Washington used would be made a part of the record, with the understanding that although it was represented to come from the Budget Committee, it says, "prepared by the Democratic staff of the House Budget Committee."

[The information follows:]



Prepared by Ways and Means Democratic Staff
Source: Center on Budget and Policy Priorities, using numbers from the Social Security Trustees, the Joint Committee on Taxation, and the Cognressional Budget Office.

The Chair would recognize the gentleman from Ohio, if he wishes to inquire.

Mr. MCDERMOTT. Mr. Chairman, could I ask one question?

Chairman THOMAS. Certainly.

Mr. MCDERMOTT. This is just a procedural question. We used a Power Point today and I brought this on Power Point, but I was told that it couldn't—the staff tried to make it work. Is there a way that we are going to be able to use Power Point in this——

Chairman THOMAS. I would tell the gentleman that I was desirous of doing that. One of the things that the Director indicated to us was that he wanted to use it. We spent the early portion of the morning double checking, making sure everything worked. As we move forward with this new technology, we are going to be able to do it, but the ability to do it instantly is probably going to produce a few disasters, so that if Members——

Mr. MCDERMOTT. There is a learning curve.

Chairman THOMAS. Yes, there is a learning curve and we would like to do it without public presence because then you will want to take the time to get it fixed if it doesn't come up. If Members in the future have material that they wish to present in similar to this format, which I think will be very helpful to the Members, we need a little bit of lead time to try to see if we can, in fact, make it work and that it would be available to us.

Mr. MCDERMOTT. Thank you.

Chairman THOMAS. So, it is both the newness of the system and the timeliness problem of having it available.

Mr. POMEROY. Mr. Chairman?

Chairman THOMAS. The Chair looks forward to many multicolor presentations on the part of the Members with this new wonderful stuff. The gentleman from North Dakota——

Mr. POMEROY. Just a quick procedural issue. The gentleman from Washington referenced a memo from the White House, Peter Wehner. I also referenced this yesterday and will again in my questions today. I wonder if we might include it——

Chairman THOMAS. Without objection, the Chair will also place that material in the record.

[The information follows:]

Memo on Social Security from Peter Wehner, Director of Strategic Initiatives for the Bush Administration

From: Wehner, Peter H. [mail to: Peter_H._Wehner@who.eop.gov]
Sent: Monday, January 03, 2005 2:57 PM
Subject: Some Thoughts on Social Security

I wanted to provide to you our latest thinking (not for attribution) on Social Security reform.

I don't need to tell you that this will be one of the most important conservative undertakings of modern times. If we succeed in reforming Social Security, it will rank as one of the most significant conservative governing achievements ever. The scope and scale of this endeavor are hard to overestimate.

Let me tell you first what our plans are in terms of sequencing and political strategy. We will focus on Social Security immediately in this new year. Our strategy will probably include speeches early this month to establish an important premise: the current system is heading for an iceberg. The notion that younger workers will receive anything like the benefits they have been promised is fiction, unless significant reforms are undertaken. We need to establish in the public mind a key fiscal fact: right now we are on an unsustainable course. That reality needs to be seared into the public consciousness; it is the pre-condition to authentic reform.

Given that, our aim is to introduce market reforms in Social Security and make the system permanently solvent and sustainable.

We intend to pursue the first goal by using our will and energy toward the creation of Personal Retirement Accounts. As you know, our advocacy for personal accounts is tied to our commitment to an Ownership Society—one in which more people will own their health care plans and have the confidence of owning a piece of their retirement. Our goal is to provide a path to greater opportunity, more freedom, and more control for individuals over their own lives. That is what the personal account debate is fundamentally about—and it is clearly *the* crucial new conservative idea in the history of the Social Security debate.

Second, we're going to take a very close look at changing the way benefits are calculated. As you probably know, under current law benefits are calculated by a "wage index"—but because wages grow faster than inflation, so do Social Security benefits. If we don't address this aspect of the current system, we'll face serious economic risks.

It's worth noting that wage indexation was *not* part of the original design of Social Security. The current method of wage indexation was created in 1977, under (you guessed it) the Carter Administration. Wage indexation makes it impossible to "grow our way" out of the Social Security problem. If the economy grows faster and wages rise, this produces more tax revenue. But the faster wage growth also means that we owe more in Social Security benefits. This has produced a never-ending cycle of higher tax burdens, even during periods of robust economic growth. It is the classic case of the dog chasing his tail around the tree; he can run faster and faster, and never make any progress.

You may know that there is a small number of conservatives who prefer to push only for investment accounts and make no effort to adjust benefits—therefore making no effort to address this fundamental structural problem. In my judgment, that's a bad idea. We simply cannot solve the Social Security problem with Personal Retirement Accounts alone. If the goal is permanent solvency and sustainability—as we believe it should be—then Personal Retirements Accounts, for all their virtues, are insufficient to that task. And playing "kick the can" is simply not the credo of this President. He wants to do what needs to be done for genuine repair of Social Security.

If we duck our duty, it can have serious short-term economic consequences. Here's why. If we borrow $1–2 trillion to cover transition costs for personal savings accounts and make no changes to wage indexing, we will have borrowed trillions and will *still* confront more than $10 trillion in unfunded liabilities. This could easily cause an economic chain-reaction: the markets go south, interest rates go up, and

the economy stalls out. To ignore the structural fiscal issues—to wholly ignore the matter of the current system's benefit formula—would be irresponsible.

Here's a startling fact: under current law, an average retiree in 2050 would be scheduled to receive close to *40 percent more (in real terms)* in benefits than an average retiree today—and yet there are *no* mechanisms in place to produce the revenue to pay out those benefits. No one on this planet can tell you why a 25-year-old person today is entitled to a 40 percent increase in Social Security benefits (in real terms) compared to what a person retiring today receives.

To meet those benefit levels, one option would be to raise the age at which people receive benefits. If we followed the formula used when Social Security was first created—make the age at which you receive Social Security benefits above the average age of mortality—we'd be looking at raising the benefit age to around 80. That ain't gonna happen.

Another way to meet those benefit levels is through the traditional Democrat/liberal way: higher taxation. According to the latest report of the Social Security Trustees, the current system's benefit formula would require some $10 trillion in tax increases over the long term. We'd therefore need to raise the payroll tax almost 20 percent simply to provide wage-indexed benefit levels to those born this year.

This will all sound familiar. In the past, the way Congress usually addressed the built-in funding problem was by raising payroll taxes (from 2 percent in 1937 to 12.4 percent today). In fact, Congress has raised Social Security taxes more than *30 times*—but it has *never* addressed the underlying problem. Avoiding the core issue by raising taxes is not the *modus operandi* of this President.

The other key point, as you know, is that personal accounts, through the miracle of compound interest, will provide workers with *higher* retirement benefits than they are currently receiving from Social Security.

At the end of the day, we want to promote both an ownership society *and* advance the idea of limited government. It seems to me our plan will do so; the plan of some others won't.

Let me add one other important point: *we consider our Social Security reform not simply an economic challenge, but a moral goal and a moral good.* We have a responsibility to fulfill the promise of Social Security, not undermine it. And we have a duty to ensure that we do not create an inter-generational conflict—which is precisely what will happen if the Social Security system is not reformed. We need to retain strong ties between the generations, which is of course a deeply conservative belief.

The debate about Social Security is going to be a monumental clash of ideas—and it's important for the conservative movement that we win both the battle of ideas and the legislation that will give those ideas life. The Democrat Party leadership, the AARP, and many others will go after Social Security reform hammer and tongs. See today's silly *New York Times* editorial (its only one for the day) as one example. But Democrats and liberals are in a precarious position; they are attempting to block reform to a system that almost every serious-minded person concedes needs it. They are in a position of arguing against modernizing a system created almost four generations ago. Increasingly the Democrat Party is the party of obstruction and opposition. It is the Party of the Past.

For the first time in six decades, the Social Security battle is one we can win—and in doing so, we can help transform the political and philosophical landscape of the country. We have it within our grasp to move away from dependency on government and toward giving greater power and responsibility to individuals.

There are of course other important issues dealing with Social Security; for now, though, I've covered quite enough ground. I wanted to let you know where things stand. If you have any questions, or if we can send you anything to clarify our plans and respond to critics, just let me know. The President remains flexible on tactics—and rock-solid on the principles. But there's nothing new there.

In one of his last public acts of an extraordinary public life, the late Democratic Senator from New York, Daniel Patrick Moynihan, cochaired the President's Commission to Strengthen Social Security. In the introduction of its report, Senator Moynihan (along with Richard Parsons, his cochair) wrote, "the time to include personal accounts in such action [reforming Social Security] has, indeed, arrived. The details of such accounts are negotiable, but their need is clear. . . . *Carpe diem*!"

And so we shall.

Mr. BRADY. Mr. Chairman?

Chairman THOMAS. The gentleman from Texas?

Mr. BRADY. Very quickly, I recognize that this chart is prepared by the Democratic staff. The source of it is not clear. Can that be clarified before it is put in the record?

Chairman THOMAS. Who is CBPP?

Mr. BRADY. Is that the Center for Budget Policy Priorities?

Mr. MCDERMOTT. The Center on Budget Priorities and something or other, another Washington acronym. I don't know what it means.

Mr. BRADY. As long as we clarify that this group is deathly opposed to both tax relief and Social Security reform——

Chairman THOMAS. Well, the gentleman should have picked that up with the scribbling in the lower right-hand corner, which indicates where it was faxed from, I assume.

Mr. LEVIN. I would object to any characterization of the source. If you don't know what CBPP is, we will tell you, but I don't think any of us should characterize——

Mr. BRADY. Other than the mumbling on what the PP might stand for, I think——

Mr. LEVIN. Policy and Priorities.

Mr. BRADY. Okay. This group is historically opposed to tax relief and Social Security reform as proposed——

Mr. LEVIN. That is not true.

Mr. BRADY. I think it is always important——

Mr. LEVIN. That is not true.

Mr. BRADY. To understand the source. That is all.

Mr. LEVIN. It is just not true.

Chairman THOMAS. Hope springs eternal, and the President's current opportunity to persuade people means even this group is open to possible persuasion. I just wanted to clarify the fact that this was not Budget Committee prepared, but by the Democratic staff from another source.

Mr. MCDERMOTT. Mr. Chairman——

Chairman THOMAS. The gentleman from Ohio——

Mr. MCDERMOTT. Could I just say——

Mr. PORTMAN. Thank you, Mr. Chairman.

Mr. MCDERMOTT. These figures were—Mr. Brady, the figures from the Social Security shortfall came from the SSA. These are not—they are taken from their data.

Mr. BRADY. And manipulated by the source. My only point is, let us just be open about what the source is and we can all draw our own conclusions.

Chairman THOMAS. The Chair would indicate that the source rather than initials would be spelled out in its entirety so that people could understand who they are.

Mr. BRADY. Mr. Chairman——

Chairman THOMAS. The gentleman from Ohio is recognized.

Mr. PORTMAN. Thank you, Mr. Chairman. I promise not to ask that any charts be inserted into the record to avoid any further disruptions to the Committee. I want to start by commending the budget. This administration has a lot to be proud of in terms of the economic growth we have seen over the last year, and when Mr. Bolten was before this Committee previously and before the Budget

Committee, we weren't sure, frankly, what the results of the tax relief would be, and now we are seeing it, incredible growth over the last year. We have also seen 9.2-percent increase in receipts in 2005. Despite all of the hand-wringing we heard about the 2001, 2002, 2003 tax relief, that it was going to result in robbing the Treasury, we have seen, what, an increase in receipts to the government.

The budget reflects that going forward. It says we need to promote pro-growth economic policy on the one hand. On the other hand, we need to restrain spending, which is the only thing that works. We saw this in the late nineties going into this decade. We need to restrain our spending and have the economy grow. So, I commend you for it. We may have some differences on some specifics, but this is an excellent budget because it does fund our top priorities and yet has spending restraint and pro-growth economic policies and I think that is the solution for us indeed meeting this target of reducing the deficit in half by 2009.

I was interested in the discussion you had a moment ago, Director Bolten, with Mr. McDermott talking about the fact that you guys don't have all the details yet on your plan and when are you going to write it down. I guess you could have said to him, when are you going to write your plan down, but then I think he said what it is, which is raising taxes. Saying that taxes on the wealthy can pay for all of our Social Security fixes, I don't believe that is true. I wonder if you could comment on that quickly, as to whether not allowing the tax cuts to continue, in other words, raising taxes on the top 1 percent would pay for all the Social Security needs over the next decade.

Mr. BOLTEN. Mr. Portman, I don't believe they would at all and it would also require a relatively radical change from the traditional Social Security system that operates within its own system to now drawing revenues out of the regular income tax.

Mr. PORTMAN. I would also ask you, because there is this assumption, well, gee, just raising taxes on the rich should solve this problem. You responded earlier that tax relief has helped grow the economy, particularly some tax relief that is pro-growth was, and I would put that in that category. What happens with regard to taxes as a percentage of our economy? Right now, we are at 16-some percent. Let us assume that the President does make permanent his tax relief which is in his budget and provided for. What happens in terms of the percentage of taxes as to our economy, our GDP? Does it go up or down? It must go down, right?

Mr. BOLTEN. It goes up——

Mr. PORTMAN. It goes up? Interesting. So, we are going to actually have more revenue coming in, and as a percentage of GDP, taxes actually go up, even though we make permanent the tax relief you have put in place.

Mr. BOLTEN. Yes. The budget figures that you will see reflected in our documents assume the full permanence of the tax cuts that the President proposed and you enacted, and even with those tax cuts in place, we see revenues rising steadily up to about 18 percent by the end of the budget window, which is the historic average that taxes have taken as a percent of our economy.

Mr. PORTMAN. So, the notion we are undertaxed, the percentage actually rises during this period that we make the tax relief permanent. How about on distribution? Who is paying these taxes? I assume from what I am hearing to the side that those who are higher-income Americans are paying less of the burden, right?

Mr. BOLTEN. The tax cuts that you enacted and that the President signed are often considered to have made the Tax Code less progressive. The truth is that they have made the Tax Code more progressive.

Mr. PORTMAN. Interesting. So——

Mr. BOLTEN. If you——

Mr. PORTMAN. Can you give me some numbers on that?

Mr. BOLTEN. If you take a segment of the population, say the top 5 percent of income earners in this country—that is people making more than $140,000 a year—in the absence of the President's tax cuts, they would be paying a little less than 52 percent of the overall income tax take of this country. After the President's tax cuts, they pay a little more than 54 percent of the total income tax take of this country. The Tax Code, as a result of the changes that you and the President have made, has become more, rather than less, progressive. Everybody got a tax cut, but the Code is more progressive than it used to be.

Mr. PORTMAN. I appreciate that clarification. I just think as we are looking at how to fund our key priorities, including Social Security, and in my view, I think the power of compound interest, having those assets out there building up, is a solution to part of the Social Security problem, one we definitely need to allow our young people to access. But, we need to look at the tax situation and realize that tax relief has helped to grow this economy. At a minimum, we should not be raising taxes. In fact, taxes will grow as a percentage of the economy and those wealthier Americans are paying more of the load, not less of the load, under the President's proposals. I think we need to lay that out. Again, I would commend you on the budget. I think it reflects those priorities. I think it will enable us to reduce this deficit in half and be sure that Social Security, therefore, is on a more solid footing. I thank you, Mr. Director.

Mr. BOLTEN. Thank you.

Chairman THOMAS. I thank the gentleman. Does the gentleman from Georgia, Mr. Lewis, wish to inquire?

Mr. LEWIS. Thank you very much, Mr. Chairman. Mr. Director, I want to thank you for being here. Mr. Director, apparently during the briefing on the budget on Monday, you told a group that you entered this discussion, you entered this debate with a happy spirit. I assume your spirit is still happy. But, how could your spirit be so happy with Social Security facing a major crisis, major problems, bankruptcy, as the President put it? I would like for you to just elaborate. I want to know your mindset when you talk about privatizing Social Security, when you talk about making a choice, a decision between making the tax cuts permanent and privatizing Social Security.

Mr. BOLTEN. Mr. Lewis, I don't believe we face a choice and I am very optimistic, A, about the short—and medium-term path that we are on if we adopt the President's pro-growth policies and spending restraint. I am very optimistic about the short—and me-

dium-term deficit path we are on. In the long-run, the serious problem we face is in the unfunded liabilities in our entitlement programs and I am optimistic that the President and this Congress will come around on the issue of Social Security to finding a way to fix that problem permanently.

Mr. LEWIS. Is it true that when the President was moving around on the stump last week, didn't he say even with private accounts, this will not fix Social Security for the long run? Why is it so sacred? Why is it so special?

Mr. BOLTEN. Personal accounts, I think, are a tremendous innovation for the Social Security system——

Mr. LEWIS. I should have said personal accounts, I guess, but it is privatization of Social Security.

Mr. BOLTEN. The personal accounts are a tremendous innovation for many reasons. One of them is that you are simply letting people keep more of their own money and control it themselves, pass it on to their heirs, and basically exercise more control over their own retirement and receive a better return on their money than the Social Security is now able to promise. So, it is a very important innovation for the system, and as part of comprehensive reform, I think it is very good fiscal news for the country, as well.

Mr. LEWIS. Mr. Director, do you subscribe to the idea, to the concept that Social Security is a contract with the American people, it is a matter of trust that we promised the American people, going back to the New Deal, FDR? So, is this administration proposing to violate this sense of trust, this contract?

Mr. BOLTEN. Oh, I think on the contrary, what this administration is proposing to do is fulfill the trust and the contract. The problem we are facing now is that by the time some of our youngest workers are ready to retire, the system will not be able to pay the benefits it promises. We need to fix that system.

Mr. LEWIS. The President said on the stump last week that this is not fixing it. You can't have it both ways. You can't say you are fixing it and then the President is saying it will not fix it, it will not make it whole.

Mr. BOLTEN. I am not sure what comment of the President you are referring to, but——

Mr. LEWIS. President Bush, because he is the President, and he said someplace during the past few days when he was campaigning in five or six States that personal accounts, private accounts, would not fix the problem or the crisis of Social Security alone.

Mr. BOLTEN. I don't know what the exact quote of the President is, but I said something similar here just this afternoon, which is that in and of themselves, the personal accounts don't solve the solvency problem of Social Security. But, they are an integral part to a comprehensive plan that does fix the system and does ensure that our workers get the kind of benefit they expect.

Mr. LEWIS. You said to some others that you don't have the blueprint, you don't have the road map, you don't have the complete plan. How can you bring a piece, a part, however this piece, this part is going to fit into the overall plan?

Mr. BOLTEN. I think the President has kicked off the debate with a portion of the proposal, which is the parameters of the personal account. I think a lot of the Members in the past have wel-

comed the opportunity to work with the administration before any proposal is in concrete and that is the process that is ongoing now. It is a process of back and forth with the Chairman and other Members who are interested in Social Security reform.

Mr. LEWIS. Thank you. Thank you, Mr. Chairman.

Mr. BOLTEN. Thank you, sir.

Chairman THOMAS. I thank the gentleman very much. Does the gentleman from Arizona, Mr. Hayworth, wish to inquire?

Mr. HAYWORTH. I do, Mr. Chairman, and I thank you, and to Mr. Bolten, welcome to the Committee. I listened with interest to my friend from Georgia and I thank him for his comments. Of course, he mentioned the historical precedent of President Franklin Roosevelt, and at least through some media outlets, we have seen that while we describe personal accounts as an innovation, at least somewhere early on in the historical record, President Franklin Roosevelt spoke of these same types of accounts eventually. I think it is perhaps interesting not to view this in a vacuum but to take a more comprehensive look at the true history and legacy of Social Security and the challenges that even FDR knew we would confront 1 day as a nation that grows and a nation that changes and a nation that evolves.

In fact, let me read this into the record. In an address to Congress on January 17, 1935, this is what President Franklin Roosevelt said, quoting now, "For perhaps 30 years to come, funds will have to be provided by the States and the Federal government to meet these pensions." But, after that, he explained, it would be necessary to move to what he called, quote, "voluntary contributory annuities by which individual initiative can increase the annual amounts received in old age," close quote. So, President Franklin Roosevelt made a call in the establishment of Social Security directly anticipating today's reform agenda. Quoting again from President Roosevelt, "It is proposed that the Federal government assume one-half of the cost of the old-age pension plan which ought ultimately to be supplanted by self-supporting annuity plans," close quote.

Mr. Bolten, do you have any reason to doubt the authenticity of President Franklin Roosevelt's remarks made in 1935?

Mr. BOLTEN. No, sir. It actually comes as news to me, but very interesting and encouraging news.

Mr. HAYWORTH. In the spirit of bipartisanship, do you welcome that account from the record?

Mr. BOLTEN. I do, Mr. Hayworth, and I think it reflects that over time, and I would hope on a bipartisan basis, that we can recognize the importance that this country has always put on individual initiative, individual ownership, and the power of the marketplace to improve lives everywhere in this country. I think that is what personal accounts do promise.

Mr. HAYWORTH. I thank you, sir, and I have no further questions. I thank the Chair and thank our Director.

Chairman THOMAS. I thank the gentleman. The gentleman from New York indicates to me that he was there and he doesn't remember that quote.

[Laughter.]

Does the gentleman from Massachusetts, Mr. Neal, wish to inquire?

Mr. NEAL. Thank you very much, Mr. Chairman. Mr. Bolten, at least ten times in your testimony, you have referenced private accounts. It was only when Mr. Lewis used the word personal account that you kind of came back to personal account. Which one is it, a private account or personal account?

Mr. BOLTEN. We prefer the phrase personal account.

Mr. NEAL. You prefer the phrase, but the idea is the private account?

Mr. BOLTEN. It may be a question of vocabulary, but personal accounts, I think, is the right way to characterize them because these are accounts that are still part of a government system. The management would still be in the government. It is not, as some would have you——

Mr. NEAL. Mr. Bolten, let me ask you, yesterday, Mr. Snow was here. He indicated that there were only two ways to balance the budget here. He said one of those would be to grow the economy and the other was to restrain spending. I think, as a group, I think you have come up with a third way, and that is not to include other costs within the budget. Are you familiar with Lawrence Lindsey?

Mr. BOLTEN. I am.

Mr. NEAL. Do you have a high opinion of him?

Mr. BOLTEN. Very high.

Mr. NEAL. Well, do you think he was accurate when he said the cost of the war was going to be between $200 and $300 billion?

Mr. BOLTEN. Well, I don't know exactly which reference——

Mr. NEAL. Well, do you think he was accurate?

Mr. BOLTEN. I don't know——

Mr. NEAL. Are you headed toward $200 to $300 billion?

Mr. BOLTEN. The costs of the war are probably headed in that direction.

Mr. NEAL. Well, how come the administration chose to lowball the number.

Mr. BOLTEN. I don't believe the administration——

Mr. NEAL. Oh, they sure did. They said $40 to $60 billion, and, in fact, 40 to 60 days, we would be out of there. Where are we headed with the cost of the war, Mr. Bolten? Is that discussed at all? Are we going to continue to use supplemental requests from the administration so that we can masquerade the size of the cost of the war and then keep it off-budget?

Mr. BOLTEN. We are going to continue to use supplemental requests for the cost of the war and that is the sound budgeting thing to do because if we do not operate on a supplemental basis, we find that those costs are entered into the base of the budget and never come out.

Mr. NEAL. Mr. Bolten, we have discussed the idea of AMT since you were a child in Congress. Do you think there is a chance that that might be included in budget projections, as well? Is that something we are going to take up, do you think, in the near future?

Mr. BOLTEN. The President has suggested that it be taken up in the context of fundamental tax reform.

Mr. NEAL. Let me ask you this. Can you assure that 40-year-old that might be listening today or watching today that there will be no benefit cut under your privatization plan of Social Security?

Mr. BOLTEN. What I can assure that 40-year-old is that the current system is unable to pay the benefits——

Mr. NEAL. Can you guarantee him that he is going to get and derive the same benefit down the road that the current Social Security system promises?

Mr. BOLTEN. What I can guarantee him is that the current system can't pay the benefit——

Mr. NEAL. Would you suggest, perhaps, that he not invest in Enron stock down the road?

Mr. BOLTEN. I am not even sure whether Enron is still trading, but that——

Mr. NEAL. Well, I am not sure that it is still trading, either, and that is the point. For those that did invest in Enron stock as part of their retirement savings——

Mr. BOLTEN. Well, if you are suggesting that the personal accounts which are referred——

Mr. NEAL. I am suggesting that retirement is a three-legged stool, personal savings, private pension, and Social Security. As it relates to Enron, only one of the three is probably secure, Social Security.

Mr. BOLTEN. Mr. Neal, if I could finish the sentence, the personal accounts to which I was referring are——

Mr. NEAL. Is it private or personal, Mr. Bolten?

Mr. BOLTEN. It is personal.

Mr. NEAL. Okay.

Mr. BOLTEN. The personal accounts to which I was referring are ones that do not permit the individual to invest in individual stocks. It would be like the Thrift Savings Plan (TSP), which has index-based stocks and so on and over time——

Mr. NEAL. I would say that is in addition to Social Security.

Mr. BOLTEN. Historically, those are not risky investments.

Mr. NEAL. That is in addition to Social Security. It is not as a replacement for Social Security.

Mr. BOLTEN. Well, no, the personal accounts I am talking about would be part of a comprehensive Social Security plan.

Mr. NEAL. When do you think we might anticipate seeing a plan here? Yesterday, if you were a Republican Member of the Committee and you asked the Secretary of the Treasury a question, you got an answer in the specific. If you were a Member on this side and you asked the Secretary a question, we were told there really wasn't a plan yet.

Mr. BOLTEN. Well, my expectation is that the full details of a plan will depend in large part on the consultations with the Congress, including the Chairman.

Mr. NEAL. Thank you, Mr. Chairman.

Chairman THOMAS. The gentleman from New York doesn't remember the President saying we would be out in 40 days, is that right?

[Laughter.]

Mr. RANGEL. No, I just, in the spirit of bipartisanship, I just hope that the Budget Director would clarify what he meant when

he suggested that the President would be presenting a plan after consultation with the Congress. Did you mean Republicans in the Congress or—because if we waited for him to get in touch with the Democrats, there won't be a bill.

Mr. BOLTEN. The President, I know, will be open to working with Members of either party who want to participate in a comprehensive Social Security reform plan——

Mr. RANGEL. Oh, you are so good. You are much better—it has been a much better day with you, I can tell you that. Thank you so much.

Chairman THOMAS. I thank the gentleman. The President is willing to work with every live Member of the House and the Senate.

[Laughter.]

Does the gentleman from Missouri wish to inquire?

Mr. HULSHOF. I thank the Chairman. To my friend, Mr. Neal, is the TSP a private plan or a personal plan?

Mr. NEAL. I think it is—do you want an answer?

Mr. HULSHOF. Sure.

Mr. NEAL. I think it is quasi-private.

Mr. HULSHOF. I think, reclaiming my time, as Mr. Bolten suggested——

Mr. NEAL. Is that a satisfactory answer, or——

Mr. HULSHOF. I think, obviously, the TSP, if, in fact, it is used as a model, is something that I think probably—I am not going to inquire of all the Members, but each Member of Congress has confidence in that type of model for a plan and I think, again, there are many ideas out there. In fact, my friend from North Dakota, Mr. Pomeroy, may recall—I am not sure if it was his last visit to the Show-Me-State of Missouri, but back in 1998, Mr. Pomeroy, in February, you and I shared the stage with the then-President of the United States in Kansas City, President Bill Clinton. It was styled as the first ever townhall debate on the future of Social Security. Our President at that time talked about the idea of getting a better rate of return. In fact, as Mr. Pomeroy probably remembers, as he and I were the only Representatives from the House of Representatives there, that the insistence was that we craft a solution sooner rather than later, I think the gentleman recalls. Of course, we had some interesting discussion about how to accomplish that.

Then, I think, Mr. Bolten, I applaud the President. Something that really struck home on a personal note during the State of the Union last week was as the President talked about if you have a 5-year-old child, which we do, a 5-year-old and a 2-year-old daughter, you would not wait until my daughter is a senior in high school before you begin to start thinking of, well, how are we going to afford college? You obviously want to look ahead and make those necessary decisions as a family. There is this discussion, which I think is a bit of a—kind of puts us in the wrong direction when we say, well, is it 2042 or is it 2052 and what sort of assumptions are being made. I have talked about what Chairman Thomas has brought up. The fact is, the baby boomer generation, what year do we generally designate as the first year of the baby boomer generation, Mr. Bolten? Born in what year?

Mr. BOLTEN. I am not sure. I think it is 1948?

Mr. HULSHOF. Nineteen-forty-six.

Mr. BOLTEN. Forty-six. Thank you.

Mr. HULSHOF. We never ask a question unless we know the answer. Early retirement age, even though for younger workers we have raised the retirement age, but still for those seniors who choose to opt out and take early retirement is what year? It is still 62. Here is a tougher question for you which I didn't know the answer to until the SSA actuaries gave us this number. Would you care to hazard a guess as to what percentage of senior citizens choose to opt out for early retirement? Do you want to hazard a guess?

Mr. BOLTEN. No, I am going to kick that back to you, Mr. Hulshof.

Mr. HULSHOF. Fifty-five percent. Fifty-five percent of senior citizens—again, this is obviously something very lawful and legal and it is their own choice to do—55 percent of our senior citizens choose the age of 62 to opt out of the workforce and then begin to rely upon retirement savings through Social Security. So, if my math is correct, not fuzzy math, but if take 1946 and you add the age of 62, we know that in 3 years, in the year 2008, over half of the senior citizen population, those that could be enlisted to help us craft a solution, are going to voluntarily choose to take themselves out of the workforce. Again, we can banter about the assumptions and whether money going out in 2018 as far as the money that comes in through payroll taxes. I agree with what President Clinton said in the Show-Me-State back in 1998. We have an obligation to act sooner rather than later.

I have a technical question for you. My time is running short. I have a concern on a specific provision from the administration's proposal regarding power rates and the Power Marketing Administration that, with your permissions, Mr. Bolten, can I submit that to you in writing? There are over half of my constituents, over 400,000 of whom depend upon rural electric co-ops for their power source, and so I have a concern, but I will submit that in writing. Never one to relinquish time that remains, I also want to applaud the White House—oops—for the permanent repeal of the death tax. Again, I am honored our former colleague, Jennifer Dunn, passed along this effort to me as far as the complete repeal of the death tax and I applaud the White House for acknowledging that. Thank you, Mr. Chairman.

Chairman THOMAS. The gentlemen's time has bountifully expired. Does the gentleman from Louisiana, Mr. Jefferson, wish to inquire?

Mr. JEFFERSON. Thank you, Mr. Chairman. I want to make two statements before I ask a question. The first is that it seems terribly disingenuous to have remarks made when one states that expiring tax ought to be used for a certain purpose to say that it is a tax increase is being urged because it is about as nonsensical to say that as to say that those who voted for taxes to expire in the first place voted for a tax increase at the point of expiration. It absolutely make no sense. If those on the other side voted for a tax that is going to end at a certain time, they obviously voted for it to increase at the end of that period. I think we ought to have

an open discussion about how we can get at this issue without distorting it with the points at hand.

Mr. McDermott's point, also, I would like to kind of give him a defense. When he talks about using an expiring tax revenue and the retort is that it is a radical departure because we fund Social Security with payroll taxes, when the government goes to redeem the bonds in the Social Security trust fund that we are now borrowing from, we are going to use moneys from general revenues to pay for it. It is not any more radical a departure than Mr. McDermott is talking about.

Now, let me ask two questions, because of all the things that aren't clear about the President's plan, there is one thing that is clear and that is that he does have a structure he has announced about the private accounts and one element of these accounts is the so-called offset or claw-back that would cut the Social Security benefits for those who refuse to open an individual account. That proposal has created a lot of confusion and misunderstanding and I want to clarify it if I can. As I understand it, this proposal would reduce your guaranteed Social Security benefit to reflect the smaller amount that you would be contributing to Social Security if you open a private account, is that correct?

Mr. BOLTEN. I believe it is, Mr. Jefferson.

Mr. JEFFERSON. Okay.

Mr. BOLTEN. I think it would be pro rata.

Mr. JEFFERSON. Right. Is it true, then, that the reduction would equal the monthly payments that could be financed if your private account had been invested at the Treasury rate, which is a real annual rate of return, which is to say it is adjusted for inflation, which is approximately 3 percent?

Mr. BOLTEN. I don't believe that is the return that is provided in Social Security——

Mr. JEFFERSON. It was just testified to by Secretary Snow that that was the amount.

Mr. BOLTEN. All right.

Mr. JEFFERSON. I think it is the amount, so let us assume that——

Mr. BOLTEN. I will accept his answer as——

Mr. JEFFERSON. All right. Does that mean that in order to come out ahead, then, that an individual who chooses to open a private account would need to earn a return at least at Treasury rate plus administration expenses? That would be correct, wouldn't it?

Mr. BOLTEN. I think so, yes.

Mr. JEFFERSON. Right. I am wondering, then, does the CBO believe that the expected—well, let me skip that question. I submit to you, then, that if an individual has to have a return of three percent, an adjusted rate of return of 3 percent, that he is going to end up at the end of the day with a benefit cut that is going to amount to around 70 percent of the benefits he would get if he left that money in the system and not invested in private accounts, and the only way he makes anything at all on it is that, somehow, he gets a return that is greater than 3.3 percent, which is really what Treasury is. He has to get a return larger than that. If he only gets what Treasury is anticipating, that would be no benefit to the per-

son and they will suffer a 7 percent reduction in their benefits. Do you disagree with that or agree with it?

Mr. BOLTEN. I think I—I am not sure I am following, but I think I do disagree. I think the detriment that—well, that there is no detriment that the investor would suffer, that the individual beneficiary would suffer from the creation of the personal accounts unless the return from the personal accounts was below the return that Social Security provides, and let me just check with my folks and see if, in fact, it is the Treasury rate of return, because my impression is that it had been lower. Okay. Well, I am confirming that you were correct, that Secretary Snow was correct. But, what that would mean is that the personal account, in order to be basically a good deal for the beneficiary, would need to beat the Treasury rate of return, which I think over almost any period of 20 years in our history—in fact, probably every 20-year period of our history—you will find that investments in a blend of stocks and bonds would provide that return.

Mr. JEFFERSON. The three percent would, in effect, be returned to the government, to the Treasury, and anything over that, the individual might be able to keep—would be able to keep. But, something about taking it out of the system, the benefit that the person would otherwise get is going to be reduced by seven percent because that is the difference between a return that—if you take the high rate of return that SSA is anticipating of 4.6 percent, only then do you get the seven percent. If you simply say that it is going to be the same as Treasury, that is no benefit to the individual and we incurred this transition cost with no benefit for the private accounts is the ultimate point I make.

Chairman THOMAS. I thank the gentleman for his time. The gentleman from Florida?

Mr. FOLEY. Thank you, Mr. Chairman. Thank you, Mr. Bolten. Have you had a chance to look through the archives when Social Security was first created to look at the assumption tables that were made when they constructed the program?

Mr. BOLTEN. I have not, but I would be interested and I have a suspicion that you have.

[Laughter.]

Mr. FOLEY. Well, I haven't. No, I haven't, but I am interested, because when you look at the longevity table back in 1935, the average age was expected to be 63.5 on your demise. Yet the SSA projected benefits either early at 62 or 65. It would seem to me it wasn't probably a very good investment to pay taxes into a fund that it was highly unlikely you would have received any of your residual based on the likelihood you would have died before collection. When I try to figure out the assumptions, and now we are seeing people living—it is amazing to me, in the seventies, Willard Scott would have maybe one person a week that hit 100 and now there are five a day, which is the joy of medicine and it is the bounty of our scientific research. But, the bottom line is, in order to provide benefits, we have to devise a new system, is that correct?

Mr. BOLTEN. Yes, I believe that is absolutely correct.

Mr. FOLEY. Now, a lot has been made today about the tax cuts. Based on, and remember again 1999 and 2000, the dramatic decline in the stock market, the lack of investor enthusiasm, the

stalling economy, coupled with September 11, had we not passed aggressive tax cuts, what would our budget look like today? What would our deficit picture look like today?

Mr. BOLTEN. I couldn't give you an exact figure, but I can tell you I think our deficit picture would look substantially worse because what led us into the fiscal hole we found ourselves in at the beginning of the previous administration, from the beginning of the previous administration, was, in fact, rapidly declining receipts as a result of the bad economy. The tax cuts were instrumental in bringing us out of that recession and ultimately restoring growth to our revenues, which after three straight years of declining revenues, we finally got the revenue growth back in 2004. We are expecting even better in 2005. I think we would be in much worse fiscal condition were it not for the tax cuts having restored growth to the economy.

Mr. FOLEY. So, it is safe to assume the people that got a per-child tax cut actually spent the money in the economy?

Mr. BOLTEN. I believe economists will tell you that they did.

Mr. FOLEY. It is safe to assume that the 15 percent capital gains structure has led to the Dow going back into the 10,800 range again?

Mr. BOLTEN. I think economists will tell you that the capital gains tax reduction and the dividend tax reduction have been crucial in promoting investment.

Mr. FOLEY. As far as the tax cuts for the top 1 percent, it is fair to assume that if that was the policy enunciated by the other side, that we just roll back the taxes, those who pay the highest taxes and those who would be asked to pay more would not receive any additional benefits by their additional contribution to the Social Security trust fund, is that correct?

Mr. BOLTEN. That is correct.

Mr. FOLEY. So, they would be asked to fill in a blank using their pre-tax income to shoulder the burden, and yet not receive an additional amount of money for that additional contribution?

Mr. BOLTEN. They would, Mr. Foley, and there is one other element I would add, and that is that as a result of the President's tax cuts, the top 1 percent pay a larger share of our total income tax take than they did before the tax cuts. Without the tax cuts, they would be paying 32.3 percent of the total income tax takes. That is just the top 1 percent in this country. After the tax cuts, that same group pays 33.7 percent of the total income tax take in this country.

Mr. FOLEY. Thank you. Thank you, Mr. Chairman.

Chairman THOMAS. I thank the gentleman. Does the gentleman from Tennessee, Mr. Tanner, wish to inquire?

Mr. TANNER. Thank you very much, Mr. Chairman, and welcome, Mr. Director. Since January of 2001, our country has been borrowing real money, hard money, at the rate of about $700 million a day. Publicly held debt has gone up $1.02 trillion, or thereabout. If you do the math, it is around $700 million a day. In this budget document you present, you anticipate another $1.3 trillion of publicly held debt accumulating for a total of over $2 trillion, $2.3 trillion in that timeframe. Would you agree with the state-

ment that we are borrowing more money faster than at any time in our Nation's history?

Mr. BOLTEN. I don't know whether that is correct, but I share your concern about that borrowing, which is why I think the spending restraint that is reflected in this budget is so important to pursue.

Mr. TANNER. Well, this is your budget. I have heard that the Members say how strong the economy has been and how we are catching on again now, and yet in this budget document you have before us, you continue to borrow a little over $700 million a day for the length of this document.

Mr. BOLTEN. There is, unfortunately, a need for continued borrowing, but absent the kind of economic growth that some of the other Members were referring to, the need for borrowing, in my judgment, would be substantially greater.

Mr. TANNER. Well, it is your budget and you continue to borrow. If the economy is weak, how bad would it be? You say it is strong and growing and vibrant because of tax cuts, and yet you continue to borrow over $700 million a day for the length of this document.

Mr. BOLTEN. Oh, I haven't——

Mr. TANNER. When are we ever going to not borrow?

Mr. BOLTEN. Mr. Tanner, I imagine that if the economy were weak, we would not be able to be on a path of reducing that deficit as a percent of our overall GDP, and so——

Mr. TANNER. Mr. Director, with all due respect, if the economy is growing and things are so good, why do we have to project continuing to borrow $700 million a day? This is a budget document where you make decisions like this, isn't it? I looked at your 2003 budget. As a percentage of GDP, the forecast then for 2005 was a 0.5 surplus. For 2006, it was a 0.7 surplus, and for 2007, a 0.8 surplus. 2 years later, in your 2005 budget submission, that had deteriorated from a 0.5 plus to a minus three in 2005, from a plus 0.7 to a minus 2.1 in 2006, and from a 0.8 to a minus 1.8 in 2007. You, by your documents, are going in the wrong direction if you see what I mean.

Mr. BOLTEN. I——

Mr. TANNER. If things are getting better, why is this picture deteriorating right in front of our eyes according to what you all give us?

Mr. BOLTEN. I do, and precisely what those earlier budgets misestimated was the rate of growth in the economy. Those estimates were made at a time when the economy was projected to grow much better than it did. We ended up being in a much longer and stickier recession than was originally projected at the time those estimates were made We now do have growth coming back into the economy and that growth is crucial in restoring our fiscal health.

Mr. TANNER. Let me get to what I really want to—if next year it deteriorates as much as it did between 2003 and 2005, I don't know, maybe we have got the wrong deal here. What is really, I think, a major concern, and it is right now, it is not years from now that we have been debating about, at the end of the last fiscal year, would you agree that foreign interest financed about 70 percent of last year's deficit?

Mr. BOLTEN. I don't know if that is accurate. Let me——

Mr. TANNER. That is pretty close. That is about right. Since October of last year, it is even higher than that. It is approaching 90 percent, foreign interest buying our publicly held debt. I can give you—that is about right, yes, sir. Now, in 2001, foreigners held about 30 percent of our publicly held debt. In 2003, it had risen to 37. It is now over 40, approaching 44 percent of our publicly held debt is held by foreign interests. Does that give you an immediate concern, and if not, why?

Mr. BOLTEN. Well, part of that is a reflection of the strength of our economy and confidence in our economy. The——

Mr. TANNER. Exactly.

Mr. BOLTEN. What is very important, then, is that we sustain that confidence in our economy of both domestic and international investors, and the way we do that is by showing fiscal discipline in the short run and dealing with our long-term unfunded liabilities in the long run.

Mr. TANNER. Yet in your budget documents, the situation is deteriorating, not increasing. Are you aware that on January 26——

Chairman THOMAS. The Chairman indicates the gentleman's time has expired.

Mr. TANNER. The Chinese minister said the U.S. dollar is no longer, in our opinion, a stable currency and that they have increased their holdings of our debt over 100 percent in the last 26 months? Let me tell you, that is the immediacy. You all can talk about Social Security in 2042 and I am telling you right now, this is an immediate problem. It could explode in our face anytime. Thank you, Mr. Chairman.

Chairman THOMAS. The Chair would urge the gentleman from Tennessee to submit that question, if he would, in writing——

Mr. TANNER. I will be glad to.

Chairman THOMAS. And would request the Director to respond in writing so that we could have a fuller examination of the issue.

[The information was not received at the time of printing.]

Chairman THOMAS. With that, does the gentleman from Texas, Mr. Brady, wish to inquire?

Mr. BRADY. Yes, Mr. Chairman. Thank you. I agree that the recipe the President is proposing for balancing the budget in getting back to where we can pay off our debt to keep this economy strong, because those two million-plus workers are now paying into Social Security, paying into Medicare, paying income taxes, helping us create new revenue.

Then the second part of that recipe is restraining spending and Congress needs to do its part. I applaud you, Mr. Director, for with the President proposing a sunset commission. Twenty-four States have similar Federal sunset—or sunset acts that look to abolish obsolete agencies and eliminate duplication. It is a very thoughtful, proven way to really create a situation where there are no sacred cows. Every agency has to prove and justify their existence and their results to America today, not just what their value was 100 years ago or 80 years ago, but do they deserve our precious tax dollars today. I am excited about that because here in the House, last fall, we showed there was strong bipartisan support for such law with over 270 votes in the House when taken to it. I think with

the President's strong support, we have got a chance to put a proven tool to work.

I am convinced in 8 years here, if Washington were a manufacturing plant, we would manufacture spending. That is what we are good at and designed to do. If we want to manufacture savings and efficiency, we have to retool the plant, and the sunset commission, the results commission, the line-item veto, I think are all tools to help us get to that point where we are making every buck really count for taxpayers. So, Mr. Director, I applaud you for that.

Mr. BOLTEN. Thank you, Mr. Brady, and thank you for your leadership on the issue. Your work, especially on the sunset commission, was basically the template for the proposals that the President has put into his budget this year and we are looking forward to working with you and a lot of other Members in getting that enacted.

Mr. BRADY. Right. Thanks. Same here, as well. In Social Security, there is some talk about just how urgent this is. I think we all recognize the baby boomers start to hit in 3 years. After that, as has been said repeatedly, for 40 years, we borrowed money from the Social Security trust fund. They are in special Treasury notes. In 2018, we start paying back those notes.

It seems to me there is some myth that that has no price to it. It seems to me in that first year, we start paying back about $18 billion or so, and then it quickly escalates to $100 billion a year, then $200 billion a year, then to $300 billion a year, and that money doesn't come from just out of the blue sky. Those dollars will compete against health care and education and veterans' issues and all that. So, as we pay that back, there is a real price in priorities to pay.

So, it seems to me we ought to heed the head of the CBO, Mr. Holtz-Eakin, who, while people freely use his numbers, forget his statement that it is very appropriate that Congress tackle Social Security right now because the problems become so urgent so fast and have a real impact on lives. Your comment?

Mr. BOLTEN. It is a very important point, Mr. Brady, and something that is overlooked is that while benefits will continue to be paid, of course, once the system goes into cash deficit, currently projected at 2018, the government still has to pay for that, make up the shortfall. We see really our deficit situation deteriorating dramatically once we hit that inflection point. Therefore, the sooner we can get to that problem, get it addressed, the better. The problem just gets harder to fix every year that goes by that we don't address it.

Mr. BRADY. Especially, as you said, at $600 billion a year. I know Congresspeople and Senators like to think our words are golden, but $600 billion a year is a little too expensive for my tastes. We should act this year. Thank you, Mr. Chairman.

Mr. BOLTEN. Thank you, sir.

Chairman THOMAS. Does the gentleman from California, Mr. Becerra, wish to inquire?

Mr. BECERRA. Thank you, Mr. Chairman. Director Bolten, thank you very much for being here with us. Before I go into the line of questioning I would like to really explore, I would like to just ask you to reexamine the President's decision to eliminate

funding for the scrapped criminal alien program, which reimburses States for the cost of incarcerating and holding for deportation immigrants who have committed crimes in this country. Without the money, the President's action will mean that it will require—the President will require cities and counties through local taxes now to absorb the cost of what is a failure of the Federal Government to enforce immigration laws until these folks can be deported who have committed crimes in this country.

So, our local jails, our State penitentiaries will be filled with individuals who, because the Federal government did not enforce immigration laws, are now stuck in what are State and county facilities, the State and county paying for them, and the Federal government, under the President's proposal to totally eliminate funding, would thereby have to absorb the entire cost. I hope that you will reconsider that as we, in fact, are debating today immigration proposals on the floor of the House.

I wanted to ask you if you will help me follow a line of thought I have. If I had a financial advisor, if I had enough money that I could pay someone to advise me on the health of my budget, my family's budget, I would think I would want that advisor to give me information about all the good and all the bad. But, as I look at your budget that you have proposed, and through the chart that you presented, you try to make a picture of what is today's economy look very rosy when, in fact, we have over the last several years accumulated the largest budget deficits that we have ever seen in this Nation's history. While the numbers may look good with some of those charts and some of those numbers, the reality is that we have never faced budget deficits larger than these.

To not include in your budget proposal the cost of privatizing Social Security, to me is something that as a financial advisor, I would never want you to do for my family budget. For you to not include the cost of extending the President's tax cuts that are geared mostly to wealthy people that will cost trillions of dollars is something I would not want you to do if you were trying to help me with my family budget. To not include the $80 billion that the President has, in essence, said that he is going to be requesting for—additional monies he will be requesting for Afghanistan and Iraq is something that I would never expect you to exclude as you talk to me about my family budget.

To me, it seems kind of odd that we are asking the American people to believe a budget document that excludes all of these various costs and makes the picture of the economy look much more rosy than it is. The question I really wanted to get to was related to Social Security and this privatization proposal. My understanding, and please correct me if I am wrong, this coming year, the Social Security system will actually have a surplus—it will spend less than it takes in—a surplus of some $160 billion, correct?

Mr. BOLTEN. That is correct.

Mr. BECERRA. That continues to add up, and fortunately, that has been adding up, so that by 2018, the Social Security surplus will amount to over $5 trillion, correct?

Mr. BOLTEN. I don't know if that is the correct figure, but there is a surplus building up in the Social Security trust fund, correct.

Mr. BECERRA. That is what the actuaries tell us. It will be over $5 trillion. Any reason to not believe the actuaries?

Mr. BOLTEN. I go with the actuaries' numbers.

Mr. BECERRA. In fact, under the actuaries' assumptions and estimates, that surplus in the Social Security trust fund will continue to grow until about the year 2027 or 2028, until it is over $6 trillion. Now, this is the question I would like to pose to you. The President in his State of the Union Address said, in 2018, Social Security will be paying out more than it takes in, and in every year afterward will bring a new shortfall bigger than the year before. In the year 2027, the government will somehow have to come up with an extra $200 billion to keep the system afloat. He thereafter uses the word collapsing to talk about Social Security. How can a system that in 2018, the year the President mentions, will have a shortfall—have a $5 trillion surplus be considered to be in shortfall, and how could a system that in the year 2027, when the President says will somehow have to find it to keep it afloat, will have over $6 trillion in surplus?

Mr. BOLTEN. Well, the numbers that the President was referring to and—I think the right way to look at it is cash in and cash out.

Mr. BECERRA. Okay. Then what you are saying is we should not take into account all the money that is coming in today that the President is planning to use out of Social Security's surplus for other than Social Security purposes.

Mr. BOLTEN. No, no, no. The——

Mr. BECERRA. Well, for——

Mr. BOLTEN. That money is going into the trust fund.

Mr. BECERRA. Okay. If it is there, why can't we count it in the year 2018? That is what it is supposed to be for, is it not?

Mr. BOLTEN. Absolutely, and that is why——

Mr. BECERRA. Okay. Then why not include it in that calculation?

Mr. BOLTEN. If I may for the record, although if I may correct one thing, Mr. Becerra, at the outset, you suggested that our budget documents do not reflect the effects of the President's tax cuts or the $81 billion supplemental that is forthcoming. Our budget documents——

Mr. BECERRA. You put it in the baseline, which hides the actual effects of the tax cuts——

Mr. BOLTEN. Our documents——

Mr. BECERRA. Which is a very clever way of trying to make the tax cuts look like they cost a lot less.

Chairman THOMAS. The gentleman's time has expired.

Mr. BECERRA. Thank you, Mr. Chairman.

Mr. BOLTEN. The documents do reflect that, Mr. Becerra.

Chairman THOMAS. The Committee will provide documents and perhaps the administration might oblige, as well, in focusing on the front-loading that began to occur with the increase in the payroll tax beyond the immediate needs in 1983. The paper that is out there that will begin to be redeemed in 2018, because the then-current income from the income tax is not adequate, that is the 2018 point. The 2042 is when the paper that needs to be redeemed will be exhausted——

Mr. BOLTEN. Will all run out.

Chairman THOMAS. Which was brought in to try to maintain the 100 percent payment, and that is why it kicks down to a determined less than 100 percent. That does need to be illustrated so people understand the current structure and the near future structure based upon decisions made in 1983, both to increase the payroll tax and to extend age. Does the gentleman from Wisconsin, Mr. Ryan, wish to inquire?

Mr. RYAN. I do. Thank you, Mr. Chairman. Let me just follow up on that point. I think it sort of puts a false perception out there that in 2018, we are going to have $5 trillion of surplus sitting in a bank account somewhere. Let me just ask you this, Mr. Bolten. Will we have that $5 trillion? Where will that $5 trillion be?

Mr. BOLTEN. It is in the form of——

Mr. RYAN. An IOU.

Mr. BOLTEN. Obligations from the Treasury. It is an IOU——

Mr. RYAN. So, there is no cash sitting there in a vault or tradable bonds or stocks. We will have to either borrow more money, raise taxes, or cut spending to come up with that $5 trillion surplus, correct?

Mr. BOLTEN. Absolutely correct.

Mr. RYAN. That is important to note. The idea that there is all of a sudden a big cash surplus to tap into is just not correct. I think a good way of looking at it is if I take money out of my right pocket, spend it, and then put an IOU to myself back in my left pocket, that is essentially what it is. I have money that is out there. I don't have any new purchasing power, and I just have an IOU that I will have to find more money somewhere else to pay for. So, the idea that all of a sudden we don't have to worry about this program collapsing for 37 years is really just not accurate.

I want to get on to some budget reforms. Mr. Bolten, you and I have talked about budget process reform quite a bit in the last few years. I just wanted to see if you could explain or elaborate to me these new enforcement mechanisms you are talking about. Particularly how does the new enforcement mechanism to control long-term unfunded obligations work, and then how do you propose doing a line-item veto that meets constitutional muster?

Mr. BOLTEN. I will start with the latter. The administration has proposed before a line-item veto that we believe would pass constitutional muster. It would be statutory. It would basically be a deferral of spending by the President that has been enacted by the Congress. There is no guarantee it would be constitutional. We believe it would pass constitutional muster and are interested to work with the Congress on its enactment or some other line-item veto mechanism. We are not stuck on that one in particular, but we do think it is important that the President have the authority to step into some of these big appropriations bills and take out some of the items that would not pass on their own.

Mr. RYAN. Deferral in that you just won't send the money out.

Mr. BOLTEN. Right.

Mr. RYAN. You will just hang onto the money in the accounts and you will have the statutory authority to do that. What happens at the end of the year? It goes back? What happens at the end of the year in those accounts where you defer the money?

Mr. BOLTEN. Then the money would just expire——

Mr. RYAN. Okay.

Mr. BOLTEN. So, the power would be effective.

Mr. RYAN. Your lawyers are telling you that that ought to pass muster——

Mr. BOLTEN. They believe it would pass constitutional muster. As I said, there is no guarantee of that and if somebody has a better idea, we would be happy to entertain it.

Mr. RYAN. The one thing I think you ought to take a look at that we have discussed is just an enhanced recision power, not necessarily in place of this deferral idea, but maybe in addition to, which is an expedited procedure whereby the President can pull spending items out of a bill, send it back to Congress for an up or down vote, just like trade agreements where you have a trigger where you can require a vote that takes place in a certain fast period of time, where we have to vote on these individual projects that if we voted on these things alone, stand alone, probably wouldn't see the light of day, or a package of these things. So, I would encourage you to take a look at that.

Mr. BOLTEN. A very interesting proposal and we would like to work with you on it.

Mr. RYAN. The unfunded obligations, I am just curious, how does that work?

Mr. BOLTEN. If I may, I will respond to you on the record with the details of that. The objective is one that I think you have been after for some time, which is to ensure that when Members make proposals and the Congress considers proposals that increase the long-term unfunded obligation, even though they are outside the budget window, if they are outside the budget window, they often escape budget enforcement rules. We want to propose a set of rules that captures those and charges the increase in the long-term unfunded obligation in the current budget.

Mr. RYAN. In a present value form?

Mr. BOLTEN. Yes.

Mr. RYAN. Yes. Excellent. Thank you.

Chairman THOMAS. Does the gentleman from Texas, Mr. Doggett, wish to inquire?

Mr. DOGGETT. Thank you, Mr. Chairman. Mr. Bolten, I gather you agree with the President's estimate that the year 2018 will be the first year in which Social Security, under current law, will pay out more than it takes in?

Mr. BOLTEN. That is the Social Security actuaries' estimate, yes.

Mr. DOGGETT. If we adopt the privatization principles for Social Security that the President announced in the State of the Union Address, that date will be accelerated to the year 2012, will it not?

Mr. BOLTEN. I don't know what the acceleration might be, but the important part——

Mr. DOGGETT. You haven't calculated that yet?

Mr. BOLTEN. I have not.

Mr. DOGGETT. Well, certainly if you take money out of the Social Security trust fund instead of putting money into it, you will certainly have this phenomenon of Social Security paying out more than it takes in occur at an earlier date, won't you?

Mr. BOLTEN. It depends on how the money is accounted for, but the important thing——

Mr. DOGGETT. I see. It depends on what accounting tools you use.

Mr. BOLTEN. The important part of the personal accounts is that if they are part of a comprehensive system, they would prevent the ultimate—they would prevent the reaching of the ultimate insolvency date, which is the key element here.

Mr. DOGGETT. Yes, sir. As far as the changes to benefit calculations that you feel are necessary by changing wage indexing, isn't that based on the basic premise that Social Security benefits are too high today and they are getting higher?

Mr. BOLTEN. The administration has not adopted any specific reform that——

Mr. DOGGETT. You support that though, don't you?

Mr. BOLTEN. The administration has not adopted any specific form of——

Mr. DOGGETT. Well didn't the President call that a good blueprint to use this wage indexing approach?

Mr. BOLTEN. He mentioned it——

Mr. DOGGETT. Yes, sir, he mentioned it——

Mr. BOLTEN. As one of the possible ways——

Mr. DOGGETT. He used the term "a good blueprint" to describe it and that is based on the assumption that the benefits that retirees are getting today from Social Security are too high and they are scheduled to go even higher.

Mr. BOLTEN. Well, the important element here is that Social Security is currently promising benefits it cannot afford to pay.

Mr. DOGGETT. So, the administration basically thinks Social Security benefits are too high today and are scheduled to go even higher and you want to reduce them. Let me ask you specifically, as it relates to this privatization plan, if you disagree with the statements that White House Senior Official, I guess it is Peter Wehner, made in his January 3 e-mail, that as you know has gotten a lot of attention, where he said if we borrow $1 to $2 trillion to cover transition costs for personal savings accounts and make no changes to wage indexing, the very thing I was asking you about, we will have borrowed trillions and will still confront more than $10 trillion in unfunded liabilities. This could easily cause an economic chain reaction, the markets go south, interest rates go up, and the economy stalls out. Do you agree with Peter about that?

Mr. BOLTEN. I don't have a view on his remarks. I have not——

Mr. DOGGETT. You don't have an opinion? You have heard this or you have read this before, you know about this——

Mr. BOLTEN. Actually, I have not read it, but it actually was referred to by one of your colleagues——

Mr. DOGGETT. I see. You don't have an opinion one way or the other on this?

Mr. BOLTEN. Not on Mr. Wehner's——

Mr. DOGGETT. The CBO, sometimes called nonpartisan, all appointed by Republicans, has come up with a risk-adjusted return that they say is the better approach to evaluate these privatization accounts. I guess the first question I would have for you is, the administration has done a lot of talking around the country about ev-

erything that people are going to get under this privatization account, but it has been pretty quiet about what they are going to lose. If someone gets a dollar put into a private account they lose a dollar in their guaranteed Social Security account, don't they?

Mr. BOLTEN. Yes.

Mr. DOGGETT. Okay. The question is do they come out better or do they come out worse? If you take the calculations that the CBO did about the risk-adjusted return, and you consider the administrative costs associated with these private plans, you would call it a claw-back, you can call it an offset, but actually the private account holder, according to CBO, actually comes out worse than if they stick with the traditional Social Security plan and a guaranteed benefit.

Mr. BOLTEN. I haven't seen the CBO analysis, but I would be inclined, based on your description, to disagree with it, because I think that personal accounts do offer an opportunity for a much better return than can be offered by whatever Treasury bill——

Mr. DOGGETT. If the nonpartisan CBO appointed by Republicans says otherwise, you just disagree with that?

Mr. BOLTEN. If it is as you described, I do disagree with it and I think history disagrees with it, too, because there——

Mr. DOGGETT. One quick non-Social Security question, in your budget, as you said, there are decisions that have to be made that are painful, but I gather one of the painful decisions this administration made, was that you are opposed to continuing the deduction for State and local taxes that is in this year's bill. It is not in your budget.

Chairman THOMAS. The gentleman's time has expired. You can respond in writing if you wish to——

Mr. DOGGETT. Just a yes or no?

Chairman THOMAS. The Chair would indicate that the CBO has modeled the Social Security Commission Plan 2 that they used to make estimates off of, not the President's plan. There may be some similarities between the President's plan and the Social Security Commission Model 2, but they are not identical, so that the gentleman's statement is narrowly inaccurate. In terms of a general reflection, we will have to see, because I am quite sure someone will ask the CBO to do the President's plan.

Mr. DOGGETT. Well, I am sure they will, and I believe that risk-adjusted return is what they do to evaluate Railroad Retirement and——

Chairman THOMAS. I understand. But, the gentleman indicated the President's plan had been modeled by CBO and——

Mr. DOGGETT. The concept in the President's plan, since——

Chairman THOMAS. It was the Social Security Commission Plan 2——

Mr. DOGGETT. Doesn't have a plan, or the Secretary of Treasury.

Chairman THOMAS. We have just got to keep the record accurate, that is all. The gentleman from Georgia, Mr. Linder.

Mr. LINDER. Thank you, Mr. Chairman. Mr. Bolten, nice to see you again. Thank you for being here.

Mr. BOLTEN. Likewise, sir.

Mr. LINDER. You said that 34 percent of the top 1 percent of income earners are going to pay 34 percent of all the taxes after the tax cut?

Mr. BOLTEN. Yes, sir, 33.7 percent.

Mr. LINDER. Do you know what they paid 25 years ago?

Mr. BOLTEN. I do not.

Mr. LINDER. Seventeen percent, when the top marginal tax rate was 70 percent. It is becoming more and more progressive every time we cut taxes. There is something else to remember about 25 years ago. We are hearing a lot about all we need to do is tax those rich people and it can fix all the problems here today, but 25 years ago, the prime rate was 21 percent. Home mortgages were 17 percent. Inflation was 14 percent. Unemployment was double digits. The economy was $2.5 trillion. President Reagan dramatically reduced the tax burden.

10 years after that, interest rates came down 125 basis points a year, mortgage rates were down, the economy had doubled in size, and the contributions to the Treasury went from $519 billion to $1.054 trillion. It seems to work. It worked in 1921. It worked in 1961. It worked in 1981. As John Kennedy said, a rising tide lifts all boats. You had more people working owing to a good economy. You had more money coming into the Treasury. I think you are on the right course and I look forward to helping you.

I would like to make one other point. You and I have talked about the tax reform proposal that I have been working on. Had we had it in place for the last 4 years, we would have had increased revenues in 14 out of 16 of those quarters. Thank you, Mr. Chairman.

Mr. BOLTEN. Thank you, Mr. Linder.

Chairman THOMAS. I thank the gentleman very much for the time. We are attempting to move the Director out by 5:00. I am doing everything I can to assure that, but I want to make sure Members are heard if they so desire. Does the gentleman from North Dakota wish to inquire?

Mr. POMEROY. I thank the Chairman. Mr. Director, you had a wonderful story here today, but then again, you always have a wonderful story. In fact, it has been kind of the trend of the administration. I had to actually quote from an address made by the President to the Congress, his first State of the Union, our joint session, I guess it was titled. "To make sure retirement savings of America's seniors are not diverted into any other program, my budget protects all $2.6 trillion of the Social Security surplus for Social Security and for Social Security alone," unquote. Well, we know, of course, that every dollar coming in for Social Security is being spent on unrelated government programs, and, in fact, you as Director have been a record setter—the biggest deficit in the history of the country last year. In fact, the year before that was the biggest. You beat that record. This year, you beat your record from last year.

Although you are telling us things are going to get better, there are some very notable omissions to the budget you have told us about, including you estimate holding discretionary spending at level levels. Among other things, you break the farm bill and so many other areas that I believe on a bipartisan basis will be re-

jected. You include no spending for Iraq and Afghanistan, even though you have admitted several times today you had $81 billion additional. That would push the total tab over $300 billion, none of which has ever been included in one of your budgets. You admit the cost of Social Security borrowing that you are going to have to do to privatize the system, even though you admit that that is better than three-quarters of a trillion dollars. You don't have any money in there for fixing the AMT, although you indicate that that is something certainly needing attention. So, I expect you are going to do her again. I expect you are going to break your own record on these deficits in light of the budget you have proposed with the liabilities that you have omitted. I would like to move to the discussion on retirement savings and——

Mr. BOLTEN. Mr. Pomeroy——

Mr. POMEROY. We were talking about——

Mr. BOLTEN. Mr. Pomeroy, may I take a moment to correct——

Mr. POMEROY. Well, regrettably not. Now, maybe the Chairman will give you additional leave, but I only have 5 minutes to work with.

Mr. BOLTEN. Understood. I will correct for the record.

Mr. POMEROY. We have been talking about the top 1 percent back at—and we will probably be talking about them a good bit more as time goes on, but I want to talk about from an income security and retirement standpoint the modest income households, the family of four making $40,000, $50,000, trying to save for retirement. We have a feature in the Code now, it is a savers' credit, and it gives them a matching credit, tax credit, for what they are putting into qualifying savings accounts. There have been five million new accounts established in families that make the qualification, the income qualification to use this.

It is not included in your budget and it goes away at the end of this year. You are recommending to Congress that we, in essence, let the modest household retirement savings effort lapse. On the other hand, you offer something quite different, these lifetime savings accounts, and retirement savings accounts on top of that which would allow $5,000 per individual after tax to go in the lifetime savings accounts for every Member of the family. Put it in, pull it out whenever you want. Retirement savings accounts, $5,000 on top of that. A family of four could conceivably tax shelter nearly $50,000 annually if they had that kind of aftertax income.

So, in my view, the modest income household, the one that is having the hardest time saving, they may say to you, but we can't afford to save. We don't have any discretionary savings left, income left. You say, don't worry. Now you can save $5,000 in lifetime savings accounts per individual, $5,000 in retirement savings. It is, as you know, a savings tool that will be beneficial to affluent households, not at all beneficial to modest income households. To have you allow the lapse of the credit that helps modest income households while advancing this other one is, I believe, absolutely upside down retirement policy.

If there is only one thing more that you could do to screw this up, you advance it with your Social Security plan, because Social Security offers a guaranteed retirement annuity. It is going to pay every month for life. It is going to adjust for inflation. The average

Social Security check is $834. Now, how much risk do you want to add to an amount that is basically subsistence household income, and that is the average, so for some, it is lower. Instead, you move into that. You reduce the inflation adjustment and you add risk into Social Security. For the modest income household, no additional help in savings and less by way of protection with Social Security.

Chairman THOMAS. The gentleman's time has expired.

Mr. POMEROY. I yield back.

Chairman THOMAS. That may be a request for a written response or rhetorical, I don't know which. Do you want a written response?

Mr. POMEROY. However the Director would like to respond.

Chairman THOMAS. Great. Does the gentleman from Colorado, Mr. Beauprez, wish to be recognized?

Mr. BEAUPREZ. Thank you, Mr. Chairman. It is good to see you, Mr. Bolten. You have been accused of a lot of things here today, in fact, recently. I will accuse you and the administration of something else, and that is for doing a pretty darn good job. My recollection is you inherited a recession that was well underway and deepening, Severe Acute Respiratory Syndrome, an event on 9/11/2001, that frankly, I believe, would have crippled and probably collapsed most any other nation in the world. Here we sit debating over what is the rate of recovery and how much recovery and on and on and on. The fact that we are in recovery is a tribute to the policies, however accidental or on purpose you have managed to put them in place. I think a job well done needs to be passed on to the administration, and I will tell you, my folks back home in the Seventh District in Colorado recognize that we are on the right track and are glad of it. So, my compliments to all in the administration, and since you are the one in front of us today, to you specifically.

We have heard today and also yesterday a lot of torturing of words. Whether it is personal or private, problem or crisis, insolvent or bankrupt, whether the system is awash in cash or maybe just fine, thank you, we have heard is it 2042 or 2052, all of those are probably going to be debated for a long, long time. As a former banker, I will tell you a couple of things that I think are pretty clear, though. When I hear unfunded liability, you get my attention, and that is exactly what we have. We hear all this pretense that somehow we are not going to pay benefits. We are going to pay. We have promised that to not only this generation, but future generations, and they have got a right to expect it. The challenge in front of us is how. How do we meet that large of a liability?

I kind of focus-grouped this back home with four people I know pretty well, my four children. They are all going to retire right around that 2042 year, just before it or just after it. They are quite concerned. They understand the concept of an unfunded liability and they know very well that the money that went into the trust fund, of which they are paying right now in their wages, isn't there. Their name is not on any of it. It is a promise from the Federal government, a promise they would like to see fulfilled, but they don't understand exactly how that is going to happen because they heard the same thing I heard from the SSA, that the system

as it currently exists is unsustainable. That is the challenge in front of us, is it not?

Mr. BOLTEN. It is, indeed.

Mr. BEAUPREZ. So, what do we do about it? I think there ought to be generational fairness. I think what my mother is currently enjoying, receiving a check every month from Social Security, I think we ought to be able to promise that to the current generation—mine. I think we ought to also be able to promise that to my children's generation and my grandson's, for that matter, and those that come after. So, how do we do it? We just heard a little bit ago that apparently Einstein had it wrong. The compound interest isn't the greatest force in the world, that somehow by setting up these personal accounts and doing the obvious, investing them in very low-risk, sound, safe investments, that somehow it isn't going to work. It does work, doesn't it?

Mr. BOLTEN. It does indeed, sir.

Mr. BEAUPREZ. In fact, we have got a whole lot of proposals floating around the Hill right now, and we will see which one or ones or combinations thereof end up becoming the bill we try to pass, but if I were to suggest that a relatively low-income worker making about $20,000 a year could put away a decent little amount, part of what they are putting away right now in an account at a predictable rate of interest, like four or 4.5 percent, and perhaps exceed their promised Social Security benefit on a monthly basis by 75, 80 percent, that would seem to me to be pretty substantial. My children, their generations get that. I commend you, Mr. Bolten, and the President for bringing this forward. I look forward to working with you to make it happy. Question, simply, how powerful is compound interest? Einstein is dead and gone. We will ask the living.

Mr. BOLTEN. I can't improve on Einstein, just to quote him, saying it is, in fact, the most powerful force we know, and——

Mr. BEAUPREZ. Wouldn't that be the—the challenge is, where is the money going to come from to pay this promised benefit? The money will come from increasing the earning power, creating the wealth to pay the benefit.

Mr. BOLTEN. A substantial part will come that way, and even beyond that, just allowing people to own some of their own retirement, pass it on to their heirs, and also put it in a place where it is not easy for the government to get at it and spend it——

Mr. BEAUPREZ. Very well said. That is why my immigrant grandfather came here for, was to own something.

Chairman THOMAS. The gentleman's time has expired.

Mr. BEAUPREZ. I yield back. Thank you, Mr. Chairman.

Mr. BOLTEN. Thank you, Mr. Beauprez.

Chairman THOMAS. Does the gentlewoman from Ohio wish to inquire?

Ms. TUBBS JONES. Thank you, Mr. Chairman. Sir, how are you? Good. Let us pick up where he just left off. People want to own some of their own retirement. The privatized accounts that are being proposed by the President of the United States, as currently proposed, will be required to be placed into an annuity and the only way I could access it is if I meet a means test, correct?

Mr. BOLTEN. You know——

Ms. TUBBS JONES. That is the testimony of Mr. Snow yesterday, just in case you——

Mr. BOLTEN. All right, but I——

Ms. TUBBS JONES. Want to be consistent with it.

Mr. BOLTEN. I think that is upon retirement, yes, that——

Ms. TUBBS JONES. Correct. But, prior to retirement, you have no entitlement to it, sir. All it is is on a piece of paper saying that it is money that you have in an account. So, what I am talking about is upon retirement, I then have to place my money in an annuity unless I can meet a means test, is that correct?

Mr. BOLTEN. Some of the proposals I have seen have said that, yes, you would——

Ms. TUBBS JONES. Right, and you have——

Mr. BOLTEN. In order to ensure that you take it out over a reasonable period of time.

Ms. TUBBS JONES. I understand the concept, but the reality is it must be put into an annuity because you don't believe that people can take a lump sum and invest it and have money down the line. You are not sure that they are capable of doing that, and to assure that they have a retirement account, you are forcing them into an annuity, is that correct, sir?

Mr. BOLTEN. Some of the proposals I have seen have had that element, yes.

Ms. TUBBS JONES. Yes. You and your colleagues have been good at trying to compare this program, these privatized accounts, to a TSP that Members of Congress and other people who work for government have access to, is that correct?

Mr. BOLTEN. Most people have suggested that the private account—the personal accounts, sorry——

Ms. TUBBS JONES. I like the word——

Mr. BOLTEN. Be structured—yes, I understand——

Ms. TUBBS JONES. Similar.

Mr. BOLTEN. But that the personal accounts be structured in a way similar to the TSP.

Ms. TUBBS JONES. The Thrift Savings Accounts, when I retire—in fact, I don't have to wait until I retire. I can take my Thrift Savings if I take a penalty. But, assume I wait until I retire. I am not required to put that money into an annuity, sir, am I?

Mr. BOLTEN. I don't believe so.

Ms. TUBBS JONES. I would suggest that you stop representing, you and the President and everybody else in favor of these accounts, representing that they are similar. In fact, with a Thrift Savings Account, there is no means test. My name is on it and I can pick it up anytime I want to or at retirement, correct, sir?

Mr. BOLTEN. I believe so.

Ms. TUBBS JONES. Okay. Thank you. Let me also—I am so pleased that so many people are worried about working Americans. I am worried about the people in my Congressional district who are not working. The conversation is there is 5.5 percent unemployment. There are areas in my Congressional district where the unemployment rate is at 13 percent, and all of those people who are unemployed would love to have a job where they could pay taxes and raise their children. In fact, all the people in my Congressional district are looking at the budget, and you are part of this budget,

or you can represent some of the budget that the President just came out with the other day, right? I am noting for my seniors in Ohio, there are cuts of $45 billion to Medicaid. You are aware that many States are struggling to pay their share of Medicaid, are you not, sir?

Mr. BOLTEN. I am aware that States are struggling and that is the reason why we are proposing some very fundamental reforms to Medicaid that would give governors more flexibility in using the Medicaid dollars——

Ms. TUBBS JONES. But, the budget cuts $45 billion, does it not?

Mr. BOLTEN. The budget seeks savings in the net range of $45 billion, reducing the growth——

Ms. TUBBS JONES. You call it savings in the net range and I call it cuts. Let us move on. It also freezes——

Mr. BOLTEN. Ms. Tubbs Jones——

Ms. TUBBS JONES. Child care funding for 5 years. It also will cause a termination of 300,000 low-income children by 2002 [sic]. It also eliminates the TRIO's program's Upward Bound, Talent Search, Gear Up, and there is one focused on veterans a la TRIO. It lowers Pell grants that had been raised and now lowered and lowers the eligibility of young people. All of this programming that would help people who want to go to work, who want to get out of poverty to be a part of a private account are struck by the budget—and that is not the budget, but you have the budget—that has been proposed over the next 10 years for people in America.

All I am saying to you is, you need to speak truth. You need to represent to the American people that with tax cuts and with various spending on the war in Iraq and the war in Afghanistan, the dollars that are available to do programming to keep the safety net going for folks on Social Security, even those that are going to be 54, 11 months, and 29 days who are locked out of your retirement program, as you propose it, are going to have a problem. Thank you, Mr. Chairman.

Chairman THOMAS. The gentlewoman's time has expired and the Chair would indicate to the gentleman from Connecticut and the gentleman from Indiana that the gentlewoman from Pennsylvania has the remainder of the time prior to the Committee adjourning unless she wishes to share it with anyone. The Chair recognizes the gentlewoman from Pennsylvania.

Ms. HART. I am actually tempted to allow the director to use all my time to answer the questions that my colleagues on the other side of the aisle didn't allow him to answer, if you would like to use the first 30 seconds.

[Laughter.]

Mr. BOLTEN. I would gladly take those 30 seconds to say a couple of things. First of all, when Ms. Tubbs Jones talked about Medicaid, we need to understand that this is a program that is growing at a rate of 7.4 percent per year in our projections, and what we are proposing to do is reduce that rate of growth down to 7.2 percent. But, the most important thing is that we reform the program so that the Governors have the flexibility to make effective use of all that additional money we are, in fact, putting out.

Ms. HART. Are you satisfied?

Mr. BOLTEN. No, but I think——

[Laughter.]

Ms. HART. Okay.

Mr. BOLTEN. But, I will have an opportunity to be satisfied in the record, I am sure.

Ms. HART. I am glad to hear that. I appreciate you being here and doing this marathon thing with us and I appreciate the time from the Chairman. I will have some time that I will give to Mr. Chocola, so I am going to go into my statement-slash-question pretty quickly, and that is, first of all, the one phrase that I have not heard, or maybe I missed it today, is nest egg. I keep hearing suggestions that people can't get into that nest egg that would be their Social Security personal retirement account any time they want, but if you have a nest egg, I certainly hope you don't want to break into it any time you want because it is still growing. Isn't the goal of having a nest egg or a personal retirement account to wait until you are retired?

Mr. BOLTEN. It is, indeed, and it is supposed to be used for retirement, which is why there are the—many of the proposals have the provisions that Ms. Tubbs Jones was referring to.

Ms. HART. The last time I looked, a couple of my retirement accounts actually have a penalty if I withdraw early for that very reason. The goal is to incentivize all of the people who are in these programs to leave the money there so it grows. That is the whole point. The money that would go into Social Security as it is currently wouldn't be able to be accessed either before retirement, right?

Mr. BOLTEN. True.

Ms. HART. So, we wouldn't be changing anything at all as far as a person, a worker's access to that Social Security money if we——

Mr. BOLTEN. Well, actually, we would be changing something very important, because if a worker today dies before they retire, they lose all of that money that they have been paying into Social Security, whereas a personal account that is in the ownership of that person, they can pass that on to their heirs.

Ms. HART. So, it is actually way better in that your name is on it. All of those dollars you pay in over all those years are yours.

Mr. BOLTEN. It is a real ownership interest and the government cannot spend it.

Ms. HART. I am very pleased to hear that, and actually, since I am sort of on the cusp of the people who might not get any money, I am really happy to hear about this. Not only that, just one quick thing. I was in the airport coming here the other day and a 60-year-old Transportation Security Administration worker stopped me and said, "Make sure you get that personal retirement account passed." I will now yield my time to Mr. Chocola.

Mr. CHOCOLA. I thank the gentlewoman for yielding. Director Bolten, thanks for being here. Very quickly, in the spirit of having the opportunity to answer questions that you were not given the opportunity to answer, you were asked previously about the difference between the personal and private, and I think you were going to explain why you don't think this is a private program and I would be interested in your answer.

Mr. BOLTEN. Thank you for giving me that opportunity. A private account would be one that is simply an investment that you control on your own. This is a part of your fundamental retirement. Therefore, the TSP that I was discussing with some of your colleagues is the right kind of model in which the government is actually managing your account and ensuring that the investments are made in what are broadly considered safe and secure investments and that you can't be using the money to gamble or something like that. So, it is not a privatization of the Social Security system. It is merely within that system the creation of a personal account that you can own and you can direct it toward one of several approved options.

Mr. CHOCOLA. I see we are running out of time. I thank the gentlewoman again for yielding, and Mr. Chairman, I yield back.

Chairman THOMAS. If the gentlewoman would yield the remainder of her time, the Chair would thank the Director and indicate—the gentleman from New York wishes to make a comment.

Mr. RANGEL. Yes. I want to thank the Director. You really acted like you enjoyed being here today and that makes it easier for us.

[Laughter.]

Mr. BOLTEN. It is always an honor to appear before you, sir.

Chairman THOMAS. The Chair thanks the gentleman for the gracious time. Except for the intervention of the bills, we would have been able to have every Member inquire. That is always the Chair's goal. If there are no further questions, the Committee stands adjourned.

[Whereupon, at 5:00 p.m., the hearing was adjourned.]

[Questions submitted from Mr. Hulshof, Mr. Stark, Mr. Cardin, Mr. McDermott, and Mr. Doggett to the Honorable Joshua B. Bolten, and his responses follow:]

Question from Representative Kenny C. Hulshof to the Honorable Joshua B. Bolten

Question: Director Bolten, thank you for your testimony today. After reviewing the President's budget submission, I am concerned that the Administration's proposal relating to Power Marketing Administrations, specifically the Southwestern Power Administration, will adversely affect over 400,000 of my constituents that reside in Missouri's Ninth District. The rate increases that could result from these changes would undoubtedly be passed on to consumers. While I understand the Administration's motives, I fear that power consumers in rural areas of my district will be unduly burdened by this change. Could you please elaborate on this proposal and hopefully alleviate my fears regarding the impact this could have on those I represent in Congress?

Answer: The budget proposes to very gradually, over several years, increase customer rates closer to what other wholesalers in the region charge for their power. The proposal's effect would be moderate because, in most states where power wholesalers buy PMA power, less then five percent of their total power is bought from a PMA. The PMA power is blended with other power either generated or purchased by the customer and in turn sold to the retail consumer. The blending of the power has the effect of diluting the impact that a rate change might have on the retail consumer. In addition, because the PMA power sold is typically such a small portion of the total retail power sold, the impact of a change is further limited. As a result, most households served by a customer receiving PMA power would see an increase of about $0.08 per month in 2006 and $0.38 per month in 2007.

I also should mention several other points about the Administration's proposal. The intent is to allow rate changes only when existing contracts can be modified. Under conditions where contracts have not expired or do not allow for a change, no

changes would be made. In addition, under the proposal, the rates would change very gradually and as fairly as possible to avoid some consumers but not others bearing an undue share of the change. Finally, the Administration in no case would allow rates to increase by more than 20% in a year. In the instance of your constituents, because about five percent of the power sold in Missouri is from a PMA, I do not believe rate changes would be near the 20% limit. Given the modest proposed increase that would gradually recapture some of the subsidies extended to PMAs over the years, and the overriding need to reduce the deficit, I was disappointed that the recent Budget Resolution did not assume the proposal.

Questions from Representative Fortney Pete Stark to the Honorable Joshua B. Bolten

Question: The budget spends $51 billion/10 on tax breaks for health proposals that primarily benefit people with higher incomes (i.e., the deduction for high-deductible policy premiums and credits to small business owners), while cutting $60 billion in Medicaid funds that serve the most poor and vulnerable people. How do you justify this reverse Robinhood action?

Answer: The tax policies you mention benefit individuals of all incomes, not just those at the upper end of the income range. In addition to these policies, the 2006 Budget includes a Health Insurance Tax Credit of $74 billion over 10 years targeted to low-income individuals and families that would make health insurance more affordable and accessible. This also includes $4 billion over 10 years in grants to states to encourage the development of purchasing pools to make coverage more accessible.

The Budget includes $15 billion over 10 years in new Medicaid and SCHIP spending to extend coverage. The reductions that you mention refer to the Medicaid program integrity proposals included in the Budget. The FY 2006 Budget includes a broad package of program integrity proposals designed to restore the credibility of the Federal/State matching system and address other payment concerns. These proposals reduce payment inefficiencies, promote personal responsibility for long term care expenses, and curb questionable financing practices that have been used by a number of States to avoid the legally determined State matching funds requirements. Even with these changes, Medicaid and SCHIP's future spending is expected to increase at a robust growth rate of over 7 percent over 10 years.

Question: Can you show me where in the budget the 10-year estimate is for Medicare spending for Part D (the new drug coverage that starts next year)? There is a five-year number ($344.5 billion) on page 395 of "Analytical Perspectives." What is the ten-year number? It seems to me that this is what happens when the pharmaceutical industry is given a blank check from which to draw taxpayer funds. Are you comfortable with this level of spending for such a meager benefit? What, if anything, would the Administration support to lower drug prices?

Answer: The Budget does not report 10-year estimates for the Medicare prescription drug benefit or any other program, but does reflect $343.3 billion in spending for the Medicare prescription drug benefit and transitional drug assistance program from 2006 to 2010. The Administration is working assiduously to implement the drug benefit on January 1, 2006, and expects that private prescription drug plans participating in the program will be successful in ensuring that Medicare and its beneficiaries get the best prices available for prescription drugs. We have seen no evidence that further federal government intervention will likely produce additional savings.

The five-year (2006–2010) net cost of the drug benefit (as on p. 395 of Analytical Perspectives) is $343.3 billion. The figure of $344.5 billion is actually a six-year cost, as it includes the years 2005–2010. The Office of the Actuary at the Centers for Medicare and Medicaid Services (OACT) originally estimated the total net cost of the new Medicare drug benefit at $511 billion for the ten-year window of fiscal years 2004–2013.

OACT recently re-estimated the cost of the drug benefit, both for the 2004–2013 period and the FY 2006–2015 budget window. OACT's current estimate of the FY 2004–2013 cost is very similar to its original estimate: they found the FY 2004–2013 net cost to be an estimated $518 billion. The net cost from FY 2006–2015 is estimated to be $724 billion. The table below lays out the original MMA estimates and current estimates for the FY 2004–2013 and FY 2006–2015 budget windows:

Medicare Prescription Drug Benefit Outlays Comparison of MMA Scoring to 2006 President's Budget Estimates ($ in billions)

MMA Estimates FY 2006 PB

		Estimates	
	2004–2013	**2004–2013**	**2006–2015**
Gross benefit outlays	820	849	1,192
Premium receipts	−102	−102	−145
Receipts from States	−85	−97	−134
Net Medicare Rx outlays	634	650	913
Net Medicare cost	−123	−132	−189
Net Rx benefit outlays	**511**	**418**	**724**

Source: CMS, Office of the Actuary

The new, voluntary Part D benefit offers assistance to all Medicare beneficiaries who wish to enroll. The benefit targets extra assistance to low-income beneficiaries, many of whom will pay no premium and face only nominal cost-sharing. In addition, the Part D benefit ensures that every beneficiary who enrolls is protected against very high drug spending. We would also note that the Medicare Modernization Act includes incentives for employers to continue offering drug coverage to their retirees. For these reasons, the Administration thinks it is inappropriate and inaccurate to refer to the Medicare drug benefit as meager.

The Administration believes that the structure of the Part D benefit—where private health plans will compete to offer affordable drug coverage to Medicare beneficiaries—is the best way to moderate drug prices.

In a January 23, 2004 letter to the Senate Majority Leader, the Congressional Budget Office said that striking the non-interference provision (the one that prohibits the Secretary from negotiating Medicare drug prices) would:

> have a negligible effect on federal spending because CBO estimates that substantial savings will be obtained by the private plans and that the Secretary would not be able to negotiate prices that further reduce federal spending to a significant degree. Because they will be at substantial financial risk, private plans will have strong incentives to negotiate price discounts, both to control their own costs in providing the drug benefit and to attract enrollees with low premiums and cost-sharing requirements.[1]

Question: Most of the President's health agenda seems to be through the Department of the Treasury, yet neither the Treasury nor the Department of Health and Human Services can explain the net effect of the President's budget proposals or the assumptions behind them. As a representative of the only cross-cutting entity, I hope you will be able to provide answers to the following questions:

- Estimated take-up rate for each program and cumulatively by AGI and/or tax bracket.
- Estimates of newly insured for each proposal, as well as the cumulative effect and the data source for these estimates.
- Estimates of the drop in employer-sponsored coverage for each proposal and cumulatively.
- Estimated out-of-pocket costs, in dollars, for individuals participating in these programs.
- Estimated out-of-pocket costs as a percent of net income for each income bracket.
- The tax benefit at each income bracket for each proposal, as well as the cumulative tax benefit of these proposals for individuals in each tax bracket.

Answer: The scoring of tax-related policies included in the Budget is done exclusively by the Department of Treasury. Questions about the detailed assumptions used in the scoring are best directed to the office of the Assistant Secretary of Tax Policy at Treasury.

Question: Current law requires deductible limits to be a minimum of $1,000 for an individual/$2,000 for a family, and a maximum of $5,000 for an individual/$10,000 for a family. However, many plans are not clear about

[1] Congressional Budget Office, Letter to the Honorable William H. Frist, M.D., January 23, 2004.

what is covered, which leads to spending that does not count toward either the deductible or the out-of-pocket limit.

- How will consumers know in advance what out-of-pocket costs do and do not count toward their policy?
- What do you estimate the mean and median out-of-pocket costs will be for individuals and families with high-deductible health plans?
- How are these out-of-pocket costs taken into account in your estimated take-up rates?

Answer: The scoring of tax-related policies included in the Budget is done exclusively by the Department of Treasury. Questions about the detailed assumptions used in the scoring are best directed to the office of the Assistant Secretary of Tax Policy at Treasury.

As is the case with conventional health plans, the high deductible health plan will be responsible for communicating the specifics of their coverage to beneficiaries.

Question: The President claims that HDHPs will control costs, but evidence suggests otherwise. Please answer the following questions:

- What are your underlying assumptions for this policy and what data are you using to support these assumptions?
- How much will aggregate health care spending be reduced as a result of high-deductible plans?
- If you project aggregate savings, how much will come from underuse of services vs. a reduction in prices vs. "more careful shopping" by patients? What are your data sources and assumptions for making such estimates?
- What are your estimates of necessary vs. unnecessary spending by individuals currently? How do you define unnecessary spending?
- What effect would unmanaged chronic conditions or deferred treatment of illnesses have on future Medicare costs?
- How many HDHP policyholders are projected to actually use their benefit (vs. simply pay premiums for coverage they cannot afford to access)

Answer: The scoring of tax-related policies included in the Budget is done exclusively by the Department of Treasury. Questions about the detailed assumptions used in the scoring are best directed to the office of the Assistant Secretary of Tax Policy at Treasury.

The Budget does not project a decrease in aggregate health spending. The Administration believes that providing consumers with greater choice and responsibility for their health care will create incentives for them to purchase services more prudently. This, in turn, will lead to lower health care costs.

Question: Previous independent analyses from the Academy of Actuaries and others have indicated that widespread adoption of HDHPs/HSAs or similar policies would dramatically increase premiums for traditional insurance. What does the Administration assume happens to premiums for traditional policies?

Answer: The scoring of tax-related policies included in the Budget is done exclusively by the Department of Treasury. Questions about the detailed assumptions used in the scoring are best directed to the office of the Assistant Secretary of Tax Policy at Treasury.

Question: The budget provides $28.5 billion to allow individuals an above-the-line deduction to offset the cost of premiums for a high-deductible health plan sold in conjunction with an HSA. Why is the President proposing a special additional tax break for these plans when even conservative analysts have indicated that the extra tax preference will distort the health insurance market?

Answer: The Administration believes the deduction will encourage individuals to purchase high deductible health plans and health savings accounts and to become more active participants in purchasing health care services. The deduction provides individuals taking advantage of these innovative products the same tax benefit that individuals with employer-sponsored health insurance enjoy. In this way, the Administration believes the deduction levels the playing field between employer-sponsored insurance and insurance purchased in the non-group market.

Question: The President is once again calling for Association Health Plans (AHPs) in the budget. This proposal is said to provide for less expensive pooling options because AHPs are exempt from state insurance regulations. However, this also means that they are exempt from consumer protections such as guaranteed issue, rate setting, and limitations on pre-existing condition exclusions. Given these facts, please answer the following:

- Which state regulations do you feel health plans should be exempt from and why?
- Do you anticipate issuers using medical underwriting to refuse to sell an HDHP?
- Will they be able to charge certain applicants higher premiums, based on their health history?
- Can they exclude certain body parts or conditions, based on the applicant's health history or history of someone in their family? If so, how will people be assured there is an affordable product available on the open market?
- How does this effect your enrollment assumptions?
- How do the grants to states to operate pooling arrangements interact with AHPs?

Answer: The detailed legislation/regulations to implement this policy have not been developed. It is important to the Administration that consumer protections are maintained while providing small employers and other groups the opportunity to access more affordable health insurance. The Administration looks forward to working with Members of Congress to form the specifics of this proposal.

Question: The budget mentions a proposal to regulate health insurance across state lines, yet state regulations for insurance products differ considerably.

- What standard is the President proposing for inter-state insurance regulation?
- Your documents suggest that you support consumer protections, but no specifics are given. Which protections do you propose to drop? Maintain?
- How will the Administration protect consumers from a "race to the bottom," where states are forced to accept policies approved in places where consumer protections are much less strong?
- Which department would have responsibility for this program—Treasury, HHS or Labor?
- How does this new policy affect your enrollment estimates?

Answer: The detailed legislation/regulations to implement this policy have not been developed. It is important to the Administration that consumer protections are maintained while providing small employers and other groups the opportunity to access more affordable health insurance. The Administration looks forward to working with Members of Congress to form the specifics of this proposal.

Question: Does the budget include any savings from malpractice reform? How were these savings calculated and what sources support these assumptions?

Answer: The Administration remains committed to enactment of medical liability reform. While these changes will have significant positive economic effects and will reduce government expenditures, current scoring practices prevent OMB from reflecting them in the budget. Therefore, the budget does not include savings associated with malpractice reform.

Question from Representative Benjamin L. Cardin to the Honorable Joshua B. Bolten

Question: Under the proposal that the Administration is considering, you have stated that individuals over 55 can expect to see no reduction in their benefits. How much of a reduction do you anticipate in the benefits for individuals under 55 who choose private accounts? How much of a reduction do you anticipate in the benefits of those who do not opt for private accounts? What effect will your proposal have for surviving spouses and children and for disabled beneficiaries?

Answer: The President has stated that disability benefits will not be affected by reform.

Under the President's proposal, retirement benefits would grow relative to today's levels. Future generations of seniors would receive benefits that are at least as high as seniors receive today, even after adjusting for inflation. The Pozen proposal referenced by the President would allow for faster overall long-term benefit growth than can be paid by current-law Social Security, with lowest-income Americans getting the fastest benefit growth of all, significantly faster than inflation. Medium-wage earners would also receive benefit growth faster than inflation, and the Social Security actuary's analysis of the plan found that low, medium, and high earners under the Pozen plan would all receive benefits that are higher than the current system can pay. All of these figures exclude income from personal accounts. SSA figures show that expected benefit growth would be even greater for those who choose to participate in voluntary personal accounts.

Under the President's proposal, Social Security would for the first time enable workers to leave a bequest at the time of their death. Workers choosing a personal account could pass the balance on to their spouse should they die before exhausting the account. These inherited account balances can significantly increase the benefits received by widows. Under current payable benefits, in 2050 roughly 3.9 percent of widows would live in poverty. Under progressive benefit growth plus personal accounts, this would be reduced to just 1.1 percent, lifting over 180,000 widows out of poverty. This poverty rate is even lower than under currently scheduled benefits, which are not affordable. (Data from SSA Office of Policy MINT model).

Questions from Representative Jim McDermott to the Honorable Joshua B. Bolten

Question: It seems likely that any number of media consultants, public relations firms, copy writers and others must be involved in the effort to communicate the President's views on Social Security to the American people. We know from news reports that the Administration pays B that taxpayers are paying B these kinds of firms, and sometimes even journalists, to spread the Bush Administration's message.

Where do I find this in the budget?

Secretary Snow says that this budget is transparent. He mentioned it several times at a recent hearing in the Committee on Ways and Means. Where do I look to find the names of the Public Relations firms that have been hired and how much they're making?

I would like a full accounting of the amount of money that the Bush Administration spent or plans to spend on public relations efforts in FY 2004 through FY 2006. Please detail the purpose of each expenditure and to whom contracts were awarded.

Answer: In his State of the Union Address, President Bush outlined for the nation his vision to strengthen and save Social Security.

The President's plan calls for reforms that would keep Social Security's promises for today's seniors and those near retirement; solve the financial problems of the current system once and for all; and make Social Security a better deal for younger workers by allowing them to set aside part of their payroll taxes in voluntary personal retirement accounts.

Thanks in large part to the President's leadership and courage, the national discussion is now focused on the serious problems facing Social Security. Americans understand that the current system won't be there for their children and grandchildren. They understand that action needs to be taken now to keep the promise of Social Security alive.

The Social Security Information Center (SSIC), which is part of Treasury Department's Office of Public Affairs, communicates both the current demographic challenges facing Social Security and the President's proposals to permanently fix this important system for future generations. The SSIC supports the Department's strategic goal of promoting economic opportunity and ownership and supporting the Secretary in his role as Managing Trustee of the Social Security trust funds.

The FY 2005 costs for the Center will be approximately $275,000 to support five government employees. The Center was not planned during the development of the FY 2005 budget and thus was not included in the FY 2005 materials. The current estimates for the FY 2006 costs, based on December 2005 wind down date, are $125,000. No funds have been used for outside commentators, consultants, or paid advertisements of any kind.

Question: If Social Security is dismantled and replaced with a system that relies on private accounts to fund retirement benefits, as the President has proposed, will the Social Security Administration (SSA) be able to send a statement that shows an exact dollar figure that individuals can expect to receive in retirement (as SSA does now), or will the statement show a band B a range B of potential benefit levels? Will there be a disclaimer anywhere that says that the benefit level is an estimate based on the expected returns of private accounts? Lastly, how accurately can one predict investment returns 40 or 50 or 60 years into the future (please give examples of such accurate predictions)?

Answer: While I disagree with the premise that the President has proposed dismantling Social Security, the President has proposed allowing younger workers the choice to voluntarily invest a part of their Social Security taxes in personal accounts. These accounts offer workers increased ownership and control, the ability to build a nest egg, and the opportunity to receive higher rates of return than traditional Social Security. The accounts will be managed in a similar way to the Thrift

Savings Plan (TSP) Records will be maintained by a central administrator and participants will receive periodic account statements. The combination of the traditional benefit and the personal retirement accounts will give younger workers the opportunity to be better off.

The Social Security Administration's independent Office of the Chief Actuary's makes projections of the expected return for personal accounts based on historic patterns for equities and corporate bonds and taking into account future expected patterns in equity and bond pricing. The actuaries project the long-term average annual real yield for the stock market will be6.5% in the future. This estimate is similar to the Congressional Budget Office's estimate of the long-term real return of 6.8%. This return compares to historical returns of 6.8% since 1871.

Projections over extended periods of time always carry a degree of uncertainty. This is true for long-term investment returns as it is for the finances of the underlying Social Security system. To account for this uncertainty, the Social Security Trustees, as well as the office of the actuary, show a range of possible outcomes. Even under a wide range of outcomes, however, certain trends are relatively certain. For example, the Trustees found that there is a 95%chance that the current Social Security program will enter permanent cash deficits at some point between 2013 and 2023.Thus, while there is uncertainty surrounding the precise details of the projection, there is considerably less so about the fundamental long-term direction of the program. Similarly, with stock return projections, there is uncertainty over the precise numerical projection, but there is not uncertainty over the fundamental projection that stocks will continue to earn higher long-term returns than the Treasury bond rate, which in turn is higher than the internal rate of return that future workers will receive from the traditional Social Security program.

Question from Representative Lloyd Doggett to the Honorable Joshua B. Bolten

Question: The Administration's budget does not include continuation of the deduction for state and local sales taxes. Does the Administration oppose continuing the deduction?

Answer: The Administration does not support continuing the deduction for state and local sales taxes. However, the Administration recognizes there is a question of fairness in allowing State and local income and property taxes to be deductible while sales taxes are not deductible. The Administration believes the inconsistency of the respective tax treatments can and should be addressed in the context of fundamental tax reform.

[Submission for the record follows:]

Statement of Eduardo Ferrero, Embassy of Peru to the United States

House of Representatives Ways and Means Committee, Hearing on the President's Fiscal Year 2006 Budget

The Embassy of Peru congratulates the Ways and Means Committee of the House of Representatives for holding a hearing and receiving written statements regarding the President's Fiscal Year 2006 Budget.

We understand that the Office of Management and Budget (OMB) has presented a budget in the framework of the Andean Counterdrug Initiative of US$ 734.5 million ($3.5 million more than Fiscal Year 2005). Unfortunately, in said initiative the amount assigned for drug cooperation to Peru is US$ 97 million or a proposed reduction of more than US$ 18 million (−16%) in comparison to Fiscal Year 2005 (US$ 115.37 million).

Within the full respect for U.S. legislation, the Government of Peru would like to express its utmost concern about the proposal to reduce the amount for bilateral antidrugs cooperation with Peru in the U.S. Budget for Fiscal Year 2006. We see this proposed reduction as counter productive, particularly if we take into account the significant progress made in the fight against drug-trafficking and the challenges we must face.

Peru and the United States share the same interest to cooperate against illegal drugs as they see this matter as a grave menace to national and hemispheric security. That is the reason why the fight against drug-trafficking has been placed as one of the high priorities of the Government of Peru in the last years. Positive results based on this effort are at hand, where close to 30,000 hectares have been eradicated in the last three years and almost 14 tons of cocaine and basic paste of cocaine have been seized from drug traffickers in the same period. These results would have not been achieved without the commitment of our Government and the

support provided by the United States. However, to continue with this effort, the valuable and important support of the United Stated is needed.

Furthermore, the reduction of these cooperation funds will have a negative effect in the progress we have obtained in the fight against drug-trafficking. Due to the success of "Plan Colombia" on the eradication of coca crops, a "balloon effect" has developed, where new coca crops have started to grow in neighboring countries. We have to realize that from a regional perspective facing this problem will have a negative correlation effect for the interdiction and eradication success in other countries of the region. Issues like security, drug trafficking and terrorism are closely related and the support of the United States is vital to continue facing together, as partners, these new challenges.

We believe that the House of Representatives has an important role to play in this matter. We also believe it has the power to re-examine the Administration proposal for Fiscal Year 2006 in regard to the Andean Counter Drug Initiative and, particularly, the proposed amount assigned for the cooperation with Peru. Therefore, we respectfully request that the proposed anti-drug cooperation funds for Fiscal Year 2006 be reconsidered or, at least, the amount provided by the U.S. Congress for Fiscal Year 2005 be maintained.

Co-responsibility is relevant because drug-trafficking affects both countries. We have to stop the demand as well as the supply.

The U.S. Congress is aware and very supportive of the efforts carried out by Peru in the fight against illegal drugs in the Andean Region. In 1991, U.S Congress approved the Andean Trade Preferences Act (ATPA) which was renewed and expanded by the Andean Trade Promotion and Drug Eradication Act (ATPDEA) of 2002. These U.S. laws have significantly contributed to coca eradication efforts in Peru by providing farmers and other populations at risk, with alternative economic activities to the highly profitable illegal crops.

Thanks to the benefits provided by the ATPDEA, in 2004 our exports to the United States grew by more than 51.8 %. Textiles and apparel, agro-products and gold jewelry lead the expansion of sales to the US, generating thousands of new jobs and improving the livelihood of peasants and workers in Peru, especially in rural areas.

Our government is firmly committed to the fight against drug trafficking. It created the National Commission for Development and Life without Drugs (DEVIDA), to design, conduct, and supervise the anti-drug policy and rehabilitation programs in Peru.

On January 21, 2005, the Peruvian Government approved an updated version of the Peruvian National Strategy to Fight Drugs 2002—2007, which focuses on four major actions:

- Reduction of the drug consumption and rehabilitation
- Interdiction
- Alternative development and protection of the environment
- Eradication and auto eradication of illicit crops

These four actions have to be sustained in time and executed in a coordinated manner.

It is very difficult to tell a "cocalero", a farmer who grows coca leaves, to cease his activities if we do not provide him with an alternative crop. A licit crop may generate sufficient profit for him to stop growing coca plants. In the areas where coca is grown there is not just one crop that may be harvested, but several like coffee, palm oil, cocoa, cotton, corn, peanuts and fruits. We currently have several projects for all these products.

As stated previously, we have to give farmers a chance to develop alternative crops and protect the environment. The production of alternative crops is only feasible if they can be delivered to major markets, either in Peru or abroad, where they can be sold. In this regard, the U.S. Government is cooperating in the rehabilitation of the important road between Juanjui and Tocache, in the Peruvian rainforest, through the U.S. Agency for International Development (USAID).

As far as the environment is concerned, we know that drug traffickers do not care about protecting the environment. All the chemicals used in the elaboration of cocaine and its derivatives, many of them highly toxic, are thrown into the rivers of the highlands and jungle of Peru, contaminating clean waters and endangering wild flora and fauna.

Current drug cooperation between the two countries has led to important results in the fight against drug trafficking. The efforts of Peruvian authorities have been very important, and the projected goals or eradication have been achieved in the last two years. As shown in the following chart, in the last three years, almost

30,000 hectares of coca crops have been eradicated, either through forced or voluntary eradication.

Coca Crops Eradication (Hectares)	2002	2003	2004
Forced eradication	7,134	7,022	7,605
Voluntary eradication	0	4,291	2,733
Total	**7,134**	**11,313**	**10,338**

Source: DEVIDA

Interdiction

Alternative development and eradication are not the only actions that our Government has taken to fight against drug trafficking. Our National Police, in cooperation with foreign enforcement agencies, have been able to seize great amounts of cocaine ready to be shipped to the United States, Mexico and Europe. In comparison to 2003, there was an increase of 71.69% in the amount of illegal drugs seized in 2004.

Illegal Drugs (kgs.)	2002	2003	2004
Seized:			
Basic Paste of Cocaine	10,439	4,366	6,329
Cocaine	4,129	3,574	7,303
Total	**14,568**	**7,940**	**13,632**

Security

It is undeniable that there is a criminal link between terrorists and drug-traffickers, not only in our country but also in other parts of the world. Illegal profits obtained from drug-trafficking may be used to buy weapons, bombs, etc. for terrorists. This "alliance" must be considered a threat to security, not only on a national level but on the hemispheric and global arena. Currently, the actions of terrorist groups, as well as drug-traffickers are not limited by official borders of countries. We must take into account that these groups move and act in less protected places where they still feel safe. The way they are organized, they are able to transcend those borders, and become a threat to security. We must be prepared to face and fight this new threat.

Due to the new and enormous challenges that we must face in the fight against drug trafficking, our Government truly and respectfully considers that anti-drug cooperation should be increased and not reduced.

The above mentioned positive results in the fight against illegal drugs, based on the cooperation between our two countries, prove that there has been important progress in the last years. Consequently, we need to continue working together to face these challenges with the valuable support of the United States.

○