THE PRESIDENT'S SOCIAL SECURITY LEGISLATION

HEARING

BEFORE THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

NOVEMBER 9, 1999

Serial 106–33

Printed for the use of the Committee on Ways and Means

U.S. GOVERNMENT PRINTING OFFICE

65–744 CC WASHINGTON : 2000

COMMITTEE ON WAYS AND MEANS

BILL ARCHER, Texas, *Chairman*

PHILIP M. CRANE, Illinois
BILL THOMAS, California
E. CLAY SHAW, JR., Florida
NANCY L. JOHNSON, Connecticut
AMO HOUGHTON, New York
WALLY HERGER, California
JIM MCCRERY, Louisiana
DAVE CAMP, Michigan
JIM RAMSTAD, Minnesota
JIM NUSSLE, Iowa
SAM JOHNSON, Texas
JENNIFER DUNN, Washington
MAC COLLINS, Georgia
ROB PORTMAN, Ohio
PHILIP S. ENGLISH, Pennsylvania
WES WATKINS, Oklahoma
J.D. HAYWORTH, Arizona
JERRY WELLER, Illinois
KENNY HULSHOF, Missouri
SCOTT MCINNIS, Colorado
RON LEWIS, Kentucky
MARK FOLEY, Florida

CHARLES B. RANGEL, New York
FORTNEY PETE STARK, California
ROBERT T. MATSUI, California
WILLIAM J. COYNE, Pennsylvania
SANDER M. LEVIN, Michigan
BENJAMIN L. CARDIN, Maryland
JIM MCDERMOTT, Washington
GERALD D. KLECZKA, Wisconsin
JOHN LEWIS, Georgia
RICHARD E. NEAL, Massachusetts
MICHAEL R. MCNULTY, New York
WILLIAM J. JEFFERSON, Louisiana
JOHN S. TANNER, Tennessee
XAVIER BECERRA, California
KAREN L. THURMAN, Florida
LLOYD DOGGETT, Texas

A.L. SINGLETON, *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.

C O N T E N T S

THE PRESIDENT'S SOCIAL SECURITY LEGISLATION

TUESDAY, NOVEMBER 9, 1999

HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
Washington, D.C.

The Committee met, pursuant to call, at 10:05 a.m., in room 1100, Longworth House Office Building, Hon. Bill Archer (Chairman of the Committee) presiding.

[The advisories announcing the hearing follow:]

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

FOR IMMEDIATE RELEASE

CONTACT: (202) 225–1721

October 27, 1999
FC–15

Archer Announces Hearing on the President's Social Security Legislation

Congressman Bill Archer (R–TX), Chairman of the Committee on Ways and Means, today announced that the Committee will hold a hearing on President Clinton's new Social Security plan. The hearing will take place on Wednesday, November 3, 1999, in the main Committee hearing room, 1100 Longworth House Office Building, beginning at 10:30 a.m.

Oral testimony at this hearing will be from invited witnesses only. 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:

On Wednesday, October 26, 1999, President Clinton submitted legislation outlining a Social Security plan. The proposed legislation reflects the third plan set forth by the President over the past 10 months. The new plan would create several budget enforcement rules to ensure that 100 percent of the Social Security surplus is used to pay down the public debt over the next 15 years. Under the proposed legislation, during fiscal years 2011 −2044, nearly $7 trillion of general revenues would be transferred to the Social Security Trust Funds in the form of interest-bearing, special-issue Treasury securities. Transfers made during the first six years are supposed to reflect interest savings generated from the debt reduction. However, the transfers would not be contingent on debt relief; instead, they would be appropriated in the law according to a specified formula. Transfers made after fiscal year 2016 would be set by law at the fiscal year 2016 level. According to Social Security's actuaries, the President's plan would extend the life of the Social Security Trust Funds to 2050 −16 years later than current law.

In announcing the hearing, Chairman Archer stated: "I have serious reservations about the President's latest plan, so I look forward to hearing from our witnesses as to how this plan actually works. Does it meet our principles of no tax hikes or benefit cuts? Does it save Social Security for 75 years? Does it offer new options for younger workers? I'll be looking for these and other answers from the witnesses."

FOCUS OF THE HEARING:

The hearing will evaluate the President's new Social Security plan and discuss the impacts of the plan on taxpayers, the Federal Budget, the Social Security program, and the economy.

DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

Any person or organization wishing to submit a written statement for the printed record of the hearing should submit six (6) single-spaced copies of their statement, along with an IBM compatible 3.5-inch diskette in WordPerfect 5.1 format, with their name, address, and hearing date noted on a label, by the *close of business*, Wednesday, November 17, 1999, to A.L. Singleton, Chief of Staff, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office

Building, Washington, D.C. 20515. If those filing written statements wish to have their statements distributed to the press and interested public at the hearing, they may deliver 200 additional copies for this purpose to the Committee office, room 1102 Longworth House Office Building, by close of business the day before the hearing.

FORMATTING REQUIREMENTS:

Each statement presented for printing to the Committee by a witness, any written statement or exhibit submitted for the printed record or any written comments in response to a request for written comments must conform to the guidelines listed below. Any statement or exhibit 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 statements and any accompanying exhibits for printing must be submitted on an IBM compatible 3.5-inch diskette in WordPerfect 5.1 format, typed in single space and may not exceed a total of 10 pages including attachments. Witnesses are advised that the Committee will rely 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. A witness appearing at a public hearing, or submitting a statement for the record of a public hearing, or submitting written comments in response to a published request for comments by the Committee, must include on his statement or submission a list of all clients, persons, or organizations on whose behalf the witness appears.

4. A supplemental sheet must accompany each statement listing the name, company, address, telephone and fax numbers where the witness or the designated representative may be reached. This supplemental sheet will not be included in the printed record.

The above restrictions and limitations apply only to material being submitted for printing. Statements and exhibits or supplementary material submitted solely for distribution to the Members, the press, and the public during the course of a public hearing may be submitted in other forms.

Note: All Committee advisories and news releases are available on the World Wide Web at "http://www.house.gov/ways__means/".

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.

*****NOTICE—CHANGE IN DATE AND TIME*****

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

CONTACT: (202) 225–1721

FOR IMMEDIATE RELEASE
October 28, 1999
FC–15-Revised

Date and Time Change for Full Committee Hearing on
Wednesday, November 3, 1999,
on the President's Social Security Legislation

Congressman Bill Archer (R–TX), Chairman of the Committee on Ways and Means, today announced that the full Committee hearing on President Clinton's new Social Security plan, previously scheduled for Wednesday, November 3, 1999, at 10:30 a.m., in the main Committee hearing room, 1100 Longworth House Office Building, will now be held on Thursday, November 4, 1999, at 10:00 a.m.

All other details for the hearing remain the same. (See Full Committee press release "fc–15.htm" No. FC–15 , dated October 27, 1999.)

*****NOTICE—CHANGE IN DATE AND TIME*****

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

CONTACT: (202) 225–1721

FOR IMMEDIATE RELEASE
October 28, 1999
FC–15-Revised

Date and Time Change for Full Committee Hearing on
Thursday, November 4, 1999,
on the President's Social Security Legislation

Congressman Bill Archer (R–TX), Chairman of the Committee on Ways and Means, today announced that the full Committee hearing on President Clinton's new Social Security plan, previously scheduled for Wednesday, November 4, 1999, at 10:00 a.m., in the main Committee hearing room, 1100 Longworth House Office Building, will now be held on Tuesday, November 9, 1999, at 10:00 a.m.

All other details for the hearing remain the same. (See Full Committee press release "fc–15.htm" No. FC–15 , dated October 27, 1999.)

Chairman ARCHER. The Committee will come to order. Good morning to everyone on this beautiful Washington fall day.

Mr. RANGEL. Good morning, Mr. Chairman.

Chairman ARCHER. Thank you, Mr. Rangel. Today's hearing is on the President's Social Security plan. We committed at the beginning of this year that when the President sent up the Social Security plan, that we would give it very serious consideration. And we are fulfilling our commitment today, and it is our pleasure to have with us the new Secretary of the Treasury, Secretary Summers, who is making his first appearance before our Committee since being confirmed by the Senate, which confirmation sailed through without controversy, a great compliment to Mr. Summers. I congratulate you and welcome you before the Committee.

The President's latest version of his Social Security plan is in some ways a step forward and a step back. It is a step forward because it has been long awaited by this Committee and the Chairman had hoped that it would have occurred much, much earlier this year to give us time to try to find a bipartisan answer this year.

It is also a step forward because the President dropped his original recommendation that the Social Security Trust Fund dollars be invested by the government directly in the stock market rather than having personal savings accounts where individual workers would be able to determine the investment of their own funds. And I applaud the removal of this provision by the President from his original plan.

In doing so, however, the President has also abandoned entirely the concept that we should use the strength of the financial markets to help shore up Social Security's finances. Most experts, including the President's own Social Security Advisory Council, believe that we should do this in some fashion, and I think it is best accomplished by providing Americans with their own personal savings accounts. But I hope the President will keep an open mind about this as we move in that direction.

I think it is very important that we find a way to resolve this problem and resolve it cooperatively between the White House and the Congress, but I must say that I am disappointed in the President's program in what I believe is a step backwards. After saying in 1998 that we should put first things first and save Social Security first, and after a year-long national debate and dialogue on Social Security and after a White House summit now almost a year ago on Social Security, after countless hearings and forums discussing the need to save Social Security, I really had hoped that the President would submit a better long-term plan.

First, this plan will not save Social Security for the required 75 years. Second, it leaves Social Security hurtling toward a cliff of insolvency at the end of the year 2050. And third, because it does not satisfy the long-term goals, I do not believe it has any chance of becoming law. Despite this, I am still hopeful that we can work together to save Social Security. And Social Security Subcommittee Chairman Shaw and some Members of this Committee may be the few other people who agree with me.

We have offered a plan that saves Social Security for 75 years without tax increases or benefit cuts, gives every working American a personal savings account that can be invested at their decision, and provide retirement security for them and their families. Others, including many senior Democrats in the House and Senate have introduced plans based on the concept of personal savings accounts. But the President apparently still is unwilling to accept this.

In closing, let me say I am still optimistic. Conventional wisdom says we cannot fix Social Security in a Presidential year, next year, but there are always exceptions to prove the rule. This so-called conventional wisdom said we couldn't balance the budget, we couldn't strengthen Medicare, we couldn't reform welfare, and that we couldn't cut taxes.

I know from the discussions that I have had personally with President Clinton that he wants to save Social Security and I think he would be a lot bolder than this plan if he were totally free of all political constraints, because I believe that deep down he knows this plan just doesn't do the job. But as is often the case in Washington, politics have gotten in the way, and that goes for both parties, but if we put principles before politics and ideas before ambition, we can fix Social Security, working together.

I now recognize Mr. Rangel for any opening statement that he might like to make and, without objection, all Members may enter their written statements at this point in the record.

Mr. Rangel.

Mr. RANGEL. Thank you so much. Good morning again, Mr. Chairman.

Chairman ARCHER. Good morning, Mr. Rangel.

Mr. RANGEL. We want to thank you and the Republican Party, really, under the leadership of President Reagan, for moving us forward in balancing the budget and looking forward to this surplus. It was your idea, and we Democrats thought that we could support President Clinton's budget and move forward and do this even without the help of existing Republicans and we reached that goal. We have accomplished it and some of us believe that the President is right in asking that while we are moving forward with this surplus, that we take care of Social Security and Medicare first.

Now, I know you have been waiting a long time for the President's legislation on Social Security. Why, I don't know, because we have always prided ourselves in the House of Representatives, and especially on the Ways and Means Committee, in not just doing what Presidents tell us to do. We like their recommendations. We like working with them, certainly when it comes to tax cuts. We didn't go to the administration and ask about the $792 billion tax cut. We are a pretty independent Committee and House. However, since we did not draft the bill and still don't have a Social Security bill, and we are the legislative Committee, let me join you in thanking the President's people for coming forward and giving us at least an outline that we can follow.

Now, this bill should not be everything that we want as Democrats or as Republicans. It should be a guideline. And, whether it is short term or long term, it is better than not having any fix at all. That is where I think with your leadership, Mr. Chairman, working with the President, Republicans and Democrats working together, we can just put aside this notion of a trillion dollar tax cut and stop cooking the books on the other side of how much this thing costs, and start moving forward and taking care of Social Security, Medicare, and, God willing, give the American people some substantial tax relief.

I certainly would hope that it would be part of your legacy that, in the last year that you are here, that you work with our President, you work with your Republican and Democratic friends, and that we do have a Social Security bill that can pass. In order to do that, I think we have to move away from $792 billion in tax cuts and kind of think in terms of what to do with Social Security.

I would like to yield to the Ranking Member of the Subcommittee on Social Security and hope he would support my position.

Mr. MATSUI. I thank you, Mr. Rangel, for yielding to me, and I appreciate your remarks and your comments. I am going to be very brief because I know we want to hear from Mr. Summers and I do believe that Mr. Shaw will have an opening statement as well. But I would like to just make one observation. I think the President's plan is an excellent starting point. It tried to accommodate some of the objections that Mr. Greenspan and you, Mr. Archer, as Chairman of the Committee, have raised regarding investments by fund managers into the equity markets. But it tried to deal with some of the issues that you raised over the last 6 or 7 months. This proposal will buy down the debt for the next 15 years, and for the first time since 1834, believe it or not, we would end up having a situation in our economy where there would be no national debt. At the same time, by using the savings from the reduction in the debt—that is, interest savings—we will be able to put that money into the Social Security fund to preserve the solvency of the Social Security account until the year 2050.

That means a child today would undoubtedly be in a better position to collect his or her benefits. Somebody who is 20 today will be guaranteed his or her benefits. And so this is a situation where it makes sense, as Mr. Rangel said, at least to get the ball rolling. We still have a number of years, over the next 50 years, to solve the additional 25 years of the problem, if in fact, as Mr. Archer suggested, that we should. But this will give us 50 years' savings on the fund.

Now, I don't want to get into charges back and forth between different plans, but I don't think you can look at the President's plan in a vacuum. And I hope there will be opportunities to talk about other plans as well, particularly the plan advanced by Chairman Archer and Mr. Shaw. The problem with that plan, I think, as everyone knows, is that if you give a $792 billion tax cut over the next decade, and beyond that as well, and then you also institute the Archer-Shaw plan with a 2 percent of payroll credit for every American in the work force, you will not have enough money available for both of these initiatives. And certainly what would happen then is we would be in major deficit spending.

In fact, under Archer-Shaw—and they admit this themselves—35 years from now when the President's plan would create a balanced situation and there would be no debt, Archer-Shaw would increase the debt held by the public by $11.7 trillion. So I would have to say the President's plan is the only realistic practical plan available. Archer-Shaw is just not an option available to us given the fact of the uncertainty of the Federal debt, and certainly our budget.

I look forward to these hearings and certainly hearing from the witnesses, but it is my hope that we begin to look at the President's plan with a little more practicality instead of ideology. I yield back the balance of my time.

Chairman ARCHER. I yield to the Subcommittee Chairman of the Social Security Subcommittee, Mr. Shaw, for a statement.

Mr. SHAW. I thank you for yielding me this time. I have been looking forward to this hearing for some time and I think we are making progress. There are two issues that are before us this morning. The first is the President's Social Security bill. As our witnesses will attest, while it takes positive steps such as paying down the debt, the President's plan will not save Social Security for 75 years. That is his own yardstick for reform. That is just not good enough for us.

The second issue is are we ready to save Social Security for all time, for 75 years and beyond? I think that we are. Most of our Democrat colleagues, including Ranking Member Rangel and Matsui, showed support for the action by cosponsoring the President's plan. We expect, Chairman Archer and I, expect to and will be introducing the Archer-Shaw plan shortly. It is in legislative form and it is ready to go.

Our plan doesn't cut benefits. It doesn't raise taxes, but it does save Social Security for 75 years and beyond. And I would say to my Democrat friends that we listened to your concerns. Several of you asked why your concerns were not addressed and why you were not part of drawing the bill. Mr. Archer and I have been working on this bill for almost—for just about 2 years. We have had more hearings on this than we had when we reformed welfare. We have been listening to you. We have addressed your concerns and I think that we have taken them into account on this legislation.

First of all, we don't touch Social Security. We don't touch it at all. The FICA tax is still out there. It is still invested in Treasury bills. The system stays exactly the way it is under the Archer-Shaw bill. We protect all the benefits so there is no need to cut COLAs or raise the retirement age. We don't do that. We maintain all existing benefits. We avoid a tax hike, a concern that Mr. Rangel and I have discussed, and we allow for tax cuts in the long run. Actually we can see and the Social Security Administration tells us that under our plan, the FICA tax can be cut in the outyears.

And we fully protect against individual risks. There is no risk. We even provide new benefits like inheritance of the individual retirement accounts and we eliminate that terrible Social Security earnings penalty, which is grossly unfair to so many of our low-income retirees, and we save Social Security for all time. That is not our estimate, this is the estimate that is given us by the Social Security Administration.

So we say to the President, work with us. No plan is perfect. Yours certainly isn't. Ours isn't either, but as I see it, we now have two clear options: One option is for you to tell us how you would further change our plan to save Social Security for 75 years and beyond, and I would say to the President, I would say to our distinguished witness today, work with us. We can do this and we can do it together.

The President has asked to us do it together and wait for his lead at the White House conference of a year ago. We waited and waited and we still have not received a plan that saves Social Security for all time. But we do still look to the White House for leadership and I think it is very important.

I would comment on Mr. Rangel's statement. Sure, we are the legislative body, but in every major Social Security reform that we have had in this country, we have had leadership from the White House. I think it is very important and I think, most important, it is important that this be done in a bipartisan way.

The other option is for you to tell us whether you would sign the Archer-Shaw plan or, if you wouldn't, what changes are needed for your signature. Again, we are ready to sit down and go to work, meet with the President anytime, anywhere, in order to reach these goals.

I want to say to you, Secretary Summers, to convey to the President personally the message that we have. And I want to welcome you. You have been a friend of this Committee, I think a very forthright witness. Some tough questions are going to be asked of you today. That is our job as the Republican side, is to look to problems that are within the Social Security plan put forth by the President, but that does not in any way diminish our desire to work in partnership with the President, and I thank you for being here, Larry.

Opening Statement of Hon. Fortney Pete Stark, a Representative in Congress from the State of California

Mr. Chairman, along with the Minority Leader, the Minority Whip and many of my Democratic colleagues on the Ways & Means Committee, I have taken the initiative to end the partisan politics over Social Security by cosponsoring H.R. 3165, the Strengthen Social Security and Medicare Act of 1999. This bill extends the life of Social Security from 2034 to 2050. In addition, this bill reduces the amount of debt held by the public from roughly 44 percent of GDP today to 7 percent by 2014. It is time for the House Leadership to meet us half way and give the issue of Social Security solvency the serious consideration it deserves.

The GOP makes false accusations that the Democrats are raiding the Social Security Trust Funds but has done nothing to ensure long-term solvency. The only reason the majority leadership has not taken action on Social Security this session is because they would rather politicize the issue than extend its solvency. All of this finger pointing and bickering over the surplus serves to hide the fact that no action has been taken to extend the life of the Social Security trust fund.

Beginning in the year 2014, the Social Security trust fund will take in fewer taxes than it pays out in benefits. This means that Social Security will need to redeem the treasury notes it holds starting in the year 2014. By the year 2034, all of those treasury notes will have been cashed in. Once those notes are gone, the Social Security trust fund will not have any additional revenue coming in other than the payroll taxes paid in week by week to pay the promised benefits. Without additional revenue, this would result in a significant decrease in the benefit of about 25 percent. But the majority party will have the American people believe that the Democrats are raiding the Social Security Trust Fund to bolster other programs.

This is simply not true!

This long-term shortfall is what Congress should be addressing now, not arguing about who's stealing the surplus dollars of tomorrow. However, the GOP would rather cloud the issue with false accusations than confront the American people with their plan to offer billions of dollars in tax breaks to the wealthiest Americans.

I have already offered my own plan to shore-up the Social Security system-H.R. 2039; however, the leadership will not consider it. So I have once again signed my name to another plan that lengthens the life of Social Security. The plan before us today extends the life of Social Security from 2034 to 2050 by paying down the public debt and using the interest savings from the debt reduction to reinvest in the Social Security Trust Fund.

The American worker wins in two respects from this plan. First and foremost, the plan helps to strengthen Social Security. The life of Social Security is extended an additional sixteen years. This is enough time for Congress to come up with a comprehensive plan to extend the system beyond 2050, so that Generation Xers can have the same confidence that their parents have in the Social Security system. Second, a lower national debt means lower interest rates. Lower interest rates is the equivalent of a tax cut that benefits middle-income families.

The bill goes one step further by protecting Medicare as well. The bill creates a lockbox for Medicare to ensure that it is protected from those who would rather give big tax breaks to CEOs and big business. The bill prohibits reducing any non-Social Security surpluses by more than two-thirds of the projected surplus unless those funds are used for a Medicare solvency package. This reserves at least one-third of future surpluses to protecting seniors' healthcare. This includes setting aside funds for a prescription drug benefit.

Finally, to prove that there is no gimmickry in this plan, the bill further protects Social Security and Medicare by extending the budget enforcement rules that have helped generate the current surpluses.

I encourage the Ways & Means Committee and the House Leadership to stop pointing fingers and take action on H.R. 3165. It is a responsible first step in shoring up the Social Security and Medicare systems.

Chairman ARCHER. Mr. Secretary, again, welcome. And we are pleased to be able to receive your testimony. And if you are ready, you may proceed.

STATEMENT OF HON. LAWRENCE H. SUMMERS, PH.D., SECRETARY, U.S. DEPARTMENT OF THE TREASURY

Secretary SUMMERS. Thank you very much, Mr. Chairman, Mr. Ranking Member, Chairman of the Subcommittee, Ranking Member on the Subcommittee. I am grateful for the opportunity to appear to testify before you with respect to the President's plan for preserving Social Security, and in a broader fiscal context, which I know to be of great interest to this Committee and others in the Congress.

I have a longer statement for the record if that is all right, Mr. Chairman, which I will summarize here today.

Chairman ARCHER. Mr. Secretary, without objection, your entire written statement will be inserted in the record.

Secretary SUMMERS. In my remarks today, I would like to address three issues: First, dramatic fiscal progress that has been achieved in the nineties and the benefits for the American people that have resulted. Second, the President's plan for maintaining this progress and assuring that the savings it brings will not be dissipated and will be channeled into strengthening the Social Security system. And third, the broader significance of the President's plan and our further economic and fiscal priorities going forward.

Mr. Chairman, I think we can all take satisfaction from the progress that our country has achieved over the last decade in bringing about, first, an end to budget deficits and budget balance, and now a period of surplus where our national debt is being reduced.

Some years ago we faced a vicious cycle of substantial deficits, high interest rates, slower growth, less tax revenue, larger deficits, and the cycle went round and round again. With the progress that we have made in recent years with the 1993 and the 1997 budget agreements, we have seen that vicious cycle converted into a virtuous circle of greater economic growth, lower interest rates, larger surpluses, still lower interest rates, greater economic growth, more revenue collections, larger surpluses and so forth.

It is that change in our Nation's fiscal position and the underlying doubling in our level of national savings that has contributed greatly to the strength of our economy over the last 6 years. It is that change which has brought the prospect not just of a balanced budget but of the elimination of the national debt over a 15-year period into view, that leaves us in a position to tackle the challenge of an aging society that is far stronger than almost any observer expected a few years ago. And it is that fiscal strength that forms the basis for the President's approach to Social Security.

Common sense is that you use a moment of opportunity to prepare for a future possible problem. Economic logic is that you use the space created by the removal of one liability, the national debt, to make room to meet another liability: the obligation we have to a generation of retiring seniors. And political logic points towards establishing a set of mechanisms that ensure that in the face of what will be very real temptations, we as a country do not dissipate the surpluses that are in prospect on either unwise spending programs or unwise tax cuts.

The President's approach has four main elements. First, the President's approach is based on the idea that we should respect the integrity of the Social Security Trust Fund by ensuring that all of Social Security surpluses are used to pay down debt rather than finance other government activities. The President's approach enhances the trust fund's ability to contribute to the government and Nation's capacity to meet its promises by ensuring that its accumulations translate directly into increases in national savings and reduced indebtedness.

The second principle behind the President's plan is that the interest savings from the debt reduction coming from Social Security should be channeled into the Social Security Trust Fund. Essentially we devote the savings that we have earned from reducing one liability, the Federal debt held by the public, to meeting another government liability; namely, promised Social Security benefits. According to the Social Security actuaries, the transfers we propose would extend the solvency of the Social Security system to 2050 compared to 2034 under current law.

The third principle is that as we look at our budget framework, we should make provision for devoting increased resources to Medicare that are likely to be necessary in the context of any enduring approach to its long-term future. Whichever route this country ultimately takes with respect to the fundamental reform of Medicare, most independent observers agree that Medicare will require increased funding to substantially extend its solvency without damaging benefit cuts or tax increases.

The fourth principle embodied in the President's proposal is that the Nation's budget plans should be based on realistic discretionary plans. We have seen that discretionary caps can be very helpful in achieving fiscal discipline over the past decade. The President's plan extends them. It would also use some of the surplus as part of a plan that extends Social Security solvency to assure we are providing and budgeting based on realistic levels of appropriations for the fulfillment of government's core functions.

To be sure, even with the President's proposal, discretionary spending will grow less rapidly than inflation, as it has in recent years. We believe that such cuts are feasible if the spending is targeted at our critical needs. Deeper cuts, such as the cuts on the order of 50 percent contemplated in some budget proposals over 10 years, are in our view not feasible if core government functions, the services that every American taxpayer expects, are to be maintained.

Respecting the integrity of a Social Security Trust Fund, channeling the interest savings from debt reduction to the Social Security Trust Fund, making proper allowance for Medicare in the context of fundamental reform and budgetary realism: If we can agree to these principles going forward, we can make a major contribution to America's economic and fiscal future.

It would be an important step for our economic future because it would continue the paydown of our publicly held debt with the projected elimination of that debt by 2015, and it would be an important step for our fiscal future because we would realistically provide funding to help us meet the existing obligations of the Federal Government that are not yet funded.

To be sure, this plan, the approach that I have described is a foundation; it is not a finished edifice. Notably other priorities would remain: the need to increase personal retirement savings, especially for the 73 million Americans who do not participate today in any of our major tax-favored savings vehicles. We will also need to make further reforms to assure the long-term viability of Social Security and Medicare. The President hopes that his comprehensive Medicare reform proposal could help provide a basis for bipartisan discussion of this critical issue in the future.

Let me conclude, Mr. Chairman, by just saying that I share the statements that you made and that members of the Minority made, that it is important that we work together in a bipartisan way on these issues; that it is important that we build on the fiscal progress that we have achieved; and that it is important that any approach we pursue be an approach that preserves the strength of the American economy and the enduring values of the Social Security program, which in many ways represents one of the most important successes of public policy over the last half century.

I am ready to answer your questions.

[The prepared statement follows:]

Statement of Hon. Lawrence H. Summers, Ph.D., Secretary, U.S. Department of the Treasury

Mr. Chairman, Mr. Ranking Member, Members of the Committee, I appreciate the opportunity to appear before you today to discuss the President's plan for preserving Social Security, which I know to be of great interest to this Committee and others in Congress.

During the last six years, the United States has made enormous progress toward putting this country's budget on a sustainable long-term path. The core principle underlying the Social Security legislation recently put forward by the President is that we should work to preserve and extend that progress—and ensure that its benefits are devoted as much as possible to meeting this country's long-term priorities.

In this context, I would like to address three topics:

- First, the dramatic fiscal progress that has been achieved in the 1990s and the benefits for the American people that have resulted;
- Second, the President's plan for maintaining this progress and ensuring that the savings it brings will not be dissipated; and
- Third, the broader significance of the President's plan and our further economic and fiscal priorities going forward.

I. Recent Fiscal Accomplishments

It is fair to say that fiscal responsibility has been the centerpiece of this Administration's economic policy from its very beginning. In conjunction with strong economic growth, difficult and sometimes unpopular choices that we made in 1993 and 1997 have helped to turn years of unified budget deficits into a surplus.

In 1992, the unified deficit was $290 billion and projected to rise; in 1998, we achieved a surplus of $69 billion, and in the fiscal year just completed, the surplus increased to $123 billion. During the past two years, we paid down $140 billion of debt held by the public, the largest decrease on record. As a result, the debt that was held by the public at the end of fiscal year 1999 was $1.7 trillion less than was projected when President Clinton took office.

The result for the American economy is that we have moved from a vicious circle of rising debt and lagging economic performance to a virtuous cycle of fiscal discipline and continued strong economic growth. An additional $1.7 trillion that would have been absorbed by government borrowing has instead been invested in America's future—in its businesses, workers, and communities.

With the resources that this progress has made available, business investment has surged, with purchases of equipment and software growing at double-digit rates for six years in a row. A rising capital stock, in turn, has contributed to a rise in workers' productivity: productivity in the nonfarm business sector has accelerated to a 2.1 percent annual average rate since the end of 1995 from the 1.4 percent that prevailed from the 1970s through the early 1990s.

And higher productivity, in turn, has helped produce higher real wages and higher standards of living. For the first time in a generation, we are seeing real wages rise. Most encouraging, real wage increases seem now to be reaching a broader spectrum of Americans, with low-and moderate-income workers benefiting in addition to workers further up the economic ladder.

When the Federal government reduces its draw on the pool of savings, interest rates fall. This decline not only lowers the cost of capital to businesses; it makes it easier and cheaper for people to borrow money to purchase houses, to buy cars and to send children to college. For example, a family with a home mortgage of $100,000 might expect to save about $2000 in mortgage costs each year. As housing has become more affordable during the past six years, an additional 8.7 million families have become homeowners, and the homeownership rate has risen to a record high.

A smaller debt also means lower interest costs for the Federal government. Net interest payments since 1993 have been a cumulative $191 billion lower than projected in 1993, which amounts to roughly $2700 per American family.

In all of these ways, our strategy of fiscal responsibility is producing tangible benefits for American workers, homeowners, and taxpayers.

A similar improvement has taken place in the stance of the government budget excluding Social Security. From a record high of $340 billion in 1992, the non-Social Security deficit, just like the unified budget, has improved in every year of the Administration. Building on the achievement of a balanced unified budget, the President, in his June budget review, highlighted the importance of setting a higher fiscal objective—balancing the government's books without using the surpluses generated by the Social Security system.

Balancing the on-budget account would mean that the bonds accumulating in the trust fund would be matched very nearly dollar-for-dollar by a reduction in debt held by the public. Put differently, accumulations in the Trust Fund will truly represent accumulations of a national asset—an increased capacity to meet our obligations to tomorrow's retirees.

This is the responsible way to prepare for the retirement of the baby boom generation: increasing the productive capacity of the economy and thus making tomorrow's workers more productive and better able to meet the benefits obligations that are promised under current law. The increment to national saving from following this approach would be dramatic: under current projections the debt held by the public would be completely paid off by 2015.

II. The Right Principles for Preserving Social Security

This discussion brings us to the crucial question: If we achieve this degree of fiscal success, how should we use the interest savings that result? Should we use them for a tax cut, for additional spending, or for Social Security? The responsible answer to this question needs to take into account two important facts about the future.

First, the retirement of the baby boomers in coming decades stands to put great stress on Social Security, which is the cornerstone of our retirement system. Social Security benefits are the largest source of income for two-thirds of Americans over age 65 and the only source of income for 18 percent of them.

The system has enjoyed dramatic success in reducing poverty among retirees, helping to lower the elderly poverty rate from 35.2 percent in 1959 to around 10.5 percent in 1998—although poverty among certain groups, such as elderly widows, remains high. Without Social Security, nearly half of today's elderly would be in poverty. We should not forget that it is also a major family protection plan: nearly one third of Social Security beneficiaries is under the age of 62 and receiving either disability benefits or survivors' benefits.

The aging of our population will challenge all of these accomplishments. In fact, the Social Security trust fund is predicted to be exhausted by 2034.

Second, in making our budget plans we need to remember that the savings that would result from continuing on the current path of fiscal discipline would be very large indeed. If we follow the President's budget framework, the amount that the Federal government spends on interest payments, relative to the interest payments that would prevail if the government balanced the unified budget, would be $107 billion lower in 2011 and more than $200 billion lower per year by 2016. We believe that we should earmark those savings to meet the commitments to future retirees that are implicit in our existing Social Security system.

Let me now describe the four main principles underlying the President's approach:

The first principle is that we should respect the integrity of the Social Security Trust Fund. By ensuring that all of the Social Security surpluses are used to pay down debt, rather than finance other government activities, the President's approach enhances the Trust Fund's ability to contribute to the government's and the nation's capacity to meet its promises.

The legislation that we transmitted to Congress embodies this principle in specific rules. The legislation extends the discretionary spending caps and pay-as-you-go rules that have been very helpful in achieving fiscal discipline over the past decade. It also goes one step further, by creating a new point-of-order to protect the Social Security surplus.

The second principle is that the interest savings from the debt reduction coming from Social Security surpluses should be channeled into the Social Security Trust Fund. These transfers are the central link between our overall budget framework and Social Security reform. Essentially, we devote the savings we have earned from reducing one liability—the federal debt held by the public—to meeting another government liability, namely promised Social Security benefits.

According to the Social Security actuaries, the transfers we propose would extend the solvency of the Social Security system to 2050, compared with 2034 under current law. This approach of earmarking the interest savings from debt reduction can be distinguished from the lockbox proposals that have been discussed in Congress this year. These do not extend the solvency of Social Security by even one day—since they do not direct those savings to Social Security and thereby help to prevent them from being used for other purposes.

In considering these issues it is worth thinking about the steps that a private company would take to address a financial shortfall in its defined-benefit pension plan. Clearly, the firm would look at ways to modernize and update the pension plan. But if it were enjoying extraordinary profits, and expected to continue to do so, then its first step would be to devote some of those profits to meeting the shortfall in its pension plan.

In much the same way, we believe there needs to be broad-based and bipartisan reform of Social Security. But we also believe that our first step should be to use the opportunity presented by budget surpluses to strengthen the program's finances today.

The third principle is that we should make provision for devoting the increased resources to Medicare that are likely to be necessary in the context of any responsible approach to assuring its future. Medicare has been a great American social policy success—but there is now widespread agreement that the program requires basic changes if it is to continue that success in a new century. In fact, the Medicare trust fund is now projected to be exhausted by 2015, nearly two decades before the projected insolvency of the Social Security Trust Fund.

The reform of Medicare poses a wide range of difficult issues. The President has put forward a plan containing his proposals for modernizing Medicare and realizing the quality and cost advantages that increased competition within the system would offer. A number of other constructive reform proposals have emanated from Congress. But whichever route this country ultimately takes, most independent observers agree that even with reform, Medicare will require increased funding to extend substantially its solvency without damaging benefit cuts or tax increases. That is why we believe that we should combine reform with steps to assure the availability of increased resources for the Medicare system in the future.

The legislation that the President just submitted to Congress would reserve one-third of the projected surpluses from any use except for reform that extends the solvency of the Medicare program. To repeat, the President wants to work with Congress to achieve comprehensive Medicare reform, but we know that reaching an agreement on this complicated issue will not be a simple process. In the meantime, we should preserve the resources that will be needed to strengthen and modernize Medicare as outlined in the legislation that the President just submitted to Congress.

The fourth principle is that this nation's budget plans should be based on realistic discretionary spending plans. The discretionary caps have been very helpful in achieving fiscal discipline over the past decade. The President's plan extends them. But it would use some of the surplus, as part of a plan that extends Social Security solvency, to provide realistic levels of appropriations for the fulfillment of government's core functions.

This is a necessary and prudent response to the unrealistic spending levels envisioned, for example, in the current Congressional Budget resolution, which by 2009 would reduce nondefense discretionary spending by approaching 50 percent, assuming that defense were funded at the level requested by the President.

It is important, in considering the President's spending proposals, to remember that this is *not* a debate about making government bigger. It is about ensuring that government has the resources to fulfill its core functions. The executive branch non-postal federal civilian workforce has declined by about 16 percent since 1993—representing more than 357,000 positions. Non-defense discretionary spending today is at its lowest level in 35 years. And for a family of four with median income, the burden of Federal income and payroll taxes is the lowest it has been in 20 years.

The President's plan would increase defense spending slightly in real terms, in order to ensure military readiness and an effective national defense. However, the plan would *reduce* inflation-adjusted nondefense spending, leaving it more than 10 percent below its current real level by 2009.

Overall, the growth of discretionary spending proposed in the President's plan would remain slightly below inflation as currently forecast. We believe that such cuts are feasible, if the spending is targeted at our critical needs. Deeper cuts, in our view, are not feasible if core government functions—the services that every American taxpayer expects—are to be maintained.

Some have said that any modest increase in discretionary spending is fiscally irresponsible. I would suggest that the opposite is true. The irresponsible course would be to build the nation's budget plans on the foundation of spending plans that we can safely predict will not be achieved.

As we have seen in this year's budget debate, unrealistic discretionary caps will be exceeded—through emergencies that expand the term "emergency" well beyond its accepted meaning, or through other budgetary gimmicks. If we base large tax cuts today on the promise of unspecified deep cuts in future spending, we may create a situation in which the spending that ultimately occurs will lead to additional and unneeded government borrowing. The result would be to erode the enormous fiscal progress that this country has made—and the enormous economic benefits that have come with that progress.

III. Broader Significance of the President's Plan and Challenges for the Future

Respecting the integrity of the Social Security trust fund; channeling the interest savings from debt reduction to the Social Security trust fund; making proper allowance for Medicare; and budgetary realism—if we could agree to respect these four principles going forward it would make a major contribution to America's economic and fiscal future.

It would be an important step for our economic future because it would continue the paydown of our publicly-held national debt, with a projected elimination of that debt by 2015. We would establish the principle of using the Social Security surplus to pay down debt rather than financing other government activities. And we would free up substantial new resources for business investment and housing, further reducing interest rates and the cost of capital, and boosting productivity and American living standards.

Respecting those four principles would be an important step for our fiscal future because we would realistically provide funding to help us meet the existing obligations of the Federal government that are not yet funded. We would extend the solvency of Social Security by earmarking for the Social Security Trust Funds the savings gained from using Social Security surpluses to pay down the debt held by the public.

Thus, the principles embodied in the President's budget and Social Security plan can provide a crucial foundation for our long-term economic and fiscal future. But they are just that -a foundation, not a completed edifice. Going forward we would need to build on this foundation, because even after passing this plan, important national challenges would remain.

Notably:

- We would still need to increase personal retirement savings, especially for the 73 million American workers who do not participate in employer-sponsored pension plans. In 1994, less than half of all individuals aged 65 and over received any private pension benefits.
- We would also still need to make further reforms of both Social Security and Medicare. As I have mentioned, the President hopes that his comprehensive Medicare reform proposal could help to provide a basis for bipartisan discussions of this critical issue in the near future.

IV. Concluding Remarks

Mr. Chairman, as I have discussed, I believe that our strong economy and dramatically improving fiscal condition offer us an historic opportunity to address some of the core long-term challenges confronting our nation. Certainly, we may have very different views about how to respond to these challenges, but I hope we can all agree that this opportunity should not be wasted.

I look forward to working with you, Mr. Chairman, Mr. Ranking Member, and others in this committee and with others in Congress as we work to progress further on these critical issues in the months to come. Thank you. I would now welcome any questions.

Chairman ARCHER. Thank you, Mr. Secretary, and thank you for making your verbal presentation more succinct. I am sure we will learn even more as we read your written statement.

You made a couple of comments that I wanted to ask you about. One is I believe you said that over 15 years you would eliminate the national debt, and you are nodding in assent that you did say that. I am curious then, should we not also incorporate a provision, if this were to become law, reducing the debt ceiling in each of those 15 years so that we would be sure that this would occur? In other words, tracking what you said in the way that you plan to pay off the national debt and simply changing the debt ceiling requirements.

Secretary SUMMERS. Mr. Chairman, I appreciate the logic of the question. While the President's proposal, based on current economic projections and the economic projections of the past, proved to be too conservative, it does provide for the elimination of the national debt by 2015. I think there would be two problems with trying to legislate adjustments of the debt ceiling to reflect those projections. First, the debt ceiling has traditionally been defined in terms of gross debt rather than in terms of debt held by the public. Most economists would agree it is debt held by the public that is relevant, but the metric that has traditionally been used with respect to the debt ceiling, which is not really what is a meaningful economic statistic, has rather different properties.

Second, while these are projections, the best available projections—I believe in some ways you can argue conservative projections—they are just that, projections. And I think it would be very unfortunate to legislate commitments that could call the country's credit rating into doubt at some point in the future or could lead to repeats of what I think both sides can agree were the rather unfortunate confrontations that took place around the debt limit increase in the winter of 1996. And so the administration believes that while the objective of public debt reduction needs to be paramount, the use of debt ceilings is probably not the right vehicle for bringing that about.

Chairman ARCHER. Mr. Secretary, I think you put your finger on my concern. It is not just traditional. It has been, as far as I know, forever that the debt ceiling applies to all of the debt. The Treasury bonds that are held in the Social Security Trust Fund represent real debt to the American people to pay off. If that debt were not there, it would be held by the public because it is there to cover the expenses of the Treasury, and I think to look at it in any different way would undermine the confidence of the people in the Social Security Trust Fund.

So the total debt of the country is the, quote, "national debt," and I think it would be appropriate because I also saw an article where the chairman of the Council of Economic Advisors, Gene Sperling said the same thing: We will pay off the national debt.

You won't pay off the national debt. Your projections are if you—if everything works right, as you said, you will be able to pay off the debt held by the public, which I would call the private debt, and you would still be having an interest in the national debt and that is why you can't reduce the debt ceiling. And I do believe that it would be appropriate, in order to convey the correct portrayal of the debt, to talk about paying down either the publicly held debt or the privately held debt, whichever you want to refer to, but not the national debt. I have town meetings where my senior citizens come and they want to know that that debt that is in the Social Security Trust Fund is just as important as the debt that is held by the public, and I tell them, yes, it is. And I don't think you would want to undermine that.

Secretary SUMMERS. Mr. Chairman, there can be no question not just about the government's obligation to the debt in the Social Security Trust Fund, but the yet more profound obligation represented by the government's commitment to senior citizens to pay the benefits that have been earned by those senior citizens. And whatever we all argue about here, I think we can all agree on a bipartisan basis that we should reassure people that the money is there in the trust fund and that promised benefits will be paid. And if we all could agree that in no way were we going to rob citizens of their benefits, I think that would be a helpful step and would perhaps cause our discussions to be less divisive.

With respect to the question of a publicly held debt versus the national debt, some of this is semantic; and I will move beyond the semantics to the underlying economics. And perhaps an analogy is helpful in conveying what I think is the view of almost all the economic experts who have looked at these questions.

From the point of view of our family, if my wife or I borrow money from a bank, that is one thing. If my wife or I borrow money from each other, that is a very different thing with respect to the economic position of our family. My wife and I lending money to each other does not represent a change in the economic position of our family. Buick borrowing money from Chevrolet does not represent a change in the economic position of the General Motors Corporation. The Social Security Trust Fund accumulating an IOU from the remainder of the Federal Government does not represent a change in the underlying economic position of the Federal Government. There is no impact on interest rates from such a transaction. There is no impact on national savings. And so the crucial question for economic performance is the movement in the publicly held debt.

Of course and this is something I think we can all agree on, the IOUs in the Social Security Trust Fund represent an embodiment of what is a crucial national commitment that we all share: the obligation to pay promised benefits to our seniors. And for that reason they have great significance. But for those concerned with tracking the performance of our economy, the relevant statistic—and this is something that I think conservative and liberal economists would all agree on—is the behavior of the publicly held debt.

Chairman ARCHER. Mr. Secretary, the important thing, I think, is that you not convey to the American people that your plan pays off all the debt of the country. It does not, as you just said; because the debt, the viable debt that has the full faith and credit of the United States Government on the bonds that are held by the Social Security Trust Fund is just as much debt and is under the debt ceiling as a publicly held debt. And so I just want to be sure that you don't convey to the people you are paying off all the debt through your plan.

Secretary SUMMERS. Let me leave it at this. No American savings would be absorbed by debt under the President's plan. The Federal Government would have no net interest liability to the public under the President's plan. The consolidated Federal Government, inclusive of the Social Security system, would have no net liability under the President's plan. There would indeed be special government bonds contained in the Social Security Trust Fund under the President's plan. That indeed would be one of the strengths of the President's plan that would expand the size of that trust fund and its capacity to pay benefits.

Chairman ARCHER. And that debt is still there in the trust fund and the reason the trust fund has that debt is because the funds came into the trust fund, and rather than borrowing from the public, the government borrowed from the trust fund to pay its current operating bills.

Now, there is also the economic argument that I have heard for many, many years, that the debt that is owed to the public doesn't matter because we owe it to ourselves. That is the same sort of argument you are making now; that if we owe it to the trust fund, it doesn't matter. Economists have said for years, many economists—and I don't agree with it—that if we owe it to the public, we owe it to ourselves, so it is part of the total national budget of our society. Therefore, it doesn't matter.

But I just want to be sure that the people understand that your plan does not pay off the debt. That debt that is in the trust fund is still there, and that obligation. And I can assure the people of this country that I personally will do everything to protect the sanctity of the debt and the trust fund as much as debt to, doubly, bondholders or people who own Treasury bonds on the outside. It has the same full faith and credit of the government.

Secretary SUMMERS. Let me put it to you this way if I could, Mr. Chairman. If my family was successful in replacing the debt that I now owe a bank with debt that I owed my wife instead, I think our family's financial position would be much stronger. I think my kids would feel better off; and that is even though my obligation to my wife would be very, very real.

Chairman ARCHER. Mr. Secretary, I would submit to you that there would be a great likelihood of greater controversy between you and your wife.

Mr. Rangel.

Mr. RANGEL. Mr. Secretary, welcome to the first bipartisan step forward to resolving this Social Security problem. I am glad to see the thrust of the Chairman's questions because in addition to being legislators, we are politicians, and before we can sit down to legislate, we ought to set aside some serious political questions. My Republican friends truly believe that they can have a $792 billion tax cut and at the same time fix the Social Security system. I would like your opinion of that, because until we can set that out of the way and commit ourselves to dealing with Social Security and not the tax cut, we will be just looking for a train wreck.

Do you believe it is possible to have close to $1 trillion in tax cuts and at the same time fix the Social Security system, either the Archer-Shaw or the President's plan?

Secretary SUMMERS. I believe tax cuts of that magnitude, Mr. Rangel, would interfere with the basic fiscal progress that we have made and would put at risk the prospect of sustained economic expansion through the virtuous circle that I described, and would therefore make it far more difficult to repair and establish long-term solvency for Social Security.

I would also make the judgment that we came to a consensus in the first half of this year, and I believe it reflected the views of many Members on both sides of the aisle, that it was important to segregate the progress we were making through accumulating the Social Security Trust Fund, through what happened in the on-budget, and that a tax cut of the magnitude you described would absorb essentially all of the available on-budget resources and would therefore make it impossible to dedicate those on-budget resources to Social Security, either through contributions to the trust fund or contributions through individual accounts. And so it would make impossible, in an arithmetic sense, a solution to Social Security, except to resort to multiple uses of the fund that were being accumulated by Social Security, the kind that were quite widely criticized as double counting.

Mr. RANGEL. The second stumbling block, it would seem to me, toward the bipartisan effort to resolve the Social Security problem, is that we would agree to work from one set of books. Now, traditionally the Republicans have rejected the President's Office of Management and Budget. To my great surprise, the Republicans rejected the Congressional Budget Office, even though they had the privilege or right to appoint its Director, after the Director says that they are $17 billion into the Social Security funds. The Republicans say no, not according to their reading. And then, of course, in evaluating the Social Security program, I think the General Accounting Office might show that the Archer-Shaw plan isn't all that they say it is, and they Republicans reject that too, I assume.

Don't you believe that one of the steps that we have to take is to agree that we are going to read from one set of books if we are going to work together?

Secretary SUMMERS. It is always helpful, Mr. Rangel, to have a common arithmetic frame for a negotiation or a discussion of this sort, and I think it is best when such a frame reflects the professional judgment of some group of technical experts. I believe such an idea was behind the Congress' judgment in establishing the Congressional Budget Office some quarter century ago and I think it has proved out over time.

So, yes, I would agree with you that common dimensioning of the problem, common dimensioning of the fiscal consequences of the various alternatives is a very useful step with respect to a negotiation. And as you noted, the Congressional Budget Office has provided us with some judgments about the consequences of the legislative actions that have taken place in recent months.

Mr. RANGEL. Lastly, you will notice that, while the majority have demanded from the President his legislation for Social Security, everytime they talk about working together in a bipartisan way and their willingness to sit down with the President to review, comment, and improve their legislation, it never happens. There is no Archer-Shaw bill but, assuming that they will have one soon as Mr. Shaw suggested, don't you believe that the discussion should also be around the President's bill as well as their bill?

Secretary SUMMERS. I think at this stage, the beginning of any profitable discussion would have to be an attempt to synthesize the various elements that are contained in the various plans. I don't think at this point there is any particular plan that has been put forward that—although I hope the President's plan will achieve this status—that has achieved a situation where it could be said to represent base text for a negotiation.

I do think that we have established what I think is perhaps the key to a solution at this point, the idea that we need to marry the issue of maintaining the fiscal progress we have made with the idea of extending solvency. And what I find unfortunate in much of the discussion of Social Security lockboxes that has taken place this year and much of the discussion of the questions of raiding the Social Security Trust Funds this year, that with the exception of the President's proposal, none of that discussion has been oriented to what I think is the profoundly important long-run question of the extension of solvency.

Mr. RANGEL. Thank you.

Thank you, Mr. Chairman.

Chairman ARCHER. Mr. Shaw.

Mr. SHAW. Thank you, Mr. Chairman.

Looking back and reading over the President's State of the Union address—and I quote him directly—"We should put Social Security on a sound footing for the next 75 years." With that statement, we all jumped up and we applauded. That was a good thing and it was a thing that we came together on.

Clearly, according to your own testimony, we are falling way short of that, so the President's plan does not fit into his own requirements. I would like to also—and anyone listening to this debate must be totally confused right now about the difference of offices of OMB and CBO. They are two groups that score the budgets, and the President's own budget is with OMB, and the OMB figures are what the Congress is using. So we are going off of one set of books.

Now, it can be argued since CBO disagrees with that, they say that the President's budget goes into the Social Security Trust Fund and they say the Republican budget goes into the Social Security Trust Fund—so I would say that we have got consistency, but it is interesting how people pick up on what suits them the best when they are trying to make a point. But I think that point needed to be cleared up for anyone who is watching these proceedings.

Dr. Summers, I want to read a statement to you, "These trust fund balances are available to finance future benefits." This is up on the placard to your right. But only in a bookkeeping sense. "These funds do not consist of real economic assets that can be drawn down in the future to fund benefits. Instead, they are claims on the Treasury that, when redeemed, will have to be financed by raising taxes, borrowing from the public, or reducing benefits or other expenditures. The existence of large trust fund balances therefore does not by itself have any impact on the government's ability to pay benefits." And that was in the President's budget, that statement. I assume you agree with it.

Secretary SUMMERS. I agree with the statement, though I may or may not agree with any implication you choose to draw.

Mr. SHAW. Let me get to the implication, because that is what I want to talk to you about because I think this is very important. You made two statements in reply to questions a moment ago, both by Mr. Rangel and Mr. Archer. You made reference to money in the trust fund. Well, clearly you know and I know there is no money in the trust fund. There are only IOUs or Treasury bills.

And you made the statement just a moment ago,"by raiding the trust fund." and I would like to dig into that for a moment, because I think that is a misstatement that Members on both sides of the aisle make, and I don't think we should be making it. We can talk about raiding the surplus, but you can't raid the trust fund because there is nothing but Treasury bills in there.

What you do, and what we are trying to protect, and what I think both the President and the Republican Members keep talking about both during the tax debate, during the spending debate that we are involved in now, and certainly during the Social Security debate, is that we have set aside the surplus into what we call a "lockbox," which is a good thing; and I think the President has bought on to that and I think he thinks that is a good thing and that does pay down the debt.

But I do want to talk about that trust fund and how it is made up. You keep talking about IOUs from Chevrolet to General Motors.

Let's put it in an even simpler case. If you write yourself an IOU—not your wife—if you write your IOU, that is not a real economic asset, is it? If you put it on your bank statement and apply for a loan and say that you are a millionaire because of that note, you would be in big, big trouble for bank fraud. So it is not a real economic asset.

Just as the President said in his own budget, the Treasury bills, where they are an obligation to pay future retirees, you cannot call that a real economic asset because it is an IOU from the government to the government. So when you start talking about real assets, you have really got to get something out there other than just the IOUs, and this is what we keep trying to get involved with.

Now, I think we have an opportunity to take on much of what the President is talking about. I think taking what we don't put into real economic assets should go to pay down the debt, and I think that is a good thing, but I don't think we should confuse the debate by saying that we are increasing solvencies by 16 years when you and I both know that in the year 2014 we are going to have to tax the devil out of the American people in order to keep benefits where they are today. That is what we have to avoid and that is what Archer-Shaw avoids because we protect those benefits, and this is not what the President does.

Secretary SUMMERS. Mr. Shaw, you have—you have suggested the need to clarify two things that I said for the public, and I would like to just respond briefly on each of them. First, with respect to CBO and OMB, it is my understanding that on a consistent application of CBO scoring, the congressional Majority's budget proposals would result in an approximately $17 billion on-budget deficit; that there have been constructions put forward that involve the use of OMB for some issues and CBO for other issues based on which would produce the most favorable scoring, that have been argued to produce a balance; but that I am not aware of a consistent accounting by anybody on which the proposals that have been put toward by the congressional Majority would result in on-budget balance.

With respect to the question of the meaningfulness of the IOU, Chairman Archer and I discussed that a little earlier. Chairman Archer made the point, with which I completely agreed, that there could be no possibility that the promise represented by those securities in the trust fund would ever fail to be honored, and in that sense, from the point of view of those who are looking at retirement and those who are looking at assessing the Nation's political commitment to meeting the benefits, could certainly take consolation from the fact that the fund that had been established for that purpose had been augmented by the actions of their government. So in that sense, I believe that the extension of solvency, extension of solvency such as that contemplated, would lead me to be more confident of the security of my children.

Mr. SHAW. Dr. Summers, you and I both know that those notes are going to be paid off out of the hide of future taxpayers and that is what I am concerned about. We can plan ahead now and that is what we need to do.

Secretary SUMMERS. We agree completely on that, Mr. Shaw, but the way to assure that it doesn't come at the hide of future taxpayers is to assure that we make the fiscal space to pay those benefits. And the way we can make the fiscal space is to pay off the national debt and to remove the 2 to 3 percent of GNP that we have been spending on interest so we don't have to meet that expense, and we can use the revenues that used to go for the purpose of serving interest instead to the objective of meeting Social Security benefits. I think that is the highest and best use that we can make of our savings from eliminating the national debt. That is the basis of the President's approach.

Chairman ARCHER. Mr. Shaw's time has expired.

Mr. Houghton.

Mr. HOUGHTON. Thank you, Mr. Chairman.

Mr. Secretary, I have some numbers here that show through a 75-year period in terms of costs of the various plans, Archer-Shaw, Kolbe-Stenholm-Kasich-Gramm, and the President and the current law. Maybe you could explain to me that for a 75-year plan under the Archer-Shaw plan it costs $64 trillion and under the President and current law it is $77 trillion. That is over a 75-year period. The others are in the same range as the Archer-Shaw plan. It is in the low to mid-sixties. Why the difference in that increased cost?

Secretary SUMMERS. The reason I believe, Mr. Houghton—and I may be corrected from behind me—is that the plan, the Archer-Shaw plan and a number of the other plans, assume that the monies will be invested in the stock market and assume therefore that there will be a high return earned. And because of the assumption that a higher return will be earned, the necessary contribution year by year is reduced. That is at least one major difference.

What I think is perhaps the more relevant measure of cost to the country is the present value of the benefit liabilities incurred—which, discounted at a common discount rate, which is the way a business would assess its pension liabilities—and if you do that calculation, of course, any plan that preserves the existing benefit structure will have the same 75-year present value cost. But I think what is driving the differences in the numbers that you describe is the assumption about the use of the stock market, which is obviously something that could be brought into a number of different approaches.

Chairman ARCHER. Would the gentleman yield?

Mr. HOUGHTON. Absolutely.

Chairman ARCHER. I don't think that is true, Mr. Secretary. He is talking about the raw costs without any feedback revenues coming off of the investments. Because over 75 years SSA has projected that the Archer-Shaw plan would generate $122 trillion surplus, unified budget surplus, and that does include the earnings from the private sector.

Secretary SUMMERS. Excuse me if I am not getting these numbers right. I think the point I was making, Mr. Chairman, I wasn't addressing the feedbacks and extra corporate revenue or anything like that. I was simply saying I think this is an analytical point, not an advocacy point in any direction. If you assume that a liability in 2030 is going to be met by putting in $1 today and that $1 is going to earn 6 percent each year, then you have to put a smaller amount of money aside than if you assume it is going to earn 3 percent real each year.

And the difference between your approach, one of the differences between your approach and the President's plan in the form that it has recently been submitted is that your approach, as you highlight it, Mr. Chairman, takes advantage of the returns offered by the stock market; and if you assume that those returns will freely be available, then you can reduce your contributions by doing that.

Clearly, I think a full analysis of that would need to recognize the risks involved, since the stock market may perform better or may perform worse than the figure that is embodied in the actuarial projections.

Mr. HOUGHTON. There are always risks when you go into the market, and I think the President and everyone in Congress recognizes that.

What I am trying to get at is this. The President's plan uses the excess FICA or Social Security income to fund the plan, entirely apart from dipping into general Treasury or general government funds later on. But the difference here, I think, is with the individual equity accounts and what that generates. That to me would be the difference between the Archer-Shaw plan and the President's current plan.

Secretary SUMMERS. I would agree with you in part and disagree with you in part. I agree with you that the difference resides in the equity accounts. One can imagine, it seems to me, a number of different approaches to equity involvement. One approach which some have advocated is a Chilean approach, where individuals simply get equity accounts and they invest them, and if the stocks do well, they do well, and if the stocks do poorly, they do poorly. That is one approach.

Another approach that would be towards the other end of the continuum would be an approach where you simply took the Social Security Trust Fund and invested a portion of it in equities with some independent government management scheme. An approach that is in a sense intermediate, if I understand it right, is the approach that Chairman Archer and Congressman Shaw have put forward in which there would be individual accounts, but to a substantial extent the government would be the beneficial owner of the individual accounts because the individual accounts would be used to finance—a significant portion of the individual accounts would be used to finance the base benefit. And so unless the individual—unless a person died early, or unless the individual account performed extraordinarily well, at the margin if the individual account did better or did worse, it would not affect the individual's promised benefit but it would affect the magnitude of the government's liability.

And so that approach, where the government would be involved in assuring that every individual had an account, that approach is in a sense an intermediate between the pure private sector approach, such as exists in Chile, and the invest the trust fund in equities approach. It involves many of the same issues because the government would clearly have a stake in making sure that individuals were not ripped off in the accounts; the government would have a stake in making sure that the investment policies in the accounts were appropriately prudent. There would still be a national system, and the concern that that national system could be used for some inappropriate political purpose at some point in the future would still be a concern that would have to be addressed. So that alternative involves many of the same issues that are involved with respect to the suggestion that a portion of the trust fund be allocated to equities.

Those problems may well be problems that could be surmounted with a great deal of thought. But to go back to what is the original premise of your question, that differences in cost do, as you suggest, derive from the use of equities, but equities can be used in ways that are more fully individual, like a defined contribution plan, or more fully collective as in a defined benefit pension plan, and the desire to use equities need not shape one's choice between a defined benefit plan and a defined contribution approach.

Mr. HOUGHTON. Could I say just one more thing, Mr. Chairman? Would you bear with me for a second? I notice the angry expression on your face [Laughter], but the bottom line of all of this, if you take the Social Security numbers—and forgetting about the Chilean plan or various other individual investment plans—that the Archer-Shaw plan would save the citizens of the United States over a 75-year period $13 trillion versus the President's plan.

Secretary SUMMERS. An approach based on the use of equities, which the President would also be prepared to support with appropriate safeguards but also be capable of realizing the same $13 trillion economy, and I think there is a strong case to be made for finding a formula that would prudently take advantage of the returns from equities; but these questions of political interference, the question of avoiding excessive exposure of individuals to risk, the question of making sure that any implicit liability with respect to uncertainty is managed, are all issues that have to be addressed.

Indeed, I confess that I was a little surprised when I looked at the numbers and saw that the beneficial ownership of the government of equities would actually be rather greater 30 to 40 years from now under the Archer-Shaw plan than it would be under the plan that the President had originally put forward because of the President's concern about avoiding a situation where government took too large a role in the private economy.

Chairman ARCHER. Mr. Secretary, just very briefly, I think this colloquy is very instructive, and I hope that at a time when we have a chance to move in a bipartisan way to an ultimate Social Security resolution, which I hope will be next year, that we will do more of this. But let me simply insert that even in Chile, there is a beneficial benefit to the government because the government guarantees benefits; and if the personal account does not equal that, the government has the responsibility to pay the difference. So I just want to point out that that very same beneficial interest to the government exists in Chile.

Mr. Matsui.

Mr. MATSUI. Thank you, Mr. Chairman. I have a series of questions I would like to ask you, Mr. Summers. One is that there has been a lot of talk about a lockbox under the budget discussions going on right now that is preserving and walling off the Social Security surplus as opposed to the on-budget surplus.

We received a letter from Mr. Crippen, the CBO director recently, and he said already about $18 billion has been invaded into the Social Security surplus for fiscal year 2000. Is that your understanding as well?

Secretary SUMMERS. My understanding of Mr. Crippen's letter is as you described it, that on a consistent set of CBO's preferred budget assumptions, that there would be—that on the trajectory that we were on as of the time he wrote the letter, it appeared that there could be a deficit that would—a deficit in the on-budget of $18 billion. Of course, the appropriations process isn't yet finished. There are still issues we all face about taxes, BBA extenders. There is uncertainty about what will happen next year to the economy, so none of us can be sure of where it will play out. But I believe your basic statement that the Congressional Budget Office, applying a consistent set of its preferred assumptions, has concluded that this path would lead to deficit is correct.

Mr. MATSUI. In fact, I don't want you to speculate, but I have heard it can be anywhere from $20 billion to $40 billion, the invasion into the Social Security surplus, in spite of the fact that the Republican leadership has been sending letters stating they don't intend to invade that surplus.

Let's assume a miracle happens over the next 48 hours and they don't invade the Social Security surplus. The money just vanishes, which I suppose on the floor of the House could happen. Does that preserve and extend the life of Social Security 1 year, 1 month, 1 day, by locking up the surplus? Does it have any impact on the fact that we will begin a cash flow problem in 2014 and then a real major problem in 2034?

Secretary SUMMERS. No, Mr. Matsui. And to emphasize, just to emphasize what I think is a crucial point, the real priority, in our judgment, should be using the budget surpluses to extend solvency of Social Security. No amount of accounting rules with respect to the on-budget deficit and the off-budget deficit, the use of lockboxes, will have that effect unless a specific mechanism is proposed for assuring that the fiscal space created by running down national debt is dedicated to the objective of Social Security. That is what I think is the very important contribution of the President's plan to this debate. Without that, we will not be making a meaningful change in the prospects for the Nation's meeting our obligations to our seniors.

Mr. MATSUI. You don't have to answer this, but the 2.09 percent of payroll problem over the next 75 years will not at all be altered by just locking up this so-called Social Security surplus as opposed to the——.

Secretary SUMMERS. That is correct.

Mr. MATSUI. Chairman Archer mentioned in his opening remarks and his question to you, I believe, that we don't have—you don't have a 75-year solution. In terms of the overall scheme of things, is it better to get started on this problem? Because it is a huge potential problem unless we begin to work on it now. Is it better to work incrementally and get what we can, rather than waiting for perfection and getting 75 years? It may not happen because maybe politically we just can't come to an agreement. Could you talk about that?

Secretary SUMMERS. Mr. Matsui, I think you may have been leading the witness but you have been leading me in a direction that I very much would agree with. Clearly it is better to extend solvency as far as possible and every bit of extension of solvency is important.

Second, if you think about what I think is an imperfect analogy, if you think about what is the best business analogy for a situation of this kind, looking at a corporation that based its pension plan—it would seem to me that before the corporation could accept an obligation to make further contributions beyond those now statutorily committed, would ask its workers to make further contributions; or before the corporation would contemplate the possibility of anything that would reduce the promised benefits, it would be natural to explore whether there was a financing technique available with the corporation's existing resources for better meeting the defined benefit obligation.

And indeed many would say that it was a basic principle of financial responsibility that you should look at the resources that are now available before contemplating tax increases or benefit cuts. And that is the essence of the President's approach. It seems to me it would not be prudent to get into the other issues until we had come to some collective judgment about what progress we could make based on reinvesting the progress that we have made in bringing down the debt.

Mr. MATSUI. Thank you. I appreciate your testimony today. Thank you.

Chairman ARCHER. Mr. Herger.

Mr. HERGER. Thank you, Mr. Secretary, for appearing before our Committee on this incredibly, crucially important issue before the American people, and that is preserving and saving Social Security not only for this generation but for the next as well.

I would like to follow up on my good friend from California's line of questioning and mention something to begin with, and that is ever since the beginning of Social Security in the early thirties the reason that 75 years was used back then, and the reason why the Archer-Shaw plan continues to use 75 years, was that as I understand, that involved everyone who would be in Social Security: the generation that was receiving it now; the generation that would be receiving it in the near future; and the generation that was just being born.

So I think it is very important that we continue in that light, not just with a 16-year plan, which I understand what the President says, or a 25-year plan, as my friend from California mentioned, but continue with the life span of those who are living.

Secretary SUMMERS. Just for clarity, the President's plan is a 50—year—I understand the argument for 75 years, but in the sense in which that measurement is taking place, the President's plan is not a 16-year plan. The President's plan is a 50-year plan.

I agree with you that the President—as I said, the President's plan is a foundation.

Mr. HERGER. Sixteen years beyond this present solvency plan.

Secretary SUMMERS. That is correct, or what would seem to be a goal of extending it, the necessary 41 years behind its current solvency so as to get to the goal of 75.

Mr. HERGER. But the question I would like to get to has to do with legislation which I authored earlier this year, legislation which passed the House by an overwhelmingly bipartisan vote, 416-12. And it is my understanding that the President's plan does contain a Social Security lockbox proposal similar to the one that I authored, and it was mentioned again by my friend that this is not a cure-all plan. All it does is try to stop the bleeding, if you will, of the spending of Social Security surplus dollars which has been over $100 billion a year for the last 30 years or more—to stop that now.

And the concern I have is that even though this plan passed overwhelmingly out of the House, the plan has been stalled in the Senate due to our inability to invoke cloture on six separate occasions. And, Mr. Secretary, it appears that the President clearly supports the concept of a lockbox. In fact, the proposal before us today uses many of the same mechanisms, such as points of order, as my legislation to protect Social Security dollars. And while Social Security lockbox is not the long-term answer, it would appear to be certainly an important and necessary first step.

Having said that, I have a simple question. Does the Clinton-Gore administration support the Social Security lockbox proposal which passed the House by an overwhelming bipartisan vote in May but has been stalled in the Senate; and if so, would the administration be willing to prevail upon the Senate Democrats to help move the proposal along?

Secretary SUMMERS. Mr. Herger, the administration supports the objective of assuring that the Social Security Trust Fund makes a positive contribution to national savings but believes that the lockbox legislation you are referring to is a flawed vehicle for achieving that desired objective for two crucial reasons: First, and most important, because it does not achieve what is the ultimate objective in this area, even a day of extension of Social Security solvency. Second, because it doesn't make use of what we have judged to be the most effective mechanisms for assuring fiscal discipline, those that include sequesters.

So while we continue to be eager—and indeed it is the purpose of my testimony today to underscore our eagerness to work on appropriate legislative vehicles for assuring continued debt reduction through recognizing the distinction between the Social Security Trust Fund and the—recognizing the distinction between the Social Security budget and the on-budget. That is exactly our objective today. We believe that the particular vehicle you are describing is flawed for the two reasons I mentioned, and it is also unfortunate that unlike the President's proposal, it does not take steps to provide funding for what I think we could probably all agree are serious Medicare issues down the road.

Mr. HERGER. Again, Mr. Summers, this was never intended to be the fix for Social Security. What it was intended to do was for the first time prevent the Congress and the President and the administration from spending over $100 billion of Social Security dollars on ongoing programs. This was meant to be a first step in doing that.

And are you saying the President does not support this first step of locking up these dollars so they cannot be spent on current programs?

Secretary SUMMERS. It is an appreciated step, one that we believe would have ultimate meaning and ultimate political impact to a far greater extent if the separation of the Social Security Trust Fund was explicitly linked to the extension of its solvency in the way that the President has proposed.

Mr. SHAW [presiding]. The time of the gentleman has expired.

Ms. Dunn.

Ms. DUNN. Thank you very much, Mr. Chairman. Welcome, Mr. Summers. Congratulations on being Secretary. We are happy you are here today.

I have a couple of questions, one of which relates to personal retirement accounts and the second relating to equity for women in the Social Security system.

These days I am concluding from folks who live in my district that people want more control over their dollars and certainly are not willing to stand for the 2½ percent average that is the return from current-day Social Security. The Archer-Shaw plan does provide for individual retirement accounts that can be left to your beneficiary until the time you retire and those dollars turn into an annuity.

I would like to know, first of all, is there any kind of element of personal retirement accounts in the President's Social Security proposal?

Secretary SUMMERS. In the President's Social Security proposal, there is not. The President believes that universalizing access to private savings, though, is a crucial value and as you know, he put forward his USAs, his Universal Savings Account proposal, some months ago to pursue that objective. It was his judgment that we, as I think has been a traditional judgment in our country for many years, that we need to have a three-pillar private savings system based on personal savings, based on pensions, and based on retirement security; and that the best place to respond to what—I agree with you, Representative Dunn—is a very strong feeling that people should have more control, that people should have access to more savings vehicles, is by strengthening the personal savings and pension vehicles. And, of course, as we designed USAs, we did it in a way that was particularly responsive to the set of concerns around female workers, around assuring that those who were widowed were properly provided for.

Ms. DUNN. Thank you, Mr. Secretary. As you know, we had a very successful and effective group of pension reforms in our tax relief plan that was vetoed by the President. For example, for women we had catch-up IRAs, so if they stepped away from the work force to raise children, they could come back in and do that kind of catch-up. And I was sorry to see the President vetoed this, but I think it is very important for folks to know that there is no degree of personal retirement accounts in the President's proposal.

I would hope that as we talk about a bipartisan plan, that that would be something that you would be open to considering.

Secretary SUMMERS. In the President's overall budget proposals, there was explicit provision for a personal retirement vehicle through the Universal Savings Account. The only difference was that it was segregated and clearly supplemental to Social Security in the President's approach, whereas in a number of other approaches it would be established in a way that was more competitive with Social Security, which we feel is a less effective approach.

Ms. DUNN. I certainly do hope eventually in our Social Security plan we will have that element, because I think it is a huge positive.

Let me ask you a second question. In the current Social Security program which was designed some 60 years ago, there really was very little consideration given beyond the role of the woman in the traditional—at that time, traditional family. Now huge percentages of women are working, and yet there continues to be that provision that would affect a working woman in the same way it affects a woman who is not working. At the end of her working career, she has paid payroll taxes through all these years. She is automatically given the larger of the Social Security payment, whether it is her husband's or herself. Generally it is her husband's because of certain inequities still in the pay scale. The same is true for women who didn't work.

So in essence, a working woman has wasted a lot of dollars during their working years, and this is where I become very quickly the advocate of the personal retirement account. If she can put dollars into that account, then she can provide for her own retirement, which lasts generally longer than 75 percent of the cases than men and involves fewer dollars.

Has the administration's policy looked at inequities in the old Social Security system, provided for some upgrading, updating?

Secretary SUMMERS. Yes. The President has made clear his commitment in the context of any overall Social Security reform to addressing in particular the set of issues surrounding survivors' benefits, which in about five-sixths of the cases involve women, and in some cases involve women who have had working lives outside the home, in some cases involve women who have not had working lives outside the home, in order to assure the adequacy of their benefits.

In considering the Universal Savings Accounts proposals, we were very focused, for the reasons that you describe, on providing for separate accounts for spouses, precisely so as to address the issue that you describe; although an important issue that is reflected in the USA, one I suspect you might support, is the idea that women who are working in the home should have an opportunity to make contributions or have contributions made on their behalf, because that is important work as well, and we need also to honor that work by making it possible for it to support contributions to retirement accounts.

I think this is an area where I sense there to be considerable bipartisan consensus on the need to be sensitive to the changing nature of family issues. Of course, another issue that arises in this context, Representative Dunn, is the incidence of divorce, which unfortunately is far, far more common in American life today than it was in the time of Social Security's founding, and we need to be sure that our benefit systems are as fair as they possibly can be in those difficult circumstances to all who are involved.

Ms. DUNN. I agree with you, Mr. Secretary. And I would hope that we could move those provisions into the President's Social Security proposal, because that makes me very uncomfortable to see them sitting in the Universal Savings Accounts part which may not pass House muster. So I would hope as you add detail to the President's plan, you will consider moving those provisions that help women as they move into retirement into your Social Security plan, as we have done with Archer-Shaw. Thank you very much.

Chairman ARCHER [presiding]. Mr. Coyne.

Mr. COYNE. Thank you, Mr. Chairman.

Mr. Secretary, in presenting the President's plan here today, you seem to put a premium on maintaining the progress on the economy that has been made while we work toward a solution to the Social Security problem. And as you outlined earlier in your testimony, there were a number of positive developments that took place as a result of the President's 1993 budget and the 1997 Deficit Reduction Act, but one element that you seemed to have left off was the record low unemployment, the best unemployment performance that we have had in the last 31 years. The figure came out last Friday. Would you want to include that as an aspect of what has happened as a result of the 1993 and 1997 Deficit Reduction Act?

Secretary SUMMERS. Mr. Coyne, I suspect I will be willing to take as much time as the Congress will allow me to sing the praises of our current economic performance. Clearly there is no more salient element in that than our success in reducing unemployment to its lowest level in 30 years and our success in reducing unemployment in many categories to levels that are lower than they have ever been before.

One of the aspects of the reductions in unemployment that probably gets less attention than it should is the very powerfully demonstrated statistical pattern of, in a sense, first-hired, first-fired. Which means that the most vulnerable groups in our society—teenagers, those with less education, minorities—have an elasticity of greater than 1 for 1. Therefore, the progress we have made in reducing unemployment in the overall rate each 1 percentage point reduction in the unemployment rate overall translates into several percentage points of reduction in unemployment for our minority populations or for our teenagers. And there is the further benefit that when the labor market in an area or in the country gets tight, as it does with 4.1 percent unemployment, employers work much harder to pull people into the labor force, and so the fraction of our young people who are not working and not in school has gone down very substantially as a consequence of our tight economy.

I think that in terms of things we need to do to prepare for the 21st century, educating our workers, giving them skills, including everybody, that there is nothing as effective as a strong high-pressure economy where in addition to having people looking for jobs, we now have jobs looking for people, and that means all kinds of steps for the benefit of workers that help them prepare going forward.

There is no question that low unemployment is probably the single most important manifestation along with, for the first time in two decades, rise in real wages of our economic success in recent years.

Mr. COYNE. I wonder if you could explain why it is important as we work towards a solution to the Social Security problem, why is it important to the President's plan that it have such a major component of reducing the deficit? Why is that important to the average worker to pay down the debt as part of a solution to the Social Security problem?

Secretary SUMMERS. There are two main reasons why it is important. First, reducing the debt is tantamount to a future tax cut because it means you don't have to pay the interest and the principal in the future, and it means by taking the pressure off credit markets, you reduce interest rates today. Each 1 percentage point reduction in interest rates translates into $80 a month on somebody with a $100,000 mortgage. Each 1 percent reduction in interest rates translates into something like $250 billion tax cut equivalent over the next decade. So, first tantamount to a tax cut.

Second, it makes the economy perform better. The $1.7 trillion that would have gone into buying government paper over the last 6 years that has instead gone into plant and equipment to make workers more productive, into homes for American families, is investment in our future that we wouldn't have if American savings had to be channeled into the sterile asset of government paper.

So I believe that our prospects as a country of avoiding recession, our prospects as a country of continuing these low rates of unemployment, our prospects as a country of continuing the significant real wage growth that we have seen in the last 2 years, depend upon nothing as much as they depend upon our success in maintaining these budget surpluses and reductions in national indebtedness.

Mr. COYNE. Thank you.

Chairman ARCHER. Mr. Collins.

Mr. COLLINS. Thank you, Mr. Chairman.

Mr. Summers, do you think it is wise to begin putting general revenues into a Social Security system without actually reforming the system first? I believe I read where Japan started this same thing by putting general revenues in and didn't reform a retirement system. About a third of the administrative costs and benefits come from general revenues. Is this not leading toward that same thing, because once you start doing this it is so easy to just continue, that you fail then to reform the system? And I believe it has been emphasized a number of times that we really need to reform this system, we need to reform the pay-as-you-go system, especially for those younger people at ages of 18 to 35. Do you think it is really wise to do this first?

Secretary SUMMERS. That is a very important question, Mr. Collins, and it is one we gave a great deal of thought to as we worked in advising the President as he came to his plan. The President's judgment—and I think it is the right one—is that an indiscriminate donation of general revenues to Social Security without reform probably would not be prudent, but that the earmarking of general revenues from general revenues of the savings achieved by reducing indebtedness, so taking a portion of the fiscal space that we create by bringing down the debt and taking a portion of that would be a useful spur to reform and in many ways a necessary foundation for reform efforts.

And so I would suggest to you that the context where you are generating an explicit savings by the reduction of a government liability and using the proceeds to fund a different growing liability makes this a very different discussion than the traditional discussions of general revenues that we have had historically in this country or in the Japanese example that you cited.

Mr. COLLINS. But in the long run, is this probably going to generate a better retirement system for people, for working folks, especially younger people? Because what I see happening here is that you are taking general revenues which are coming from additional taxes or other taxes and you are merging them with an already, I think, excessive payroll tax, but you are not changing the system. You still have the current pay-as-you-go system.

Secretary SUMMERS. I guess I would respond to that in two ways. First, ultimately the pillar on which any long-term retirement security system rests is the strength of the underlying economy, and by supporting debt reduction, we strengthen the underlying economy with this plan.

Second, we are not raising general revenue taxes or cutting a general revenue program to make room. We are taking the savings that come directly from reducing the stock of the government's debt and using it for this purpose, and we are not taking the whole reduction from the debt stock reduction. We are simply taking the interest savings which come from the reduction of one liability and using it to serve as another.

I make these points to emphasize that I think the President's plan is an important, desirable and valuable first step. Clearly there is also scope for addressing the kinds of issues that Representative Dunn raised, the kind of issue that Chairman Archer raised in his opening statement with respect to the retirement test and other structural issues with respect to Social Security that certainly also warrant our attention, but I think that the President's plan of using the interest savings in a sense represents harvesting a low-hanging fruit and ought to be a foundation for future efforts.

Mr. COLLINS. I know it is a first step and I hope the President will move in a direction that we can all be involved in the second step, but I am very concerned about additional revenues being placed into the trust fund for the purpose of benefits. I don't see that as a long-term solution to this problem.

Secretary SUMMERS. I appreciate your concern.

Chairman ARCHER. Mr. Portman.

Mr. PORTMAN. Thank you, Mr. Chairman. Mr. Secretary, thank you for being here and I appreciate your comments you made about increasing our national savings and importance of reducing the debt. I don't know how to say this diplomatically other than to say I think the proposal is a copout and it is a copout in the sense that, maybe to put it in more diplomatic terms, it is, as Mr. Matsui said, a start. He said it is an excellent start but he said it is a start.

You said it is harvesting the low-hanging fruit, it is a useful spur to real reform, it is the necessary foundation to reform.

You have only got a year left in this administration. As you know when you became Treasury Secretary, many of us believed strongly that given your background and your interest in grappling with the issue of retirement savings generally, that we might be able to spur some real reform in the next year rather than just issuing a proposal that moves some money around that in the end could spur reform for somebody else.

I also think we are setting the foundation now for the next administration. I believe next year we could handle this issue if we had a real proposal on the table, but in any case I think unfortunately, whether it is the Gore administration or the Bush administration, whoever it is, they will be using this as their foundation too, and I am afraid we haven't gone far enough. I would hope we could go further. The Archer-Shaw proposal is out there. As you know, it is a substantive proposal that makes real reforms. It can be analyzed in different ways but it is a real reform and it does save Social Security, not just for 75 years but forever.

I would just like to focus on two specific things if I could. First is what does this do? As I analyze it, what it does essentially is it takes a page from the Wally Herger Republican book and says, let's stop the raid, which is fine and that is good and I think the President now is on board with that. It just means that the money going in from our FICA taxes doesn't go for other government spending. Instead it is used in the Social Security Trust Fund to pay down the publicly held debt, which is fine; and then the additional angle that you all have added in this proposal, is to the extent there is interest savings to the taxpayer because the debt is being reduced, which is a good thing, let's take that calculation of what that interest savings is, which is general revenue, and let's pump that back into Social Security benefits; and by doing so we keep the system solvent until about 2050 instead of 2034, so it is 16 more years you get from putting more general revenue.

That is fine. You can use any calculation you want. It doesn't have to be the interest savings. It can be any amount of general revenues. It is general revenues. But I really hope we can move beyond this and get into some real reform.

I guess I have two quick questions for you, and if I have time, I want to talk a little bit about retirement savings generally, because I do appreciate very much your focus on that and the need to help everybody plan for retirement through IRAs, private pensions and so on.

Would you say that by making some structural reforms to permit some kind of private savings—and let's take the Archer-Shaw plan because there are so many different assumptions you could make, but taking some part of the Social Security Trust Fund surplus and allowing that to be invested directly. And let's say it is individually directed, although that is not necessarily relevant to this question. Do you think that would encourage and increase economic growth in this country? What would the macroeconomic impact be?

Secretary SUMMERS. The crucial question for economic growth in the country comes not from the question of a portfolio composition of assets, comes not in my judgment from the question of the trust—the question of the trust fund per se, but comes from the impact of any proposal on national savings which, of course, is the sum of public savings and of private savings.

The reason why I believe that the President's approach is probably in many ways the most constructive for economic growth is that it is consistent with maximizing the level of public savings, whereas some of the proposals that have been put forward would include on the side very large tax cuts, or even if they didn't include on the side very large tax cuts, would include contributions to accounts of some kind that were very large relative to the on-budget surpluses, would risk a reduction in public savings that might offset any possible benefits that would result from increased private savings under those proposals.

Now, of course there is the question, which is very much what has to be worked out in all of this, of what would happen. Is the public sector capable of maintaining a high rate of public savings for a number of years? There are those who are—who feel that the lesson of experience is cynicism and who believe that that is not possible and therefore favor various kinds of tax cuts.

Our judgment is that with legislation like that proposed by the President, we can lock in the basic fiscal progress we have made, maintain large surpluses, and maximize the public contribution to the high national savings that is ultimately responsible for economic growth. That is the logic behind the President's proposal, and I think there has been a quite widespread agreement that if we can maintain the surpluses, use the surpluses for debt reduction, that is, the use of those surpluses rather than any particular kind of contributions, that can make the greatest contribution to spur economic growth.

Mr. PORTMAN. My time has expired. I would just make the obvious comment that reduction of national debt has nothing to do with Social Security per se; and the ability to get a higher rate of return and the ability to have private investment in our capital markets will, I think you would say regardless of what we do on the debt side, not as a tradeoff to debt, but that will spur additional economic growth and will lead to higher national savings because of that economic growth.

And I understand that this is the easy way to go. This is the low-hanging fruit, as you said. There is no reason for anybody to oppose a proposal that says let's pay down the debt and use that interest savings which is general revenue for Social Security, but it doesn't answer the tough question: How are we going to make this system solvent over the next 75 years or even into the future, as the Archer-Shaw proposal does? I would hope we can get together and work on that as well as working on these other proposals that you talked about, which are great ideas, but I am getting no support from Treasury on our pension proposals, for instance, although you may personally support them. I am amazed we can't come together even on the private savings side.

I apologize for taking so much time, Mr. Chairman. I look forward to continuing to work with you, Mr. Secretary.

Chairman ARCHER. The gentleman's time has expired. Mr. Levin.

Mr. LEVIN. Thank you. Mr. Secretary, I am a bit perplexed. You know there is a discussion that the President's plan covers 50 years and Archer-Shaw 75 years. The Republicans have a majority on this Committee and in the House and in the Senate. If they really were so sure of the Archer-Shaw plan, they could have introduced it by now and acted on it. We are going to mark up a minimum wage bill, I guess in a few hours, that the President opposes but that won't deter their marking it up. If it is a good plan, mark it up.

I think the problem is that there are problems with Archer-Shaw in terms of the immense amount of general funds that are used by that plan, among other problems. And so I think the question is whether a realistic plan as proposed by the President that admittedly covers or expands the security of Social Security for 50 years is better than an unrealistic plan that it says covers 75 years.

So let me just ask you to boil it down. Some people are watching. As I understand what the administration is saying, is take the savings from using monies to pay down the public debt to lock them in so that it increases the odds that Social Security will be funded. Is that—just say it as simply as you can, the essence of the plan?

Secretary SUMMERS. Pay down debt, use the savings for Social Security, reduce one liability, assure you can meet another. Those are the premises of the President's plan. Fix the roof while the sun is shining. Use the surpluses that we have today to meet the obligation that we have tomorrow.

Mr. LEVIN. And as I understand it, the notion is that that would promote growth, right?

Secretary SUMMERS. Right.

Mr. LEVIN. And also as I understand the President's proposal, there are provisions in it to try to make sure that Congress uses the money for Social Security to extend its life rather than for other purposes?

Secretary SUMMERS. That is exactly right.

Mr. LEVIN. I would submit it is realistic if we will make those tough decisions. One of our colleagues said it is easy to do that. It wasn't easy to pass the 1993 deficit reduction package and it wasn't so easy to act in 1997, so I hope you will keep on explaining the essence of this so that we all understand that it would be a significant step even though it would leave unresolved issues beyond the 50 years, right? That is acknowledged.

Secretary SUMMERS. [nodding in the affirmative.]

Mr. LEVIN. Let me just say one thing because there is reference to Chile and that is kind of a motto for our doing something. In Chile, the way that the private accounts can be invested is quite heavily regulated by the government. And one of the problems with a plan like Archer-Shaw is that there is a danger that it becomes kind of a gamble and the government picks up the loss if the gambler loses.

So I would suggest, Mr. Secretary, that you persevere and encourage this Congress to take what I think would be a courageous step, and that is paying down the debt using the surpluses that are saved for Social Security, promoting national growth, and taking steps to try to be sure that the savings from lower or no interest payments are used for Social Security. That would be a courageous step by this institution.

Secretary SUMMERS. If I could just amplify briefly, Representative Levin, on your comment. I think it is a misconception to believe that somehow this is the easy way that avoids a tough choice.

I think very much the opposite. The tough choice embodied in the President's approach to make the investment in the future of our country by reducing debt is by forswearing what is always the enormously strong temptation for all of us to propose new programs, expensive new programs or to propose large tax cuts, and instead to work at paying down debt. Those are the difficult and real choices that we can make that will benefit our economy and benefit our national retirement system.

And I think the alternative approach of precommitting today large amounts of resources in the form of tax cuts or contributions to accounts and so everybody is getting—everybody is being promised something, and no resistance to future spending or future tax cuts are being built in, is in many ways the easier approach and I believe is the less prudent approach.

So while I urged that the place for us to begin and in many ways the easier Social Security policy was a policy using the savings from debt reduction, I don't want to be misunderstood. The most important consequential and I believe courageous choices that we face involve whether we commit as a country to debt reduction over the next 10 years. I believe that the President's approach can help us make those choices in the right way and that is why I think it is so very important.

Mr. LEVIN. Thank you.

Chairman ARCHER. Mr. Hulshof.

Mr. HULSHOF. Thank you, Mr. Chairman.

Mr. Summers, welcome. I was going to try to resist the temptation until the last gentleman's question, resisting the temptation to make the difficult choices or to expand additional government programs like hiring 100,000 new teachers, or Federal monies to purchase private lands for public consumption. I agree with you that those choices are extremely difficult.

I do want to just focus on, however, some of the things that you summarize in your oral testimony and your written testimony specifically talking about the four principles that the President and you agree with, and one of them is that we should respect the integrity of the Social Security Trust Fund. That was the first principle you talked about by, quote, ″ensuring that all of the Social Security surpluses are used to pay down debt rather than finance other government activities,″ end quote.

Now, about 10 months ago, the President addressed a joint session of Congress in the Nation in the State of the Union address and said we should take 62 percent of the Social Security surpluses and set them aside. To what do we owe this change of position from 62 percent in January now to 100 percent—which I am reading at least in between the lines—to what do we owe that change of position by the President of the United States?

Secretary SUMMERS. Let me just respond first to the earlier part of your question, if I could, Mr. Hulshof, with respect to the teachers and the police.

The President and I make no apology for proposing a budget that includes proposals that address what we think are crucial national needs. What has been accomplished in the last 7 years, for the first time since the Second World War, is a protracted period in which the size of government has been reduced by some 600,000 workers, by more than 13,000 workers at the Treasury Department.

What is embodied in the President's proposal is continuing reductions in the size of civilian government, with spending that does not keep up with inflation, even as new priorities are accommodated.

With respect to the 62 percent and the 100 percent, the President's initial budget was crafted in the context of a unified surplus framework, and he proposed the allocation of a certain portion of the unified surplus to Social Security.

As the debate evolved, it became clear that there was a strong desire in the Congress to frame these issues in terms of a separation between the on-budget and the Social Security off-budget. So the President recrafted his basic approach of using the surpluses and the debt paydown to finance extensions of solvency into that framework and that improved proposal, or proposal that has been responsive to the concerns of many in Congress, including, especially in your party, is the proposal that I am presenting here today.

Mr. HULSHOF. Also in your testimony, in your written statement, you mention Medicare, and, as Mr. Greenspan who appeared before us earlier this year said, fixing Social Security, I am paraphrasing, is a walk in the park compared to fixing Medicare. And I want to point out that there has been a bipartisan commission that came very close, absent one vote, of having a very realistic reform of the Medicare system.

My time is about to expire. Let me quickly ask, regarding the President's proposal, is the President still interested in eliminating the earnings penalty, and is it included in this plan?

Secretary SUMMERS. Yes, he is, and I don't know whether it is included in this particular—in this particular piece of legislation which goes to the overall fiscal framework, but that is a continuing—that is a continuing commitment on the President's part.

Mr. HULSHOF. Are the USA accounts included in this legislation?

Secretary SUMMERS. I believe not.

Mr. HULSHOF. As a final point, and in the remaining time that I have, as a complete pandering new father of a daughter who is 10 days old, I just—President Ford, former President Ford, was just recently honored with the Congressional Gold Medal, and something that he said in early 1977 regarding Social Security being the third rail of politics, former President Ford said that our conscience demands what our children deserve; God willing, we will disappoint neither, which I hope that we will continue to use as our theme if we are truly serious about restructuring Social Security for not only today's seniors, but for tomorrow's.

Thank you, Mr. Chairman.

Secretary SUMMERS. Mr. Hulshof, congratulations on the birth of your daughter. It is a reflection on the remarkable progress our country has made and is making in many spheres that your daughter, like my twin 9-year-old daughters, can, according to the—according to some of the best available experts, have a chance of 1 in 3 or even 1 in 2 of living to 100, and those improvements in life expectancy really point in another way to the importance of the challenge that is before us of preparing our economy for the challenge of an aging society.

Mr. HULSHOF. Thank you, Mr. Secretary.

Chairman ARCHER. Mrs. Johnson.

Mrs. JOHNSON of Connecticut. Thank you, Mr. Chairman.

Welcome, Honorable Secretary Summers.

First of all, I am very concerned about the fact that your proposal condemns anyone who is 14 years or under to no Social Security. If you are 14 years old now, if you are 13, if you are 12, if you are 11, if you are 10, since your program would leave Social Security bankrupt by 2050, they will get no Social Security benefits. If you are 18, you will only get 4 years.

So I just want to say that because I want to highlight that.

Secretary SUMMERS. Well——.

Mrs. JOHNSON of Connecticut. Wait a minute. Let me just finish because the real core of my question is later on.

I just want to highlight how important I think it is that when we take action on Social Security, we take action to the 75-year measure that the law requires, because it takes a long time to build consensus on reforming such a big program, and it is just imperative that we not let ourselves fall short of that 75-year measure.

Now, I do want to comment. You described your—and ask you a question. You described your proposal to one of my colleagues as very simple. We simply want to take the savings from the interest on the debt, as we reduce the debt, and dedicate it to Social Security.

Now, first of all, that is just general fund tax revenues, and the question is, do we take general fund tax revenues to fix Social Security?

Currently, currently, if we do nothing, just under current law, in less than 5 years, I don't remember the exact amount, but in a handful of years this Nation will be spending 44 percent of all the money that comes into it on people over 65.

Now, you talk about your daughters and you talk about Kenny's new baby. You know, there is a limit to how much of the Nation's resources can be spent to support our grandparents, as much as we love them, and they will tell you the same thing.

So your solution, and my concern about your solution, is that all the money you are taking is from the general revenue—the general revenues of the Nation, and you are pushing—you are going to push that 44, because that's without any change, up toward 50. At a certain point, fairness and equity, how will we fund the public schools? How will we fund environmental enforcement? How will we fund the much more state-of-the-art airport system?

So I liked your first idea better, and I know you abandoned it for a good reason, but at the beginning of this discussion, the President understood that we needed to bring the higher earnings capability of the market into Social Security. In other words, we needed new resources, but we could get a significant portion of the new resources from the market.

You proposed the government investing the surpluses. Everybody agreed the government should invest the surpluses. Now, my

Chairman and Mr. Shaw have proposed a very useful way of using Social Security surpluses going on down into individual accounts, not unlike the Federal Employees Retirement Plan, and through that mechanism creating real assets and, therefore, real new money into the system.

Now, laying aside the technicalities of this challenge, that seems to me—and furthermore, recognizing your USA account, this seems to me ground on which we ought to be working together. That is one issue.

Your other comment that you made, strengthening pension plans is very important. Fifty percent of Americans do not work for an employer who provides pension benefits, and yet if we do it only the USA account way, again, it will be general revenues, more general revenues, to support retirement security. If we do it through pension reform, like Mr. Portman wants to do, and I strongly support, and we had in our tax bill, you will enable small employers to provide pension plans and bring the power of the private market to the earning capabilities, the retirement security planning of employees.

So in pension reform, we have a chance to bring outside resources to help that 50 percent who don't participate if we reform our pension laws.

If we look at the Archer-Shaw proposal, there are ways to bring the higher earnings of the market in to strengthen Social Security in a way that is absolutely secure, respectful of the job of Social Security, and would make a difference long term and have very, very solid projections against it. Whether you like every detail of the Archer-Shaw plan, it does secure Social Security for 75 years or all time.

That is my concern. You use entirely general revenues. In the long run, that is not going to be supportable. You had ideas similar to those of the Chairman. Can't we work together on trying to get those earnings in? Can't we work together on pension reform? Can't we work together to use public and private resources not only to secure Social Security, but to give people much greater retirement security both in terms of monetary income and health care?

Secretary SUMMERS. Let me respond by saying five things very quickly. First, on budgets for seniors versus others, I hope you will pass your concerns on to the appropriators as we work to ensure adequate funding for COPS, for teachers, for technology——.

Mrs. JOHNSON of Connecticut. I will, but I will just say——.

Secretary SUMMERS [continuing]. In these last, in these last few days.

Second, with respect to—I am sorry.

Mrs. JOHNSON of Connecticut. I am just very proud that the Republicans have brought a very good Medicare reform bill to save all those providers outside there, and we hope the administration will support us on it.

Secretary SUMMERS. I am sure we will work something out. That is one area where I expect we will find some bipartisan cooperation.

Second, with respect to fiscal space, I agree with you about the dangers of new, unpaid-for claims on general revenues, and that is why the President's proposal is carefully crafted to assure that any claims it places on general revenues use only a portion of the general revenue savings that it achieves by reducing future interest burdens through debt paydown, because I think you are absolutely right about the dangers of unpaid-for claims on general revenues, and I might say that in that regard I do have some concerns about the Chairman's proposal, which I think does potentially involve larger use of general revenues.

With respect to the use of equities and the power of the market, I continue to be very sympathetic to the sentiments that you expressed, with these qualifications: I think we need to assure that the risk is not borne to a dangerous extent by individuals. We need to ensure that we do not have excessive government intrusion into the economy, and we need to be mindful of the fact that we have been extraordinarily fortunate in what has happened to markets in this country over the last 17 years and that it will not always be that way; that we need to be careful not to do anything that threatens the progressivity of the Social Security System, but if we can find a way to use the power of markets subject to those tests, that is something that the President would very much support.

With respect to pensions, I share the broad sentiment that you and, earlier, Congressman Portman expressed, but would caution that in our judgment, the right priority should not be raising the limits for the minority who already have a substantial opportunity to save, but taking steps for the majority, who really have very little capacity to take—or no capacity to take advantage of tax-favored savings right now.

Finally, I agree with you very much, and I know the President agrees with you very much, on the importance of bipartisan cooperation in all of these areas, and that is something which we are very much committed to.

Chairman ARCHER. Mr. McDermott.

Mr. MCDERMOTT. Thank you, Mr. Chairman.

Mr. Summers, I must say the President's proposal, I like this one better than the other one because you took out the private accounts and those kinds of things.

I want to understand or at least hear your thinking about this whole issue, because when I came to Congress, the Dow Jones was at 3,000. It is now at 10,000. And I think it would be a little grandiose for me to take credit for doing that, but there are periods—there have been periods when we have not had that kind of growth in the stock market.

Now, if you begin in 1966, the Dow was at 1,000. It didn't get back to 1,000 until 1982, almost a 17-year period when there was no growth, and my feeling is, or at least my question, the dollar went from worth 100 cents to 30 cents because of inflation over that period of time. Why should we ever put any of our money out into the stock market if we want to make absolutely sure it is going to be there when we come to the time of retirement?

What is it that—I mean, everyone is mesmerized by the Dow Jones right now because of what it has done, but it hasn't always been that way.

Secretary SUMMERS. Congressman McDermott, you are very right in pointing to the uncertainties, even over substantial periods of time, in the behavior of what happens to stock markets, to a substantial decline in the Dow Jones average that you mentioned as one example. The performance of the Japanese market over the last decade is another example.

Clearly, stock market investments do carry higher returns on average, though those higher returns come with substantial risks.

The judgment of retirement planners in most contexts, I think about as an example State and local pension funds where there is a defined benefit obligation for workers, or most corporate defined benefit pension plans, or most of us as individuals planning for our own retirement, is that prudence can take the form of accepting a small amount of that risk in return for a higher return. The longer we have, the more risk we can probably accept, because over time it averages out.

In designing the President's original proposal, we were very mindful of this and tried to calibrate an amount of risk that would assure that the fiscal burden would be a tolerable one, even in the event that the stock market outcome was quite an unfortunate one, but I would suggest to you that what is important is that we collectivize that risk because the national government, as an entity, has a capacity to bear that risk, to spread that risk over long periods of time that any one of us, as we think about the years before our retirement, does not have.

That is why the approaches that we favor would rely on the principle of defined benefits, but would accept the funding of those defined benefits through the partial use, the prudent use, of equities. Where we would be concerned is in the use of equities for individual accounts, because to take the period that you cited, Congressman McDermott, the stock market over one interval in 1974 actually fell by two-thirds in real terms. Imagine if those were the 9 months before your 65th—before one's 65th birthday.

So I think that we have to look for approaches that are collective. Now, that, of course, has the consequence of—this is something that Chairman Archer and Mr. Shaw have recognized in their plan, in guaranteeing defined benefits, but when you guarantee defined benefits, you create a situation in which because the government has the defined benefit liability, the government becomes the beneficial owner. It is better off if the stock does better, just as the State of Washington is better off if its pension fund does better, given that it has a fixed obligation to the teachers.

Then the question arises whether one can find suitable means of political insulation of those equity investments in a situation where the government is the beneficial owner, and that is part of the challenge of mechanism and institution design.

Mr. MCDERMOTT. You are saying——.

Chairman ARCHER. The gentleman's time has expired.

Mr. English.

Mr. ENGLISH. Thank you, Mr. Chairman.

Mr. Secretary, your testimony so far today has been illuminating, and I really appreciate the opportunity to pose a couple of questions that I hope will clarify the President's position.

I am delighted that the President has come forward with a more detailed proposal. I believe that Social Security reform, in order to be successful, must be bipartisan. So I guess what I wanted to first get a sense of, given that a number of Members, including a number of Members of the President's party, have signed on to a variety of Social Security reform proposals over the course of the past year, can you share with us does the President see any common ground for building a bipartisan product based on any of those proposals, or does he fully oppose every one of the plans that have been presented so far in Congress?

Secretary SUMMERS. I think the President sees a number of elements in various proposals that represent important common ground: the use of the resources provided by the surpluses; the maintenance in many cases of the progressivity of Social Security; the commitment to using Social Security reform as a vehicle for encouraging fiscal discipline; the desirability of addressing the special needs of widows and more generally the changed nature of the American family since Social Security was founded; the need to address the retirement test.

These are all very important points of common ground, that the President sees them as things on which he can and we are very much prepared to build. But there also are lines that are not possible to cross: exposing individual workers to excessive personal risk with respect to their benefits; threatening to unravel the fabric of a system which provides in a number of different ways for progressivity and for transfers across individuals that we need to preserve both now and in terms of avoiding any political dynamics that could lead to its unravel. There are a number of other——.

Mr. ENGLISH. Mr. Secretary, I think those are very good general principles, and perhaps we could follow up in writing and spell out some of those differences in a little more detail. I think it is important for us to understand where those lines are if we move forward, as I hope we do, and try to build a concrete bipartisan proposal on Social Security.

Let me say on one particular issue, the President's original proposal in embracing the idea of relaxing the earnings limit for recipients of the old age retirement system, recipients who currently, if they continue to work, face higher tax rates than Donald Trump. I was very encouraged that the President embraced the idea of getting rid of that earnings limit in his earlier proposal, reversing a position that administration Representatives had taken when they had previously testified from that seat before our Committee.

Mr. Secretary, I noticed in the current proposal there is no reference to eliminating the earnings limit. Can you give us a sense of what the administration's position is now?

Secretary SUMMERS. Yes, I can. The President continues to support the need to eliminate the retirement earnings test; to reduce poverty among elderly women. He believes that the details of these proposals need to be worked out as part of the bipartisan efforts to build on the foundation. His plan would provide and extend solvency for at least 75 years.

I can't resist, Mr. English, since you made a comparison of marginal tax rates, suggesting that, without referencing any particular individual, I would hope that this Committee's work in the tax shelter area would do something to ensure that those comparisons of marginal tax rates between different individuals would be less challenging to all of us.

Mr. ENGLISH. Mr. Secretary, we look forward to exploring the administration's proposal and looking for ways of making it perhaps a little more viable and a little less arbitrary, and there may be some common ground on that.

On a final point, I noticed that you have, as Mr. McDermott noted, dropped the idea of USA accounts in this legislation. Why is that?

Secretary SUMMERS. The President's legislation was an attempt to codify the fiscal framework that would underlie an expansion of Social Security—of Social Security. We would hope to return next year, in the context of our overall budget discussions, to the question of private savings, which I think we can all agree is something that is very important, and that it is very important that we find ways of spreading the benefit of tax-favored savings to a larger fraction of Americans than now—than now enjoy them.

At this point in the tax debate, when the tax discussions are largely and, in my judgment, appropriately focused on extenders, and, in my judgment, extenders that should be fully paid for, that did not seem the appropriate moment for a broader tax policy discussion.

Mr. ENGLISH. Thank you, Mr. Chairman.

Chairman ARCHER. Mr. Foley.

Mr. FOLEY. Thank you very, very much, Mr. Chairman.

Mr. Summers, thank you for your appearance today.

Mr. Rangel raised some questions earlier regarding the tax policy of this Committee, and we had advocated a tax cut. Would you acknowledge that the tax cuts we initiated, the capital gains tax cut specifically, had the influence, if you will, of increasing transactions and increasing revenues to the Treasury vis-a-vis the sale of those underlying assets?

Secretary SUMMERS. I am sorry, Mr. Foley. Are you referring to the 1997 tax changes in this?

Mr. FOLEY. Right.

Secretary SUMMERS. Or are you referring to proposals that were contained in the legislation this year?

Mr. FOLEY. I am referring to prior tax cuts that have been initiated into law. Do you feel that they stimulated revenues to the Treasury?

Secretary SUMMERS. I have not seen a careful analysis of the last 2 years' statistics. It was our—it was the judgment of the Treasury, and I believe the judgment of the Joint Committee at the time, that while there would be, particularly at the beginning, some induced realizations as a consequence of those tax changes, that the net revenue consequence would be negative, for two reasons: Because each of the transactions would yield less revenue, so even if there were more of them, unless there were a lot more of them, you would still be realizing less revenue; and because the reduction in the capital gains rate would encourage various kinds of shelter opportunities—that is perhaps a pejorative word—various kinds of situations in which transactions would be created where individuals took interest or depreciation deductions at the full rate and then took capital gains on the other side of the transaction, and so one might see larger volumes of capital gains revenues, but the total collections of the tax system would nonetheless be reduced once one took account of the offsetting deductions.

So while there were undoubtedly some feedback and economic offsets, I have not seen any evidence that would call into question the judgment that was reached at the time, that there was a net revenue cost of those proposals.

Mr. FOLEY. On Social Security, the President had initially proposed a government investment vehicle, if you will, where the government would invest in equities. Would you explain to me the difference why the government is a better investor in the equity speculative market versus the investor, the individual, the IRA account holder, in a stand-alone or side account established? What makes the government a more wise investor and insulates the government and the taxpayers and Social Security from risk? Why shouldn't the individual have that same liberty to make judgments based on the marketplace?

Secretary SUMMERS. It is not a judgment, Congressman Foley, that the government is a superior investor. Indeed, in no proposal of which I am aware would the government exercise investment discretion. It would simply ask market managers to—private managers to track published indices. So there is no notion of the government exercising discretion as an investor.

The crucial question is the one I referenced in the conversation I had with Mr. McDermott regarding the spreading and bearing of risk. If, as is common in Social Security arrangements, one envisions annuitizing a stream at the age of 65, someone who faced a situation such as occurred in 1974 or occurred in 1987, where the stock market fell by a large margin in the 6 months or the year prior to a person's retirement, could see their retirement annuity fall by one-third or fall even in the 1974 case by two-thirds because of an adverse movement in the market.

Mr. FOLEY. Wouldn't that be the same result if the government was investing?

Secretary SUMMERS. No, because the government could function like most States do, with their defined benefit pensions, or most corporations do, with their defined benefit pensions in providing a fixed benefit and then managing the fund to finance those benefits so that over time the fund would do well—the fund would do well at certain points, and the fund would do poorly at certain points, but it would be possible to maintain a fixed level of benefits.

The government has a capacity, by virtue of being a permanent institution, to spread risk over time that an individual facing retirement at a particular point in time does not have. That is why most State and local governments have adopted defined benefit pension plans for their workers.

The basic premise of why Social Security was started was the premise of the government's ability to spread risk across individuals and spread risk over time, and, therefore, to provide for defined benefits. Indeed, that is something that is very importantly recognized in Mr. Archer's and Mr. Shaw's plan, where for the vast majority of individuals, they would be getting a guaranteed government benefit regardless of how the stock market performed, and only in cases where the stock market performed extraordinarily well would there be the possibility of supplementation of those benefits, or at least that is my understanding. Perhaps it is wrong for me to be trying to characterize the Chairman's plan.

Mr. FOLEY. Let me just—I know my time has expired, but following along on that thought, would you be agreeable to pursuing the initiative of Mr. Shaw and Mr. Archer based on, if you will, a mutual fund concept?

You mentioned the government would have these independent private equity managers that would go out and make the risk assessments and insulate, if you will, from a certain degree risk. Using the Archer-Shaw model as a separate account and IRA account, but using your model as a global money manager, allowing individuals to have, as we have in Congress, 401(k)-type plans where you designate your deposits but aggregate them so they are not separate and apart, but they are indeed investing in private vehicles, but ownership would reside would the individuals, would you concede that that may be something to look at?

Secretary SUMMERS. These are certainly questions—certainly all ideas, I think—these are sufficiently important questions that I think all ideas should be looked at, and the question of the definition of ownership in a situation where there is going to be a guaranteed level of benefits, it becomes a little bit unclear what one means by ownership.

I mean, just to use an example, if it is said that I am going to pay you $100 1 year from now, but that you have an account in which $2 has been placed in the stock market, which is going to be used as one component of that $100 that I owe you, so it is very unlikely that the $2 would come to exceed $100, then who is the real owner of that?

Is it you because it is said to be your account, or is it me because those $2 are going to be—if it turns into $4 or $6, that is going to reduce my payment from $98 to $94? I am not sure in that case who one should think of as the owner of the account.

There is a similar kind of ambiguity that is involved, it seems to me, in thinking through Chairman Archer's proposal, but it is certainly—and Mr. Shaw's proposal, but it is certainly a very valuable contribution to thinking through what I think we all agree is a very powerful idea, which is the use of markets to help make—to help assure increased solvency with a minimum of any changes in tax rules or benefits.

Chairman ARCHER. I hate to call the end of time when you are on such a positive note, Mr. Secretary, but the gentleman's time has expired.

Mrs. Thurman.

Mrs. THURMAN. Thank you, Mr. Chairman.

Mr. Secretary, I am sorry I wasn't here. We were out doing another issue that many of us are concerned about on pharmaceutical assistance for our seniors in this country, so I apologize for not being here.

The only question I want to ask you is: What is the significance of us not doing anything? And how long do you think, in your judgment, we have to really work through this issue before it does become a problem and we can't do anything without adding lots and lots of money to the system?

Secretary SUMMERS. Mrs. Thurman, Hippocrates had a very powerful principle when he said, first do no harm, and I think it is of the greatest importance for these issues that we respect that principle and not take steps this year or in any subsequent year that interfere with the broad progress we are making in paying down national debt. That is why I am very concerned about the reluctance in parts of the Congress to accept the various offsets, particularly the tobacco policy that the President has proposed this year, and to maximize the fiscal integrity of the outcome that we come out with this year.

That is why I believe it is very important that tax extenders legislation be paid for in the interest of our economy to achieve that objective. I believe that to the extent possible that should be done with respect to any legislation, such as the important objective of repairing problems that have arisen with Medicare providers.

So, overwhelmingly, I would assign importance to assuring our progress in continuing to reduce debt. Beyond that, I don't know that there is a point where one falls off a cliff, but it is the arithmetic of compound interest, and it is common sense that the sooner we move to address these problems, the less painful the necessary adjustments will be, and that now at what is such a fortunate moment for our national economy, it seems to me to be—when we have surpluses to commit, it seems to me to be an ideal time to address the challenges facing both Social Security and Medicare.

Mrs. THURMAN. And as this economy continues to grow, we have also seen, I believe, over the last couple of years, so does the solvency of the Trust Fund. So everything that you are talking about that is working, and if we can continue keeping that moving the way it should, puts us in a better position at any time to work through this.

Secretary SUMMERS. I would agree with that.

Mrs. THURMAN. Thank you. I thank you very much for spending the time with this Committee today.

Chairman ARCHER. Mr. Weller.

Mr. WELLER. Thank you, Mr. Chairman.

Mr. Secretary, good to see you. Good afternoon.

Secretary SUMMERS. Good to see you.

Mr. WELLER. You have been here for a while. I appreciate you taking the time to be with us today.

Before I begin a couple of questions, I would like to ask you on Social Security—of course you brought up the issue of education, which, of course, is a major priority in this Congress. This last weekend I had a discussion with a local school board member. In Illinois, our school board members are volunteers, but they are elected officials, and it is their job to set the priorities in the local school district, particularly how they spend their money.

He asked me to convey, if I ever had the opportunity, to our friends in Washington, he says, you know, we are pretty good people out here. We feel we have a pretty good understanding of the needs of our communities, but we sure would like to have some greater flexibility on how to use the dollars we have to spend.

He pointed out that while about 6 percent of the money that comes from—that funds our local public schools comes from Washington, so do two-thirds of the mandates. He said, you know, we are pretty happy with our class size. We are pretty happy with the number of teachers we have, and we appreciate the extra money, but we would really like to be able to decide how best to do that ourselves. Maybe we want to put that money into putting in the wire and the fiber and the hardware so we can put in computers and Internet access for our schools, and they asked for that choice. I realize that is really one of the fundamental discussions as we finalize the budget over the next couple of days: Does Washington essentially hog-tie our local school board members on how they can use Federal dollars, or do we give them the flexibility and respect to make those decisions themselves? My hope is that we will give the flexibility to our local school board members.

Now, getting to your Social Security plan——.

Secretary SUMMERS. Can I——.

Mr. WELLER. My friend here, Kenny Hulshof, has a beautiful little girl named Casey, just born last week, and we all wish he and the Hulshof family a hearty congratulations on the birth of their daughter. One of the concerns I wanted to raise about the Social Security plan that you have brought before us today is that Casey turns 67 in the year 2066. Now, under the President's Social Security plan, the proposal that you are advocating today, Social Security will go bankrupt 16 years—excuse me, yes, 16 years before it is her turn to collect. Of course, during that time she will be in the work force and paying taxes into the Social Security system.

Now, you stated in your comments earlier that the President's guidelines, since he was looking at Social Security proposals, was that he wanted to extend the life of Social Security for 75 years. Now, under the Social Security actuaries for the Social Security Administration, they state that your proposal will only extend the life of Social Security to the year 2015—excuse me, 2050, which, of course, is only 16 years later than current law, so by 16 more years of life, but it falls short for little Casey Hulshof by 16 years.

I was wondering, why did you not propose a plan that actually met the President's goal of 75 years so that little Casey Hulshof will have Social Security there when it is her turn? Mr. Secretary.

Secretary SUMMERS. Let me first say that I yield to no one in my concern for the welfare of little Casey Hulshof.

I just want it to be absolutely clear on that point.

Mr. FOLEY. We will take up a collection at the end.

Secretary SUMMERS. Frankly, because I am concerned—because, Mr. Weller, I am concerned with Casey Hulshof's welfare well before she faces retirement, I strongly support a Federal commitment to assure that she has the opportunity to go to a public school where class sizes are sufficiently small; that she can receive adequate attention, and that seems to me to be a particularly important Federal priority in this——.

Mr. WELLER. Mr. Secretary——.

Secretary SUMMERS [continuing]. And one we should encourage. But I am not an expert on education policy.

Mr. WELLER. Mr. Secretary, we have a philosophical disagreement. I think our school board members should be able to make those choices themselves if they have other priorities to meet the needs of their communities.

Secretary SUMMERS. I think we probably do have a disagreement there, but I think we all have a national stake in Casey Hulshof's successful education, and so earmarking how Federal money is used.

Mr. WELLER. Mr. Secretary, reclaiming my time, I would point out that our Budget Act provides more money for our schools than the President's budget.

But getting back to my question here for little Casey Hulshof, your proposal, Social Security goes bankrupt 16 years before she is eligible. And if the President's goal is to have a plan that keeps Social Security solvent for 75 years, why did you not come forward today with a proposal to keep Social Security solvent for 75 years so that little Casey Hulshof will have it when it is her turn?

Secretary SUMMERS. We would like to work together in a bipartisan way to achieve full 75-year solvency. We believe that the steps contained in the President's—in the President's proposal provide a very useful foundation for such efforts in strengthening the national economy so that Social Security will be stronger in the out years.

I think if it were possible to find bipartisan consensus on this set of starting measures, which would be a significant contribution to the Social Security system, I am confident that we would be prepared to build on that agreement and progress to see if it were possible to go the rest of the way.

Before we contemplate whole new approaches, or before we contemplate changes in benefit formulas, or before we contemplate raising burdens on subsequent generations of workers, I would hope that not as a final step, but that as a first step we could all find agreement on the idea of using the progress we are making in reducing the national debt to strengthen Social Security, and I think if we could all come together on that idea, that would be a powerful spur to taking the various other kinds of steps that are important to assure that we can pay promised benefits.

Mr. WELLER. Mr. Secretary, I noticed in your response there, you said that before you contemplate benefit changes, are you saying that after the end—after the year 2050 that there may need to be reductions in benefits for Casey Hulshof and her peers in order to extend it? Is that why you did not go beyond 50 years?

Secretary SUMMERS. I think that clearly there are a variety of steps that can be explored, changes in investment policy.

Mr. WELLER. So you are considering benefit cuts? Or are you are considering——.

Secretary SUMMERS. We have laid out our proposal, which we believe is the right basis as we go forward, for subsequent discussion. Other measures would have to be explored and debated on their own terms with respect to commitments of general revenues that go beyond the savings in interest; with respect to any consequences they might have, positive or negative, for benefits or subsequent taxes. But we believe this approach that the President has put forth provides a useful forward step and a foundation for future efforts.

Chairman ARCHER. The gentleman's time has expired.

Mr. McCrery.

Mr. McCRERY. Thank you, Mr. Chairman. I think all the good lines have been taken, so I am going to be brief.

I commend the President for at least making us all talk about Social Security. It has been a rather sensitive political subject over the years, and so I think he is to be commended for at least putting it out front and encouraging us all to talk about it.

Mr. Archer and Mr. Shaw are certainly to be commended, as are Mr. Kolbe and Mr. Stenholm, for going even further than the President has, not just tiptoeing up to the edge of the Social Security swamp, but actually diving into the swamp.

Our job, though, is to try to reconcile all of these differences and how we would approach saving this very important program.

I would hope that we would look at the offerings that you have made and take them for what they are, and it really is no more than just a temporary approach to really solving the problem.

When you look at the numbers provided by the Social Security Administration, the bottom line is the President's proposal over 75 years costs $13 trillion more than the Archer-Shaw proposal. So I would hope we could agree that maybe we should look at something like Archer-Shaw for the long term of the country and not just put these short-term blinders on and say, well, what can get through the next 10 or 20 years. Let's look longer term.

As to Mr. McDermott's point about the stock market being so unreliable. If it were so unreliable, why are all the labor unions' pension funds invested so heavily in the stock market? They must think it is a pretty good investment, and they have got the responsibility to provide pensions for their members forever.

As you have pointed out, State and local governments invest in the stock market. So, again, I would hope that we could all agree that we have got to figure out a way to get a higher rate of return for the investment that the American citizens are making through their payroll taxes to Social Security.

The President's own proposal, initially at least, held out that option of investing, in his case directly into the stock market. Archer-Shaw would have an indirect investment. But, look, if we don't do something like that, if we don't get a higher rate of return for Americans' investment, we are going to have to cut benefits or raise taxes. That's it. Let's get it out on the table.

So if we don't want to raise taxes, and you said you don't want to cut benefits, and we don't want to cut benefits, then let's cut through all of that and say, how can we get a higher rate of return? We are going to have to sit down and figure that out.

I am encouraged by the President's proposal. I am encouraged by his initial proposal. We have wasted a lot of time, in my view, in not sitting down and excluding what we all know to be politically unpalatable and figure out what we can do, what we should do, to save this system over the long haul.

With that, Mr. Chairman, I will let the Secretary make any comments he wishes on my time.

Secretary SUMMERS. If I could just briefly, Congressman, let me first say that we are comfortable with the idea, if an appropriate formula can be found, for taking advantage of higher returns that equity markets would provide. And if there could be agreement on taking the President's proposal as described, with the single modification of modifying—of investing a portion of the Trust Fund contribution in equities so that further solvency was achieved with a defined benefit structure, I would expect that that could be an agreement that could be worked out very quickly.

Mr. MCCRERY. Let's try that. Archer-Shaw does exactly that. It is a defined benefit, it is a defined benefit, just as you have said, so let's get together and work on it and see if we cannot come up with that. I mean, we are very close, I think.

Secretary SUMMERS. Well, let me say also—let me say also that while obviously in a setting like this, it is the nature of what we do that we point up flaws in approaches, I think it is important to recognize that there are some common elements, defined benefits, uses of the surpluses, and those are very important common elements.

I do have the concern that with respect to the Archer-Shaw proposal, as I understand it, and I am certainly not the authority on it that its authors are, that one does face the question of its financing and where it is to be financed from, and it isn't clear to me whether it is envisioned that it would force the on-budget into a deficit, which would represent a rather substantial contradiction between the objectives of the lockbox legislation that many have stressed this year, or whether it is instead contemplated that somehow the Social Security Trust Fund revenues would be recycled multiple times, which might get into the area that had raised concerns surrounding double counting.

We would like to take advantage of the surpluses to achieve 75-year solvency, too, but in putting forward our proposals, we have been constrained by the imperative of assuring that we don't multiply use the Social Security Trust Fund, and the imperative that we use general revenues only to the extent that we have provided the fiscal space by achieving interest reductions, and if a way can be found of respecting those two principles and extending solvency further, that would certainly be something we would be very interested in looking at and discussing.

Chairman ARCHER. The gentleman's time has expired.

Mr. Watkins.

Mr. WATKINS. Thank you, Mr. Chairman, Mr. Summers, Members of the Committee. I guess I was one of the last ones here, but I don't apologize. I was with a friend of Mrs. Robinson's and mine that has terminal cancer, and I spent some time with him during the first part of this, and so I got here late. And he was also probably most concerned about his family and all in the future.

Let me say, Mr. Summers, I think that the President erred in his State of the Union message. He realizes it. I think he realizes—I first will say I think we are making progress. The President has realized he made the error in the State of the Union message where he said, you know, that he is going to use 60 percent of the Social Security funds—or 40 percent of it will be used, be spent. If you look back at that statement and all, I have to say that thanks to this Committee, Mr. Archer and Mr. Shaw, that I think this ship has helped keep the President's feet to the fire where now he has moved in our direction.

Instead of spending 40 percent of the Social Security surplus, now we are going to be applying it to the future of Social Security and making it much more solvent. So I want to say, from his first proposal to his second one, he has definitely come a long way. I want to say I think this Committee and this leadership of the Congress has helped protect that money.

Also being kind of a farm boy, I know what it means by low-lying fruit. It is easier to pick, and it is easier to waste, and I am concerned about if from the—paying down the debt, yes, I want to pay down the debt, but how is that savings going to be utilized?

I realize exactly the steps that are being taken there, but that is also dollars or fruit that can easily go into spending. The President, as handed to him, the first proposal he realized that the American people didn't want that 40 percent spent that way, and he moved in the right direction. I am concerned about how we spend that other savings.

But I think we are making some headway, and we are investing in the future, and I don't want us to be partisan, but when you bring up COPS and education, as my friend from Illinois said, you know, we do propose more money for education, but it is going back to the local school boards and the local school administrators to be utilized in order to meet the needs of those areas, and I think that is the way it should be.

Let me say for Archer-Shaw, I have tried to look into that and study it a big deal. We have been to Chile to talk to Jose Linear about that proposal, along with a lot of other people.

Let me say it does several things. There is money left available to pay Medicare. I don't know where the President went with Medicare. The bipartisan commission was squelched. Ask Senator Breaux about that, Bill Thomas, and even the commission members. But where is the revenue going to come from to meet those needs for Medicare? Archer-Shaw helps solve that problem along the way.

We look at the individual retirement accounts. I was kind of—are you saying, Mr. Summers—I know you must not be—that everybody who has got their money in thrift savings accounts is at great risk? Should they be taking it out, as Mr. McDermott's proposal? I don't think you meant that. You left, I think, a great deal of risk there in the minds of a lot of people. I don't think it is that alarming.

But also we have got the lowest—you know this better than anybody else, I think, probably, or most, Mr. Rubin and Greenspan and others, we have got the lowest savings of any industrialized country in the world, and we need to increase savings. That is what the Archer-Shaw plan—one of the great things it would do. It would be definitely increasing that and building that up. So we can have that kind of investment there to move our country forward.

I would just like to say, I think we have—the President's second proposal, and let's give him credit for making that shift, and the Archer-Shaw proposal, have moved forward and come closer together. But you have been around here, and you didn't come in on a load of watermelons last night, and I didn't, but it is positioning. It is the bickering there.

I think the President should stand up, and I think you should advise him to stand up and take the lead in a very bipartisan way and sit down together and look at the great possible benefits we have there so we can resolve it, not only for our, yes, grandparents, our generation, children and our grandchildren. And I hope we won't be alarming the American people about one of the plans, because I think both of them are so much more sound today than they were when the President proposed his in the State of the Union message.

That is all I have to say.

Secretary SUMMERS. I am not sure I have—I am not sure that I have a response to that. I think we can all agree on the desirability of increasing national savings, as you suggested. As I tried to make clear, I think there is a lot that is very interesting in the plan that Chairman Archer and Mr. Shaw have put forward, and I raised some rather specific questions having to do with the ultimate fiscal impact of that plan, which may be worthy of further examination.

I welcome what seems to be a growing consensus on the desirability of using surpluses and the desirability of assuring benefits, and certainly I know that you can agree with me on the importance of individuals being able to rely on an assured benefit, and I can agree with you on individuals being able to accept that a certain amount of their wealth—whether this should be their Social Security wealth, I think, is a very much open question, and I would be rather skeptical—but a certain portion of their wealth invested in markets that are subject to fluctuation.

Chairman ARCHER. The gentleman's time has expired. The Chair welcomes the comments by the Secretary that we should be able to find some common ground to ultimately solve this problem. The Chair wishes very much to be able to find that ground, and I think the Secretary knows that.

Mr. Cardin.

Mr. CARDIN. Thank you, Mr. Chairman.

Mr. Summers, despite the administration's best efforts to point out the urgency for us to move forward with a Social Security bill in 1999, at the end of the day this year when Congress adjourns sine die, we will not have done anything to extend the solvency of the Social Security Trust Fund, and I find that incredible.

I support the administration's proposal. I think we need to dedicate some of the surplus to Social Security solvency, and I have heard some of my colleagues point out this is just moving money around or using general funds, but the one thing that it does is it permanently dedicates some of the surplus to extending the solvency of the Social Security Trust Fund, as you point out, by an additional 16 years or 50-year solvency. If we don't do that, I am afraid that your comment about first doing no harm won't happen.

There are many proposals in this Congress—in fact that have passed this Congress—that do not just spend more money for appropriation programs, but to do it in a way that is not good accounting. We have developed more different accounting gimmicks including calling things emergency spending that aren't emergency spending, creating a 13th month, doing some type of creative scorekeeping, all of which I don't think bodes well for the Social Security system to get a fair shake out of the surplus monies.

And then we have—we seem to conveniently have forgotten a tax bill that is sitting out there that still has not been brought, up by the way—the President has vetoed it, but for some reason it has not been brought back to the House—that would spend about $900 billion that obviously would compromise our ability to deal with the Social Security Trust Fund.

So I guess I would start out by underscoring the urgency for us to do something. I applaud the administration's effort to at least put some of this money away permanently to deal with the Social Security system as well as to pay down the debt. If I felt that Congress wasn't going to spend the money on either spending programs or tax programs, I wouldn't be quite as concerned, but I think this session does not bode well in that direction.

And then I want to mention one other thing. I agree with you that we need to work in a bipartisan effort to go even beyond the President's proposal so we can get to 75-year solvency, and I also believe that we need to do more for private savings and retirement. I support your USA proposal. I think it was a good step towards private savings.

I also, as you know, am a cosponsor with Congressman Portman on a bill to reform our pension laws. If I might make a plea to you in that regard. I agree with you that our priority must be to get people who are not currently putting money away for their retirement to put money away for their retirement. That is a prime goal of our—the Portman-Cardin—legislation, but we also should adjust the caps so that those that do put money away, at least those limits keep up with inflation. They haven't. We are actually taking steps backward in that direction. I think we can do both.

So I guess I would urge you as you look over what we can do to improve private retirement in this Nation, how we can improve retirement security, both Social Security and private retirement, that we try to find a way to come together on this retirement proposal. I think we can. I think we are very close.

I am not happy, by the way, that we are proceeding in attaching it to bills that have no chance of becoming law. I do think at the end of the day we should be working together to improve retirement opportunities, both the Social Security and the private retirement plans, and I would be glad to yield my remaining time for your comment.

Secretary SUMMERS. I think we agree on the importance of strengthening the retirement security system, Congressman Cardin, and certainly I think that if there could be an agreement on the principle that legislation in this area should devote a substantial majority of its resources to expanding access to those who do not have pensions while perhaps making some room for some adjustments of limits, if there could be an agreement on that principle, I think that would be an agreement with which we could work.

My understanding is that the legislative vehicles that have been discussed have devoted the lion's share of their costs to increasing the limits that apply to a small fraction of the population.

Mr. CARDIN. I am not sure that is true. We might want to sit down and review that.

Secretary SUMMERS. That would be useful for us all to look at.

Mr. SHAW [presiding]. Mr. Johnson.

Mr. JOHNSON of Texas. Mr. Secretary, you know, you have done an exemplary job on dodging the question on Social Security's earning limit, and I would just like to refresh you. Maybe you have forgotten what the President said. I know it has been brought up, but his quote is from his State of the Union address is, "We should eliminate the limits on what seniors on Social Security can earn." And I might refresh you on your own testimony before this Committee on March 3 this year. You stated personally, and I quote, "We should also find room to eliminate the earnings test, which is widely misunderstood, difficult to administer, and perceived by many older citizens as providing a significant disincentive to work. In addition, it is critical that we not lose sight of the important role that Social Security plays as an insurance program for widows and children and for the disabled." end quote. You said that. And you have said a couple of times this morning that this legislation doesn't contain any repeal of the earnings limit; instead, I would presume, it favors discriminating against seniors who choose to work. I wonder if you can answer more directly why you didn't include that.

Secretary SUMMERS. This legislation coming at this point in the year was an amendment to provide a foundation for addressing Social Security, not an attempt to do everything that was desirable. The President continues to be absolutely committed to elimination of the earnings test and measures to reduce poverty among elderly women. Those are desirable changes in Social Security. Those are changes we support. Those are changes we believe should be worked out as part of any overall Social Security agreement.

Mr. JOHNSON of Texas. Well, I might tell you I believe that Archer-Shaw does include that.

Let me ask you another question if I may. You talk about debt reduction and interest reduction, and yet, according to the numbers I see, the Social Security program is still going to run a deficit of about $252 billion in 2030 and $516 billion in 2070. How can we be paying down debt and still running deficits without increasing debt?

Secretary SUMMERS. Of course the President's proposal addresses that in two ways. By augmenting the size of the trust fund with the general revenue contribution, it provides for more interest income and therefore reduces the deficit that there otherwise would be, and it provides a larger stock of assets that can be reduced, as is always true when you accumulate a trust fund for a purpose, and then the moment of purpose arises, the trust fund is depleted, is drawn down. That is why that shows up as a deficit. So by augmenting the size of the trust fund and its earning power, the President's proposal makes it possible to handle what is the challenging situation we face, a rising old-age population that will rise more rapidly than the income growth among the younger earners, thereby giving rise to the deficit.

Mr. JOHNSON of Texas. OK. Thank you very much, Mr. Chairman. I yield back the balance of my time.

Mr. SHAW. Mr. Lewis.

Mr. LEWIS of Georgia. Thank you, Mr. Secretary. Mr. Secretary, you have been here a long time, and I think I am bringing up maybe the end, I guess, Mr. Chairman, and so I want to be very brief and agree with you in responding to two of my colleagues from the other side of the aisle. We do need additional police officers. We do need the 100,000 teachers. We do need to save and apply private land for the public and the common good. That is the role—one of the functions and the role of our national government should be, but I know you are here to talk about the President's proposal and Social Security.

Let me just ask you, Mr. Secretary, is it true or am I misreading something. Does the President's Social Security plan set up a Medicare reserve fund?

Secretary SUMMERS. Yes.

Mr. LEWIS of Georgia. Could you explain it and tell us how it will work?

Secretary SUMMERS. The President's proposal establishes, supported by various points of order and a sequester mechanism, a framework for using the on-budget surpluses that are in our fiscal future. One element of the use of those surpluses is the dedication of approximately $300 billion over the next 10 years to be preserved for use in the context of possible Medicare reforms. The President recognizes that there is a great deal of controversy about the future of the Medicare program. He has proposed his own competitive model of reform, including also pharmaceutical drug coverage. Others have different approaches and the judgment here is not an attempt to prejudge that issue. Rather, it reflects the judgment of the vast majority of experts that whatever approach is pursued, there is likely to be a need for some revenue augmentation and to assure that those resources are available.

There is an understandable concern with committing those resources before the reform takes place, and that is why all the President's proposal does is to assure that those resources are maintained and not depleted until such time as Medicare reforms can be agreed. We hope that will be next year.

Mr. LEWIS of Georgia. Does the Republican plan offer anything similar for Medicare to the best of your knowledge?

Secretary SUMMERS. Not to my knowledge.

Mr. LEWIS of Georgia. How does the President's plan affect minorities and women, low-income women and minority recipients of Social Security?

Secretary SUMMERS. The President has made clear his commitment to measures to strengthen survivor benefits, measures to assure the maintenance of the progressivity of the Social Security system, and he has made clear that that is one of his bedrock principles. And I am not in a position at this point to compare different plans on that score, but I can tell you absolutely that a bedrock principle for the President is the maintenance of progressivity and addressing in particular the needs of minorities and women.

Mr. LEWIS of Georgia. To the best of your knowledge, can you tell us whether any other plan offers additional benefits for women and for minorities?

Secretary SUMMERS. I am not familiar. Honestly, Mr. Lewis, I am not familiar in detail with the provisions that are contained in a number of the other proposals that are directed at those concerns but I wouldn't want my lack of familiarity to be taken as a judgment one way or the other with respect to that issue.

Mr. LEWIS of Georgia. Thank you very much, Mr. Secretary.

Thank you, Mr. Chairman.

Chairman ARCHER [presiding]. Thank you, Mr. Lewis.

Mr. Secretary, thank you for your patience and the time that you have given to the Members of the Committee today. I will say to you that I hope that I will be seeing you again today, before the day is out, on the matter of other concern before we conclude this Congress.

I had just a couple of follow-up comments and questions to make on the Social Security program. Number one, I am pleased to know that there is an opening on the part of the administration for further negotiation as to how we harness the returns from the private sector to help solve the Social Security problem. There are only two ways to do it. One is to have the government directly invest in the market and the other is to find a way to create personal accounts for every working American. And in the end we've got a bridge-sized gap if we want to harness the returns in the private sector.

I am curious as to why you stopped in your salvation scheme for Social Security in the year 2044; why you did not just continue to infuse general Treasury monies thereafter.

Secretary SUMMERS. Because of a—Mr. Chairman, one of the principles I established which was we only wanted to infuse general revenues to the extent that that infusion was justified by savings that we had achieved through debt reduction, and we wanted to assure that even with our infusions of general revenues, that the on-budget surplus would continue to be in surplus and those two constraints led to the path that we described.

Our concern for the reasons that I thought were rather well articulated on your side of the aisle here today would be with an approach that either created an on-budget deficit or with an approach that infused general revenue savings that were not earned through the reduction of debt. That was obviously the concern that I was also trying to raise with respect to the proposal that you had put forward.

Chairman ARCHER. Well, if I understand your proposal, though, your infusions of general Treasury funds are not tied into the interest savings on any debt. There are arbitrary amounts of money that do not directly relate to the interest savings.

Secretary SUMMERS. No, I think, Mr. Chairman, that the proposal is based on the allocation of the savings and interest that result from the accumulation of the Social Security surplus and the resulting transfer of what had been a debt obligation to the public to an internal debt obligation of the government; and it is that which constrains the size that we regard as appropriate of the general revenue transfers, along with the additional constraint that we are desirous of avoiding an on-budget deficit, a protected on-budget deficit at any point in the future. We think those are important principles that programs should strive to achieve.

Chairman ARCHER. But the actual dollar amounts that are provided in your program on an annual basis do not tie into the interest savings. That just happens to be a reality if you read your proposal. They do not tie into the interest savings. They are an arbitrary amount of money annually in order to reach your desired goal.

Secretary SUMMERS. Mr. Chairman, on the contrary, they are calculated directly on the basis of the projected interest savings, constrained by the projected interest savings, and the imperative, as we saw it, of maintaining on-budget surplus. If, as I suspect is implicit in your proposal, you are prepared to commit general revenues beyond interest savings or to accept projected on-budget deficits, then it is possible to achieve longer expansions of solvency through greater contributions. That was a step that we were reluctant to take.

Chairman ARCHER. I understand the premise that you are building your scheme on, but the actuaries have evaluated your plan and they say in their report, transfers are not contingent on the actual amount of reduction in debt held by the public, which means that the transfers are not contingent on the interest savings.

Secretary SUMMERS. I think in context, Mr. Chairman—and if I am speaking inaccurately, I will correct the record—the actuaries' statement is correct, as is mine. My statement was that the interest savings were based—that the contributions were based on the projected interest savings and I think that is a correct statement. The actuaries' statement about contingency referenced the fact that we are making the commitment today based on today's projection, and there is obviously uncertainty about what will happen in the future with respect to the public debt. That is the basis of the actuaries' statement.

Chairman ARCHER. That is well stated. But for your plan to be fiscally responsible, as you said earlier, it should be that the amount of money will be the amount of interest savings rather than a specific amount that may not be the amount of interest savings in reality. But rather than belaboring that, because I think we have explored it and understand it now, let me ask you why you delay until the year 2011 to make any infusion of general Treasury funds into the Social Security trust fund?

Secretary SUMMERS. Because we are very focused on what is the common objective this year, I think, of assuring the maintenance of on-budget surpluses so that the Social Security Trust Fund is neither raided nor double-counted. And therefore we believe, given the imperative of setting aside resources for Medicare as we see it, given the imperative of providing a realistic discretionary spending path, that it is desirable to delay making those transfers so that we don't find ourselves in a situation where we are either—"raid" is a pejorative word——.

Chairman ARCHER. That was just a discretionary decision based on what you have just mentioned. I was just curious as to why that was.

Let me just say one thing finally and that is relative to the President's scheme for Social Security, the savings in debt reduction are already in the baseline. Your scheme will not change that. Do you agree with that?

Secretary SUMMERS. No.

Chairman ARCHER. The interest savings from debt reduction as a result of the projected surplus are already in the baseline because both CBO and OMB assume that all of this money will be used to pay down the debt.

Secretary SUMMERS. Mr. Chairman, in an arithmetic sense, what you are saying is, of course, exactly correct. What we see as one of the major virtues of the President's plan is that by establishing a link between the idea of debt reduction and the contributions to the trust fund, we make it more likely that along with the other procedural protections that are included, we make it more likely that the savings will in fact be realized and the debt reduction will, in fact, materialize.

So it is the safeguards which are an integral part of a proposal to transfer the benefits of debt reduction to the trust fund that mean that our plan is making it much more likely in our judgment that those projections will in fact materialize rather than be used to finance large new expenditure programs of an imprudent kind or large unfinanced tax cuts that we feel would reduce the Nation's ability to meet this obligation.

Chairman ARCHER. It is unfortunate we haven't had the opportunity today to pursue some of those technical aspects of your plan, but those so-called procedural safeguards are the very same safeguards that have been criticized severely on the Democrat side of this Committee relative to the Herger Social Security protection plan. And if they could be criticized there, they would likely be criticized here too.

I don't want to spend a lot of time on this but what I do want to get into is the fact that irrespective of how you present it, these savings are already in the baseline. The law of the land provides for the spending caps and the spending is therefore determined in advance and into the baseline, and all of the interest savings from paying down the debt are already in the baseline and your plan does not change those projections. And I don't think there is any change in the projections based on your procedural safeguards or all the other things that you just mentioned. The projections are still the same.

Now, you are therefore taking money out of the general Treasury that is already going to be there irrespective of your scheme and you are transferring it into the Social Security Trust Fund. Now, that is a massive demarcation from the way Social Security has always been structured. Massive. In fact, Franklin Roosevelt would probably roll over in his grave to hear this proposal. It destroys the direct connection between the worker and their benefits that the payroll tax has guaranteed them over the years. Our paths regularly, year after year, oppose the simple infusion of general Treasury funds into the trust fund, and this is a massive infusion of general Treasury funds which temporarily keeps the program afloat; and in doing so, it now relies on income taxes into the trust fund for the first time and destroys the relationship to the payroll tax.

So the taxes will be increased to take care of this on Casey Hulshof, on my grandchildren who are older. They will be obligated to pay more taxes in order to be able to infuse this general Treasury money into the fund, but it will be income taxes instead of payroll taxes. Now, that is the reality of your program.

Now, all of the programs are going to require some infusion of general Treasury money so we are not absent the same criticism on any other program. But I would simply say that before we start comparing programs, they should be compared on a level playing field, which is, no program should be treated the same unless it saves for 75 years and beyond the Social Security program.

Now, I was on the 1982 Commission for Social Security reform and I opposed—I wrote Minority views against that proposal and I voted against them in 1983, and the reason I did is I said it doesn't really save Social Security for 75 years and beyond. But what it did is it saved it, projected by the actuaries, for 75 years. But if you looked at the last few years, you were on a glide path to disaster, and the minute you got into the 76th and 77th year, you were over the cliff, and that is why we have a problem today. And if we don't have an ultimate plan that goes not just 75 years but extends beyond that, within reason and believability, we will be right back in the soup again.

God help us if we don't do it right this time. So the door is open, Mr. Secretary, for us to try to get together, but it needs to be 75 and beyond, not just 50 with a cliff. And I think as a man of goodwill, which you are, and I believe myself to be, I hope we can get together and figure out a way that we can do this for the long term and be sure that our grandchildren really have been accommodated.

And I thank you for listening to me and I thank you for being here today.

Mr. RANGEL. Mr. Chairman.

Chairman ARCHER. Mr. Rangel.

Mr. RANGEL. Mr. Chairman, I just wanted to be a part of this bipartisan dialogue. I didn't want it to conclude without me indicating that it is very difficult for the administration to be critical of your proposal because it is not in legislative form, and God knows where it is going to end up.

Chairman ARCHER. If the gentleman will yield. The administration is well aware of all the details of this proposal. There is not anything that has been left to doubt. So it is easy for us to have an exchange on it.

Mr. RANGEL. There was a time when you were well aware of the administration's proposal, but you insisted on them proposing a bill—for reasons which I don't understand.

In any event, to get back to my original point, I think what we want to do is to make certain that the administration is on board with a Ways and Means proposal. I don't expect that this President, or any other President, would just dictate to this historic Committee what we are obligated to do to repair Social Security.

The President has provided leadership and guidance in this area, but I don't expect that they will be writing the bill that we will sign on to as the conference report. So whatever differences we have with their proposal, it would seem to me that we might reconsider the bill that you and Mr. Shaw have, to see whether or not we can get some Democrats on board after conferring with the administration, and collectively, not by just pointing fingers at each other, to see the areas of agreement and how we could improve upon what we are doing.

In any event, to show my willingness to be bipartisan, I want to support and encourage the President in working with the Republican leadership to try to get us out of this budget disaster that they have placed us in and to try to work out the differences, rather than to have them close the government down as they did before.

While the President and administration are working with them, I hope you don't forget who took the President to the dance, so that we all will leave here happier. Thank you for your testimony and your patience.

Chairman ARCHER. Thank you again, Mr. Secretary. I am looking forward to seeing you later today.

Secretary SUMMERS. Thank you very much. I look forward to working closely with all the Members of this Committee, representing both sides of the aisle, on the challenges facing us both in the near term as this session winds down, and over the longer term with respect to the very important issues that we have been discussing today. I am grateful to you and to Ranking Member Rangel for the opportunity to testify before you today.

Chairman ARCHER. Thank you, Mr. Secretary.

Our next witnesses will testify as a panel. The honorable David Walker, Comptroller General of the GAO, and Dr. Dan Crippen, the Director of the Congressional Budget Office. Gentlemen, welcome.

Mr. Walker, would you lead off?

STATEMENT OF HON. DAVID M. WALKER, COMPTROLLER GENERAL OF THE UNITED STATES, U.S. GENERAL ACCOUNTING OFFICE

Mr. WALKER. Thank you, Mr. Chairman. It is a pleasure to be here today to discuss the President's most recent proposal for addressing Social Security and the use of the unified budget surplus. I have a full statement that I would like to be entered into the record, Mr. Chairman.

Chairman ARCHER. Without objection, your full statement will be inserted in the record.

Mr. WALKER. Thank you, Mr. Chairman. In testimony before this Committee's Subcommittee on Social Security this past spring, we at the GAO offered an analytic framework for assessing Social Security reform proposals. That framework consists of three basic criteria: first, the extent to which the proposal achieves sustainable solvency and how the proposal would affect the economy and the Federal budget; second, the balance struck between the twin goals of income adequacy and individual equity; and third, how readily such changes could be implemented, administered, and explained to the public.

Mr. Chairman, as you requested, my testimony today will discuss the President's current proposal for Social Security financing in the context of this framework. Importantly, just last week, we issued a report applying these same criteria to several pending Social Security reform proposals, including the President's Social Security financing proposal. I holding up a copy of that now. I would seriously commend to you and to every Member this report. I think it is "must" reading.

I might also note, Mr. Chairman, that we issued in May of this year a primer on debt, which I think I would also commend to the members in light of the budget surplus situation. Some of the questions that came up today are answered in this document. My remarks today about the President's proposal are based primarily on our analysis of his proposal contained in our report. We also analyzed the USA proposal in our report, but I am not going to cover that in my summary testimony.

Before I get into our analysis of the President's proposal, I think it is important to put things in a longer-term context. It is important to look at the President's proposal in the context of the fiscal situation in which we find ourselves. After nearly 30 years of unified budget deficits, we look ahead to projections of surpluses as far as the eye can see. At the same time, we know that we face a demographic tidal wave that poses significant challenges to the future of the Social Security system, Medicare, and our economy as a whole.

In this context, we commend the President's use of a longer-term framework for resource allocation than has normally been customary in the Federal budgeting process and for proposing that a significant portion of the projected budget surplus be used for debt reduction.

We further note that the Congress is also concerned with the future and has committed to save a significant portion of the current surplus for debt reduction.

Although all projections are uncertain and they get more uncertain the farther out that you go, we have long held that from a long-term perspective, it is important to look beyond 5 years, 10 years, even in some cases beyond 50 years in establishing fiscal policy and assuring solvency and sustainability of entitlement programs.

Each generation is in part the custodian for the economy it hands to the next. The Nation's long-term economic future depends in part on today's budget decisions. This perspective is particularly important because our long-term economic model and that of the Congressional Budget Office continue to show that absent a change in policy, the changing demographics to which I referred above will lead to renewed deficits.

Unlike in prior years, demographic trends are now working against us rather than for us. This longer-term fiscal challenge provides the critical backdrop for making decisions about today's unified surpluses. Stated differently, if we fail to make prudent decisions about the disposition of the budget surpluses or fail to engage in meaningful entitlement reform, the Nation's fiscal future and the standard of living for future generations of Americans will likely decline.

Now, with regard to the President's proposal. According to administration officials, the President's proposal would constitute a significant down payment on Social Security reform while contributing to achieving the administration's goal of eliminating publicly held debt by the year 2015. The proposal would significantly reduce debt held by the public from current levels by both the amount of Social Security surplus and a portion of the on-budget surplus equivalent to the general fund transfer. The proposal would not, however, reform the basic Social Security program in any way. Rather, the administration's proposal seeks to increase the likelihood that projected unified surpluses would be preserved for Social Security and debt reduction.

The President's current proposal for addressing Social Security now embodied in legislative language differs in some respects from his proposal in the July mid-season review primarily in dropping the proposal to invest a portion of the surpluses in equities. What remains is the proposal to provide additional program financing by transferring general funds to the OASDI trust funds. This transfer represents an unearned grant of future general revenues to Social Security. Stated differently, it represents an increase in funded benefit commitments—and hence future general funds—as compared to current law.

The Office of the Chief Actuary of the Social Security Administration, which provides estimates on how proposals would affect the OASDI trust funds based on the trustee's assumptions, has stated that the President's transfer proposal would extend the solvency of trust funds from 2034 to 2050. It would not, however, restore the program's long-range, 75-year actuarial balance. This has been the traditional long-range test of solvency used by the Social Security trustees.

As you know, Mr. Chairman, I was a trustee for 5 years from 1990 to 1995.

Let me turn now to a few bottom-line comments about the proposal. Our first criterion deals with financing sustainable solvency. And here we evaluate whether or not it achieves solvency over a 75-year projection period and beyond. The bottom line is while the President is to be commended for the amount of debt reduction he is proposing, and that clearly would confer a number of economic benefits on the Nation as well as help with the budgetary situation, the proposal does not address the program's sustainability in any way. It addresses solvency but it does not address sustainability.

We believe it is critical that both have to be addressed. The system's cash flow still turns negative in 2014 and Social Security becomes a draw on general fund revenues as it must redeem the securities beginning in 2014 to pay that down. That means you either have to increase taxes, reduce spending or otherwise achieve some type of incremental rate of return on invested funds through compounding in order to meet those obligations.

Again, 2014 is a critical date, not just 2034, the date that the trust fund assets run out, or 2050, or frankly even 75 years from now, because we need to assure the program's sustainability over the long term. In this regard there is a the risk that transfers in the President's proposal may induce an unwarranted complacency about the financial health of the Social Security program.

From a macroeconomic perspective, the critical question is not how much in trust fund assets there are—or solvency—but whether the government as a whole has the economic capacity to finance benefits both now and in the future; namely, sustainability. Nothing in the President's transfer proposal changes these pictures. Social Security as a share of the economy and a share of Federal revenues remains unchanged under the President's proposal.

The administration acknowledges the need for further reform, but it is critical that we engage in such further reforms. The President's proposal does not make any changes in current Social Security benefits and as a result would not have any effect on adequacy. There would be a need to try to address a potential expectation gap about whether or not there has been meaningful reform here, which would have to be addressed. There would not, however, be any implementation issues because it does not change the system in any way.

So in summary, Mr. Chairman, I agree with Secretary Summers that unified budget surpluses present us with an opportunity but they also present us with an obligation. We have an opportunity to use our unprecedented economic wealth and fiscal good fortune to address today's needs but an obligation to do so in a way that improves the prospects for future generations. Restoring solvency to the Social Security system is a formidable challenge, but we have an obligation to meet that challenge before Social Security begins to squeeze out other spending on other national priorities or places an unbearable burden on future generations. And solvency alone is not enough.

The health of our economy and projected budget unified surpluses offer a historic opportunity to meet these challenges from a position of financial and economic strength. Such good fortune can indeed help us to meet a historic responsibility, a fiduciary obligation, if you will, to leave our Nation's future generations a financially stable system and to retain our commitment to the elderly.

The transfer of surplus resources to the OASDI trust funds, which the administration argues is necessary to lock in projected unified surpluses in the future, would constitute a fundamental shift in the financing of the Social Security program. Such an approach would have a significant beneficial result of reducing debt held by the public. However, it would not constitute real programmatic reform because it does not modify the program's underlying commitments and cash flows in any way.

Moreover, the proposed transfer, even though it would extend the program's solvency, could create complacency or a false sense of security about the program's long-term sustainability. This could actually make it more difficult to engage in substantive program reform needed to assure the program's long-range sustainability.

There is increasing recognition that the time has come for meaningful Social Security reform. No single proposal is likely to be the answer. Therefore, it is important for the Congress and the President to build on the dialogue engendered by these proposals.

Further, in deliberating Social Security reform, it is important to keep in mind Medicare. Medicare is in much worse shape than Social Security. In addition, Medicare reform is much more likely to need general revenue infusions to assure the sustainability of that program. We cannot look at these programs in a vacuum. Social Security reform is not easy, but it is not impossible. I might add, Mr. Chairman, I think there is much more in common between the President's proposal and some of the ones that have been talked about, than has been focused on today. There is a lot of common ground when you look at substance rather than form.

Further, meaningful reform in a timely fashion can enable us to exceed the expectations of all generations of Americans. Mr. Chairman, I have been in town hall meetings with the President, the Vice President, Senators and House Members, of both parties, and all over the country. I am absolutely convinced that we can effectuate Social Security reform that will exceed the expectations of all generations of Americans. We need to get on with real reform before the demographic tidal wave hits and while our economic and budget sun is shining. We must deliver on the promise to save Social Security.

Thank you, Mr. Chairman. We at GAO stand ready to help the Congress in a professional, objective, nonpartisan and nonideological way to address this formidable challenge.

Chairman ARCHER. Thank you, Dr. Walker.

[The prepared statement follows:]

[An attachment is being retained in the Committee files.]

Statement of the Hon. David M. Walker, Comptroller General of the United States, U.S. General Accounting Office

Mr. Chairman and Members of the Committee:

It is a pleasure to be here today to discuss the President's most recent proposal for addressing Social Security and use of the unified budget surplus. This proposal concerns one of the most important issues facing the nation, both now and over the longer term. Social Security forms the foundation for our retirement income system and, in so doing, provides benefits that are critical to the well-being of millions of Americans. Current unified budget surpluses provide a valuable opportunity to improve the nation's capacity to address the looming fiscal challenges arising from the retirement of the baby boom generation and transition to a more sustainable Social Security program. As you know, Mr. Chairman, a wide array of proposals have been put forth to restore Social Security's solvency, and the Congress will need to determine which proposals or elements thereof best reflect our country's goals for this retirement income program.

In testimony before this Committee's Subcommittee on Social Security this past spring,[1] we offered an analytic framework for assessing reform proposals. That framework consists of three basic criteria:

- the extent to which the proposal achieves sustainable solvency and how the proposal would affect the economy and the federal budget;
- the balance struck between the twin goals of income adequacy (level and certainty of benefits) and individual equity (rates of return on individual contributions); and
- how readily such changes could be implemented, administered, and explained to the public.

Mr. Chairman, as you requested, my testimony today will discuss the President's current proposal for Social Security financing in the context of this framework. Importantly, last week we issued a report applying these same criteria to several pending Social Security reform proposals, including the President's Social Security financing proposal.[2] My remarks today about the President's proposal are based primarily on our analysis in that report. Our report also analyzes the President's Universal Savings Account (USA) proposal for individual savings accounts, and I will also touch briefly on this proposal. While I understand that the subject of this hearing is the President's most recent proposal, I would be happy to answer questions on any of the proposals included in our report.

CONTEXT: LONG-TERM OUTLOOK IS IMPORTANT

It is important to look at the President's proposal in the context of the fiscal situation in which we find ourselves. After nearly 30 years of unified budget deficits, we

[1] Social Security: Criteria for Evaluating Social Security Reform Proposals (GAO/T-HEHS–99–94, March 25, 1999).

[2] Social Security: Evaluating Reform Proposals (GAO/AIMD/HEHS–00–29, November 4, 1999). In addition to analyzing the President's transfer proposal, this report also presents an analysis of the President's proposal for Universal Savings Accounts (USA) accounts. The Administration considers the USA proposal, which would establish individual retirement savings accounts, separate from its Social Security proposal. Besides the President's, the proposals we considered are: (1) the Social Security Guarantee Act outlined by Ways and Means Committee Chairman Bill Archer and Social Security Subcommittee Chairman Clay Shaw; (2) H.R. 1793, The 21st Century Retirement Security Act, (3) the Senate Bipartisan bill, S. 1383, announced by Senators Judd Gregg, Bob Kerrey, John Breaux, and Chuck Grassley, and (4) the Social Security plan outlined by House Budget Committee Chairman John Kasich.

look ahead to projections for "surpluses as far as the eye can see." At the same time, we know that we face a demographic tidal wave in the future that poses significant challenges for the Social Security system, Medicare, and our economy as a whole. In this context, we commend the President's use of a longer-term framework for resource allocation than has been customary in federal budgeting. We would further note that the Congress is also concerned with the future and has committed to save a significant portion of the current surplus for debt reduction.

Although all projections are uncertain—and they get more uncertain the farther out they go—we have long held that a long-term perspective is important in formulating fiscal policy for the nation. Each generation is in part the custodian for the economy it hands the next and the nation's long-term economic future depends in large part on today's budget decisions. This perspective is particularly important because our long-term economic model and that of the Congressional Budget Office (CBO) continue to show that, absent a change in policy, the changing demographics to which I referred above will lead to renewed deficits. Unlike in prior periods when we entered a period of surpluses after years of deficits, demographic trends are now working against us rather than for us. This longer-term fiscal challenge provides the critical backdrop for making decisions about today's unified surpluses.

Budget surpluses are the result of a good economy and difficult policy decisions. They also provide a unique opportunity to put our nation on a more sustainable path for the long term, both for fiscal policy and the Social Security program itself. Current decisions can help in several important respects: (1) current fiscal policy decisions can help expand the future capacity of our economy by increasing national savings and investment, (2) engaging in substantive reforms of retirement and health programs can reduce future claims or better permit their financing, (3) by acting now, we have the opportunity of phasing in changes to Social Security and health programs over a sufficient period of time to enable our citizens to adjust, and (4) failure to achieve needed reforms in the Social Security and Medicare programs will drive future spending to unsustainable levels and eventually "squeeze out" most or all discretionary spending. If we let the achievement of the current unified budget surplus lull us into complacency about the budget, then in the middle of the 21st century, the nation could face daunting demographic challenges without having built the economic capacity or program/policy reforms to handle them. Stated differently, if we fail to make prudent decisions about the disposition of budget surpluses or fail to engage in meaningful entitlement reform, the nation's fiscal future and the standard of living for future generations of Americans will likely decline.

THE PRESIDENT'S SOCIAL SECURITY PROPOSAL

According to Administration officials, the President's proposal would constitute a "significant down payment" on Social Security reform while contributing to achieving the Administration's goal of eliminating publicly held debt by 2015. The proposal would reduce debt held by the public from current levels by both the amount of the Social Security surplus and a portion of the on-budget surplus equivalent to the general fund transfer. The proposal would not, however, reform the basic Social Security program in any way. Rather, the Administration's proposal seeks to increase the likelihood that projected unified surpluses would be preserved for Social Security and debt reduction. Officials have also explained that the Administration remains committed to long-term Social Security reform that would extend the solvency of the Old Age and Survivors Insurance and Disability Insurance (OASDI) trust funds at least through 2075. The Administration has expressed a desire to work on a bipartisan basis to enact both its current proposal and long-term Social Security reform.

The President's current proposal for addressing Social Security, now embodied in legislative language contained in S. 1831 and H.R. 3165,[3] differs in some respects from the proposal put forth in his July 1999 Midsession Review. One important difference concerns the President's previous intention to increase future revenues to the OASDI trust funds by investing a portion in equities. This part of the proposal has now been dropped.

What remains is the proposal to provide additional program financing by transferring general funds to the OASDI trust funds. It is this transfer proposal that we analyzed in our recent report and that I will discuss in this testimony. As in the Midsession Review, the President proposes to use the entire Social Security surplus

[3] Those bills contain other provisions in addition to the transfer of general funds to Social Security. These provisions extend the discretionary caps through 2014, clarify and extend through 2014 the pay-as-you-go requirement for direct spending and receipts, and set aside as a Medicare surplus reserve one-third of any on-budget surplus for fiscal years 2000 through 2009.

and a portion of the projected on-budget surplus to reduce debt held by the public. The President projects that his proposal would reduce debt held by the public by $3.6 trillion over the next 15 years, eliminating publicly held debt by 2015. Beginning in 2011, the President proposes to transfer additional Treasury securities to the OASDI trust funds in an amount equal to the "fiscal dividend"—i.e., interest savings that result from lower publicly held debt. In effect, the President proposes to reduce publicly held debt by increasing government-held debt. Unlike the Midsession, the transfers are not open-ended but end at 2044. The Office of the Chief Actuary at the Social Security Administration (SSA), which provides estimates of how proposals would affect the OASDI trust funds based on the Trustees' intermediate assumptions, has stated that the President's transfer proposal would extend the solvency of the trust funds from 2034 to 2050. It would not, however, restore the program's long-range (75-year) actuarial balance. This has been the traditional long-range test of solvency used by the Social Security Trustees.

Let me turn now to our analysis of the President's proposal based on the three criteria we have developed—financing sustainable solvency, balancing individual equity and income adequacy, and how readily changes could be implemented, administered, and explained to the public. I would like to note at the outset that these criteria represent certain trade-offs that policymakers will need to weigh in considering changes. It is virtually impossible for any proposal to rate perfectly on all criteria. As I have said in earlier testimony, it is critically important to evaluate the effects of an entire package before considering whether these proposed changes add up to acceptable program reform. If a comprehensive package of reforms meets policymakers' most important goals for Social Security, individual elements of the package may be more acceptable. In addition interactive effects may tend to smooth the rough edges of individual elements.

Financing Sustainable Solvency

Our first criterion evaluates the extent to which the proposal achieves sustainable solvency over the 75-year projection period and more broadly, how the proposal would affect the economy and the federal budget. While the President's current proposal for Social Security financing differs in some respects from his earlier proposals—for example, the President no longer proposes to invest a portion of the OASDI trust funds in equities—in other respects, the bottom line of the proposal with respect to sustainable solvency is unchanged. The Administration acknowledges that its proposal is not a comprehensive reform package, describing it as a first step.

In summary, the proposal:

- Reduces debt held by the public from current levels, which reduces net interest costs, and raises national saving, thereby contributing to future economic growth.
- Provides general revenues to the OASDI trust funds in the future, thereby representing a fundamental change in Social Security financing.
- Has no effect on the projected cash flow imbalance in the Social Security program's taxes and benefits, which begins in 2014.
- As a result, the President's proposal represents a financing, rather than a Social Security reform proposal.

In our recent report, we used our long-term economic model to help us assess the potential fiscal and economic impacts of Social Security reform proposals. In analyzing the President's transfer proposal in our report and in this testimony, we considered its budgetary and economic effects in isolation from all other Administration proposals, including those in his Midsession update and also the non-Social Security related provisions of S. 1831 and H.R. 3165. This treatment is consistent with our analyses of the other proposals discussed in our report.

- We compared these proposals, including the President's transfer proposal, to three alternative fiscal policy paths developed in our ongoing model work. Implicitly all paths assume that Social Security and Medicare benefits are paid even when the trust funds no longer hold sufficient assets to cover benefits.[4]
- A "**No Action**" path that assumes no changes in current policies and thus results in saving the unified surpluses. This path, which I have sometimes called "**Save the Unified Surplus**," assumes that actual discretionary spending—including for emergencies—remains within the existing discretionary caps.

[4] The Social Security Act specifies that Social Security benefits may be paid "only" from the trust funds. As a result, absent a change in law, benefits would not be paid at the point when assets were insufficient to cover those benefits.

• An "**Eliminate non-Social Security surpluses**" path that assumes that permanent unspecified policy actions (i.e., spending increases and/or tax cuts) are taken that eliminate projected on-budget surpluses through 2009.

• A "**Long-term on-budget balance**" path that assumes that projected on-budget surpluses are eliminated through 2009. Thereafter, the on-budget portion of the unified budget is kept in balance for the rest of the simulation period by actions that cut spending and/or raise revenue.

Since 1992 we have provided the Congress with a long-term perspective by modeling the implications of differing fiscal policy paths for the nation's economy. We offer these simulation results not as precise forecasts but rather as illustrations of the relative fiscal and economic outcomes associated with alternative policy paths. That is, our long-term simulations provide a useful way to compare the potential outcomes of alternative policies within a common economic framework. Our model reflects the key interaction between the budget and the economy—the effect of the unified federal deficit/surplus on the amount of national saving available for investment, which influences long-term economic growth.

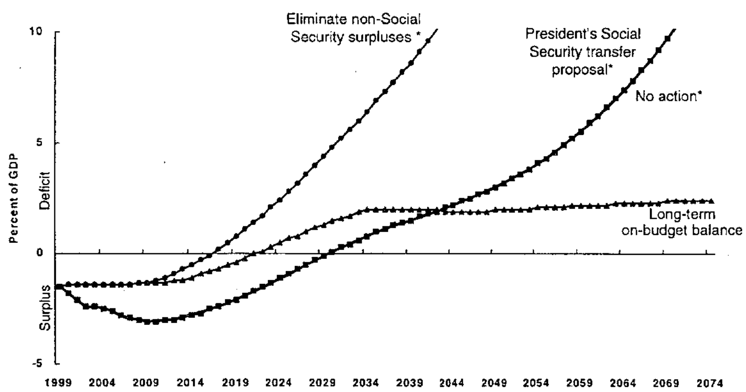
Our analysis shows that the President's Social Security transfer proposal has the same effect on the economy and the federal budget as a policy of "No Action" that would simply continue spending and revenue along its current path while making no change in Social Security or Medicare benefit payments. In effect, the President's Social Security transfer proposal does not address sustainable solvency. While it extends the solvency of the OASDI trust funds by 16 years to 2050, it does this without substantive reform of the program. Stated differently, the President's proposal does not directly address the sustainability issue. The Administration acknowledges this saying that it is a down payment that we can make on Social Security reform this year.

The following two figures compare the three fiscal policy paths—No Action, Eliminate on-budget surpluses, and Long-term on-budget balance—to the President's transfer proposal, showing the impact of each on the unified surplus/deficit and debt held by the public. In modeling the President's transfer proposal, we maintained all of the No Action assumptions about compliance with existing discretionary caps and no changes in current policy. Thus, the only difference between simulations of No Action and the President's transfer proposal are the explicit general fund transfers to Social Security.

As a result, the graphs show three lines—not four—because the President's proposal, from an overall fiscal perspective, is identical in its effect with a policy of "No Action." This is because, in essence, the proposal transfers funds from one part of the budget (the on-budget, or non-Social Security portion) to another (the off-budget, or OASDI trust funds). On a unified basis, the transfers net out. Although they increase debt held by the trust funds, they have no effect on the unified fiscal position and no effect on levels of debt held by the public compared to No Action. The Administration has stated, however, that its proposal would reinforce the resolve to stay, in effect, on a No Action course by linking debt reduction to the transfer of new resources to Social Security.

Figure 1: President's Social Security Transfer Proposal

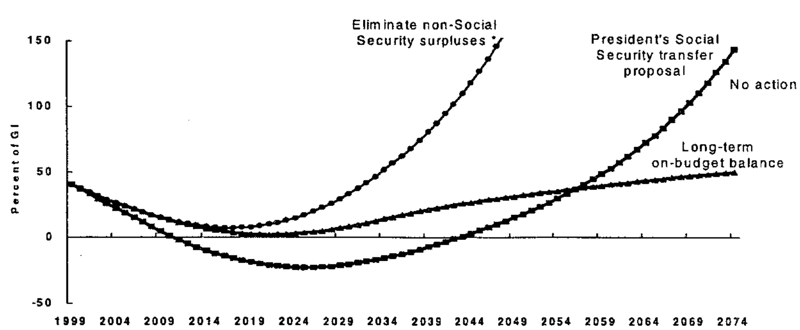
Unified Deficits/Surpluses as a Share of GDP



*Data end when deficits reach 10 percent of GDP.
Note: As noted in the text, the President's Social Security transfer proposal follows the no action path. Analysis is limited to the effects of the President's proposal for general revenue transfers to the OASDI trust funds. Sufficient data were unavailable to incorporate effects of the proposed USAs.

Figure 2: President's Social Security Transfer Proposal

Debt Held by the Public as a Share of GDP



*Data end when debt reaches 150 percent of GDP.
Note: As noted in the text, the President's Social Security transfer proposal follows the no action path. Analysis is limited to the effects of the President's proposal for general revenue transfers to the OASDI trust funds. Sufficient data were unavailable to incorporate effects of the proposed USAs.

According to Administration statements, the President's proposal seeks to provide a mechanism to increase the likelihood that projected unified surpluses would be preserved for Social Security and debt reduction. No Action assumes that the entire unified surplus would be used for debt reduction. Although this reflects current law, the current debate suggests it is increasingly unlikely that the on-budget surplus will be used for debt reduction. The President's transfer proposal would reserve the Social Security surplus and a portion of the projected on-budget surplus for debt reduction, articulating in law what has been generally agreed by both the President and the Congress in principle. Such debt reduction would confer significant short- and long-term benefits to the budget and the economy.

Our work on the long-term budget outlook has illustrated the benefits of maintaining surpluses for debt reduction. Interest on publicly held debt today represents the third largest program in the federal budget, representing about 15 percent of federal spending. Reducing the publicly held debt reduces these costs, freeing up budgetary resources for other programmatic priorities. For the economy, running unified surpluses and reducing debt increases national saving and frees up resources for private investment. As shown in figures 1 and 2, compared to spending the on-budget surpluses under "Eliminate non-Social Security surpluses," the President's transfer proposal would result in higher unified surpluses, lower unified deficits, and lower debt held by the public.

Our long-term simulations have consistently shown that any path saving all or a major share of projected unified budget surpluses ultimately leads to a stronger fiscal position and a stronger economy. GDP per capita would more than double from present levels by saving most or all of projected unified surpluses, while incomes would actually fall in the long term if we fail to sustain any of the unified surplus. Although rising income is always important, it is especially critical for the 21st century, for it can increase the economic capacity of a slowly growing workforce to maintain a good standard of living as well as to finance future government programs and the commitments for the baby boomers' retirement.

While reducing debt held by the public appears to be a centerpiece of the proposal—and has significant benefits—the general fund transfer is a separate issue. The transfer is not technically necessary: whenever revenue exceeds outlays and the cash needs of the Treasury—whenever there is an actual unified surplus—debt held by the public falls. The President's proposal appears to be premised on the belief that the only way to sustain unified surpluses is to tie them to Social Security. He has merged two separate questions: (1) how much of the unified surplus should be devoted to reducing debt held by the public; and (2) how should the nation finance the Social Security program in the future.

While providing the OASDI trust funds with additional Treasury securities equal to the projected "fiscal dividend" from debt reduction may be intended to help preserve projected unified surpluses, we have several concerns about this aspect of the President's proposal. The trust funds already earn interest on their surpluses. Under the President's current proposal the trust funds will receive, in effect, a second interest payment equal to interest savings that result from paying down publicly held debt. This is simply a grant of future general revenues to Social Security—which brings me to my second concern. As the SSA Deputy Chief Actuary has stated, while the transfers are intended to be roughly equal to the expected reduction in interest on debt held by the public as a result of the Social Security surpluses in fiscal years through 2000 through 2015, the transfers are not contingent on the actual amount of debt reduction. In other words, under the President's current proposal, the transfers would occur whether or not debt reduction actually takes place and the interest saving is realized.

We are also concerned about the implications of the general fund transfer for Social Security financing. As in the earlier proposals, the President's current proposal in effect trades debt held by the public for debt held by the trust funds. It thereby commits future general revenues to the Social Security program. This is true because the transfers would be in addition to any buildup of payroll tax surpluses. Securities held by the OASDI trust funds have always represented annual cash flows in excess of benefits and expenses, plus interest.[5] Under the President's proposal, this would no longer continue to be true. The value of the securities held by the trust funds would be greater than the amount by which annual revenues plus interest exceed annual benefits and expenditures.

This means that for the first time there would be an explicit general fund subsidy. All of the proposals we analyzed in our report make some use of general funds and, as I have said before, there are legitimate arguments on both sides of the question of bringing some general fund financing to Social Security—but the issue should be debated openly and on its merits.

An explicit general fund subsidy would be a major change in the underlying theoretical design of the Social Security program. Whether you believe it is a major change in reality depends on what you assume about the likely future use of general revenues to meet expected shortfalls in program financing. For example, current

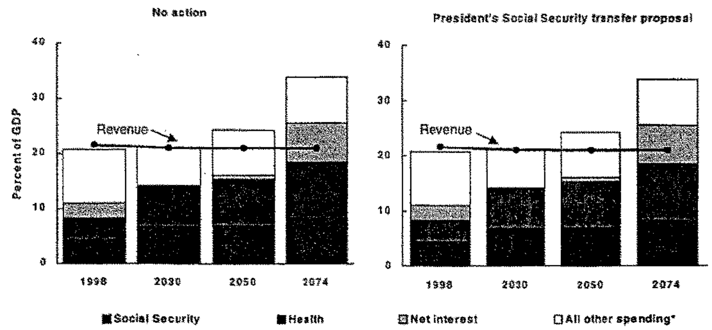
[5] Cash flow into the Social Security trust funds is composed of payroll taxes and a portion of the income taxes paid on Social Security benefits. Income taxes make up a relatively small component of the surplus. Interest paid to Social Security is analogous to interest paid on publicly held debt in that both come from the general fund. Interest on publicly held debt is recorded as an outlay. Interest to the trust funds is credited in the form of additional Treasury securities.

projections are that in 2034 the OASDI trust funds will lack sufficient resources to pay the full promised benefits. The Social Security Act specifies that Social Security benefits may only be paid from the trust funds. If you believe that the expected shortfall would—when the time came—be addressed by legislation that would authorize the use of general funds to pay Social Security benefits, then the shift embedded in the President's proposal merely makes that explicit. If, however, you believe that there would be changes in the benefit or tax structure of the fund instead, then the President's proposal represents a very big change. By increasing the securities in the trust funds, the President's transfer gives the Social Security program an explicit claim on future general fund revenues. In either case, the question of bringing significant general revenues into the financing of Social Security is a question that deserves full and open debate.

While the President is to be commended for the amount of debt reduction he is proposing, we remain concerned about the consequences for trust fund financing and Social Security program reform. It is fair to note that nothing in his proposal changes the fundamental structural imbalance in Social Security. The system's cash flow still turns negative in 2014 and Social Security becomes a draw on the general fund as it redeems its Treasury securities to pay promised benefits. When unified deficits re-emerge, however, baby boomers will still be retiring with long expected lifespans in retirement. If the President's proposal to transfer interest savings to the OASDI trust funds is adopted, their solvency on paper is extended, but the structural imbalance will remain. The new Treasury securities will be redeemed and constitute a new claim on the general fund until they run out in 2050. Cash to redeem these securities can only come from some combination of cuts in other spending, increases in taxes, or increases in borrowing from the public. Absent substantive program reform, our children and grandchildren will be saddled with a budget heavily burdened by commitments to fund entitlement programs for the elderly. (See figures 3 and 4.)

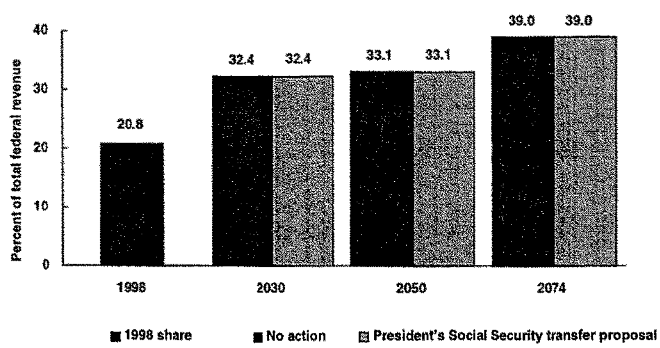
The risk is that the transfers in the President's proposal would induce an unwarranted complacency about the financial health of the Social Security program. From a macro perspective, the critical question is not how much a trust fund has in assets—or solvency—but whether the government as a whole has the economic capacity to finance benefits now and in the future—namely sustainability. This is illustrated in figures 3 and 4. These figures show the composition of federal spending as a percent of gross domestic product (GDP) and Social Security spending as a percent of federal revenue over the 75-year simulation period under the No Action path. Nothing in the President's transfer proposal changes these pictures. Social Security as a share of the economy and as a share of federal revenue remains unchanged under the President's proposal. The Administration acknowledges the need for further reform, but we are concerned that the proposed transfers will reduce the perceived need to do so until well into the next century.

Figure 3: Composition of Spending as a Share of GDP in 1998 and Under No Action and the President's Social Security Transfer Proposal



*All other spending includes offsetting interest receipts in 2030 under no action and the President's transfer proposal.
Note: Analysis is limited to the effects of the President's proposal for general revenue transfers to the OASDI trust funds. Sufficient data were unavailable to incorporate effects of the proposed USAs.

Figure 4: Social Security Spending as a Share of Total Federal Revenue in 1998 and Under No Action and the President's Social Security Transfer Proposal



Note: Analysis is limited to the effects of the President's proposal for general revenue transfers to the OASDI trust funds. Sufficient data were unavailable to incorporate effects of the proposed USAs.

Balancing Adequacy and Equity in the Benefit Structure

This criterion evaluates the balance struck between the twin goals of income adequacy and individual equity. Income adequacy refers to the level and certainty of benefits provided to retirees, the disabled, dependents and survivors. It is particularly important for low-income workers who are most reliant on the program, and may be achieved, in part, through a progressive benefit formula. Individual equity refers to rates of return on individual contributions. That is, it concerns the relationship between the benefits individuals receive and the contributions they have made to the Social Security system. Individual equity also implies greater choice and control for workers over their contributions to the system. It applies not only to equity within a generation, but across generations as well.

The current Social Security system makes certain tradeoffs between the degree of income adequacy and individual equity provided by its benefit structure. Redistributive transfers embedded in the current system create an implicit "safety net" for workers and their families.[6] At the same time, linking benefits to contributions invokes the standard of individual equity.

Because the President proposes no changes to the structure of the current Social Security system, his proposal does not affect income adequacy. It retains the existing safety net and the linkage between contributions and benefits. Specifically, the President's proposal maintains current-law benefits for current and future retirees, including low-income workers and others most reliant on Social Security, and makes no changes to disabled, dependent, or survivor benefits. The proposal also makes no changes from the current Social Security structure in the way workers are covered, and it preserves the progressivity of the system. Additionally, it retains the compulsory nature of the current payroll tax.

To the degree that the President's transfer proposal uses general revenue to fund the Social Security program it will have an impact on future contributions and benefits and therefore intergenerational equity may be adversely affected. Other proposals address the intergenerational equity issue by introducing individual accounts as an advance funding mechanism. These accounts may lead to increased retirement income for future retirees, thereby reducing their reliance on the Social Security program, and relieving the burden on future generations.[7] However, the way these proposals would handle the current long-term financing shortfall and the costs of making a transition to a new system could have negative effects on intergenerational equity.

Implementing and Administering Reforms

This criterion evaluates how readily proposed changes could be implemented, administered, and explained to the public. Implementation and administration issues are important because they have the potential to delay—if not derail—reform if they are not considered early enough for planning purposes. Moreover, such issues can influence policy choices—feasibility and cost should be integral factors in the ultimate decisions regarding the Social Security program. In addition, potential transparency and public education needs associated with various proposals should be considered. Reforms that are not well understood could face difficulties in achieving broad public acceptance and support.

Because the President's transfer proposal does not alter the current Social Security program in any way, there are no implementation costs, and the program's current administrative costs will remain less than 1 percent of benefit outlays. Without programmatic change, there are no changes that must be explained to the public and no risk of an "expectations gap" with respect to benefits. It is important to note, however, that the mechanics of the proposed transfer of general funds to the OASDI trust funds are complex and difficult to follow. Public understanding of the financing of Social Security is necessary in order to retain broad-based support for, and confidence in, the program. In particular, it will be important for the public to understand that this transfer proposal is only one part of the solution to the OASDI trust funds' long-term solvency problem. For that reason, public education would still be necessary in order to avoid either unwarranted complacency or skepticism about the financial health of the program.

The USA Proposal

Let me turn, for a moment, to the President's other relevant proposal. Although the President considers his proposal for USAs[8] to be separate from Social Security, these accounts are aimed at increasing the ability of Americans to fund their own retirement. The President has proposed that a USA be established for each worker with family earnings of at least $5,000 annually. Low-and moderate-income workers would receive a flat annual general tax credit of up to $300 and a 50–100 percent government match on voluntary contributions, also financed by income tax credits. Total contributions could not exceed $1,000 annually, including the match. Low-income workers would get a one-to-one match to their contributions, while higher income workers would receive a lower percentage match or none at all. Both the credit

[6] While there is no minimum benefit guarantee in the current Social Security program, the earnings-related structure of the program ensures that all eligible workers receive a benefit.

[7] See Social Security: Evaluating Reform Proposals (GAO/AIMD/HEHS–00–29, November 4, 1999).

[8] The proposal was described in administration statements made on April 14, 1999.

and the match would ensure that most people would have some savings for retirement.

Because the administration has yet to fully develop the USA proposal, our assessment of it against our criteria is necessarily limited. With regard to the sustainable solvency criterion, the tax credit would increase private saving and reduce government saving with no net effect on national saving. The incentive provided by the government match of voluntary contributions to USAs could result in some increase in national saving. However, there is no expert consensus on the effect the USA proposal or any of the proposals that establish individual accounts would have on the saving behavior of individuals. The tax credit financing of USA accounts would either decrease projected unified surpluses or increase projected unified deficits.

As a savings vehicle independent of the Social Security program, the USA proposal addresses the concepts of adequacy and equity differently. Progressivity is built into the USA structure through the government match, which provides a higher match for lower income workers and eliminates the match altogether for higher income workers. With USAs, workers could earn market returns but would bear the risk of market losses as well. In terms of individual choice and control over the accounts, workers could expect to have some investment choice, subject to certain limitations. Intergenerational equity is promoted by USAs to the extent that current workers save for their own retirement.

Costs associated with implementation and administration necessarily depend on the design of the program, which has not yet been detailed. However, some administrative costs would be expected, at least in starting the program and in educating the public on how it works. As the specifics of the program are developed, a public education program will be especially important to explain the USA structure as well as its significant elements, such as the matching funds provided by the government to low-income workers. For example, individuals would need information on basic investment principles, the risks associated with available choices, and the effect of choosing among alternatives that may be offered for annuitizing the accounts. Like any of the other individual account proposals, the USA proposal would need to be assessed on how it addresses the preservation of account balances for retirement purposes. We understand the President's USA proposal would not permit workers to make withdrawals from their individual accounts prior to retirement, thus seeking to ensure that funds will be available in retirement.

Other program details will need to be evaluated when the proposal is fully developed, such as the amount of individual choice to be permitted in making investment decisions. The existing description of the USA proposal does not specify what safeguards, if any, would be put in place to prevent politically motivated investing.

CONCLUSIONS

Unified budget surpluses represent both an opportunity and an obligation. We have an opportunity to use our unprecedented economic wealth and fiscal good fortune to address today's needs but an obligation to do so in a way that improves the prospects for future generations. This generation has a stewardship responsibility to future generations to reduce the debt burden they inherit, to provide a strong foundation for future economic growth, and to ensure that future commitments are both adequate and affordable. Prudence requires making the tough choices today while the economy is healthy and the workforce is relatively large—before we are hit by the baby boom's demographic tidal wave.

Restoring solvency to the Social Security system is a formidable challenge. But we have an obligation to meet that challenge before Social Security begins to squeeze out spending on other national priorities and places an unbearable burden on future generations. The health of our economy and projected budget unified surpluses offer an historic opportunity to meet these challenges from a position of financial and economic strength. Such good fortune can indeed help us meet our historic responsibility—a fiduciary obligation, if you will—to leave our nation's future generations a financially stable system and retain our commitment to the elderly.

The transfer of surplus resources to the OASDI trust funds, which the administration argues is necessary to lock in projected unified surpluses for the future, would constitute a shift in financing for the Social Security program. Such an approach would have the significant beneficial result of reducing debt held by the public. However, it would not constitute real programmatic reform because it does not modify the program's underlying commitments for the future. Moreover, the proposed transfer, by extending the solvency of the trust funds, could create complacency about the program's financing; this could make it more difficult to engage in the substantive program reform needed to reduce the unsustainable burden on the future economy.

The framework we have put forward is intended to help clarify the debate on various proposals in order to support the Congress in addressing this important national issue. The use of our criteria to evaluate all of the various reform proposals highlights the trade-offs that exist between efforts to achieve solvency for the OASDI trust funds and to maintain adequate retirement income for current and future beneficiaries. If comprehensive proposals are evaluated as to (1) their financing, fiscal, and economic effects, (2) their effects on individuals, and (3) their feasibility, we will have a good foundation for devising an overall reform package that will meet the most important objectives.

There is increasing recognition that the time has come for meaningful Social Security reform. No single existing proposal is likely to be the answer. Therefore it is important for Congress and the President to build on the dialogue engendered by these proposals. Further, in deliberating Social Security reform, it is important to keep Medicare in mind. Medicare insolvency looms sooner—and Medicare reform presents an even more formidable challenge than does Social Security reform. Social Security reform is not easy—but it is not impossible. Further, meaningful reform in a timely fashion can enable us to exceed the expectations of all generations.

We at GAO stand ready to help you address both Social Security reform and other critical national challenges. Working together, we can make a positive and lasting difference for our nation and the American people.

Mr. Chairman, this concludes my remarks. I would be happy to answer any questions you or other Members of the Committee may have.

Chairman ARCHER. Dr. Crippen, you may proceed.

STATEMENT OF DAN L. CRIPPEN, PH.D., DIRECTOR, CONGRESSIONAL BUDGET OFFICE

Mr. CRIPPEN. Thank you.

Chairman ARCHER. Without objection, your entire written statement will be inserted in the record.

Mr. CRIPPEN. Thank you. At the risk of starting a swearing contest, let me stipulate that I care a lot about Casey Hulshof. Make sure we all understand, Mr. Chairman, that this morning's discussion, not unlike many others in Social Security, has really been a mixture of economics, policy, polemics—kind of glued together with differing objectives, assumptions, and numbers.

What I am going to try to do in looking at the President's proposal is also return to some of the basic economics that we need to be mindful of as we talk about reforming Social Security as well as trust fund accounting and what it does or does not do.

The President's most recent Social Security proposal extends the apparent solvency of the Social Security Trust Fund by adding general funds. The proposal does not include any changes in the program's tax or benefit provisions. It maintains the earlier mechanism of transfers to trust funds as a means to pay down debt.

The proposal suggests further changes in congressional rules but imposes no additional requirements on the executive branch such as the submission of a budget with on-budget balance. Critically, it includes no enforcement mechanisms such as sequestration or debt limits, as the Chairman suggested earlier this morning. Indeed, the amount of the transfer is arbitrary and not even conditioned on achieving surpluses either in the on-budget portion or in the total budget. The Congressional Budget Office (CBO) concludes, therefore, that the proposal does not address the challenges posed by the impending retirement of baby boomers. Between 2010 and 2030, the number of retirees will increase by 80 percent. At the same time, the work force will grow by only 2 percent. As a result, there will be only two workers to support each retiree.

The best way to view the economic implications of this change is to analyze the fraction of the economy dedicated to Federal programs that benefit retirees. Figure 2 in my prepared statment, Mr. Chairman, illustrates the actuaries projections of costs of the Social Security and Medicare programs as a percentage of gross domestic product (GDP) over the next few decades. Spending for those programs is expected to rise from 7 percent of GDP in 1998 to almost 12 percent in 2030.

The concept embedded in this chart is important because ultimately it is not the form of financial transfer—a public or private pension, equities, or government debt—that matters. What is important is the amount of real resources, food, clothes, cars, and housing that those financial assets provide—real resources that will be consumed by the retired population. What matters is whether the economy will have expanded enough to meet the needs of retirees as well as the needs of the working population.

Obviously it is possible to change the outlook shown in this chart by making the numerator (the program benefits) smaller or the denominator (the size of the economy) larger. Social Security reform can affect the size of the numerator, the size of the denominator, or both. One test you might want to impose on any proposal to determine whether it is real reform is to see whether it changes either of those numbers. Indeed, we suspect the President's proposal does not.

Many of the current proposals for reform, including the President's, do not include fundamental reductions in Social Security or Medicare benefits. Therefore, the numerator will stay the same. The President, in transmitting his latest plan to the Congress, stressed the importance of reducing the debt and contributing to the growth of the overall economy. It is an application of what we have all been taught: If you save today and forgo consumption, you will be better off in the future. That tenet is as true for the country as a whole as it is for each of us.

Savings for the country include savings and borrowing by individuals, governments, and business—what we economists call net national savings. Simply moving the same resources from one pocket to another won't help. The larger the economy, the easier it will be for the working population to pay for the benefits expected by retirees. This statement doesn't require adherence to any particular strain of economic thought or political philosophy. Nor is it an attempt to make a case for any particular approach to reform.

In speaking about the importance of economic growth in the context of Social Security, Dr. Alice Rivlin—at a recent roundtable discussion at the Urban Institute—said that this is "a terribly fundamental point. And. . . not everybody gets it. . . it's is a question of everybody's pension plan, public and private, when those bills come due to the elderly and have to be paid out of the GDP that's being produced at that particular moment. Whatever it is, going to be much harder if that GDP isn't bigger. And the only way to make it easier is to make the GDP bigger. I mean, there isn't any other solution to this." As straightforward as that may seem, the current debate on Social Security is replete with confusion. Perhaps the murkiest corner of the debate can be found in the discussions of the meaning of the trust fund in the Federal budget and its economic implications.

The first thing to understand is that the government trust funds may have important political, maybe even moral, implications, but they have very few real economic implications. Trust funds are simply accounting devices. They facilitate long-term projections of cash commitments to help maintain an essentially pay-as-you-go system, but they have virtually nothing to do with whether obligations will be met or payments made.

More fundamentally, the balance in the Social Security Trust Funds tells us nothing about the economy's ability to pay for the benefits expected by retirees. The President's latest budget states that the trust fund balances are claims on the Treasury that, when redeemed, will have to be financed by raising taxes, borrowing from the public, or reducing other expenditures. The existence of large trust fund balances therefore does not by itself have any impact on the government's ability to pay benefits.

That is the primary problem with the President's proposal. It does not change the fundamentals. The transfers do not assure debt reduction, and the proposal contains no programmatic reforms. The transfers could, however, interfere with the one function the trust fund serves: assessing the financial balance in the program, whether dedicated taxes meet the program's promised benefits.

The point of all this is simple, Mr. Chairman. The larger the economy, the easier it will be for the working population to meet its obligations to retirees. Similarly, policies that diminish economic growth will make that job more difficult. Trust funds matter little in this economic context. Social Security reform, and perhaps other proposed policies as well, should therefore meet at least the criterion of helping, not hurting, future economic growth. There is no assurance that the President's latest proposal would meet that criterion or that it would change the fundamental nature of the trend shown in figure 2. Thank you, Mr. Chairman.

Chairman ARCHER. Thank you, Dr. Crippen.

[The prepared statement follows:]

Statement of Dan L. Crippen, Ph.D., Director, Congressional Budget Office

Mr. Chairman, Congressman Rangel, and Members of the Committee, I appreciate this opportunity to appear before you today to discuss Social Security financing and the President's recent proposal to extend the solvency of the Social Security trust funds.

My testimony focuses on several major themes:

- Financing the nation's current promises to the elderly will require a major reallocation of society's resources once the baby-boom generation has retired.
- A strong and growing economy will make it easier to fulfill pledges to Social Security and Medicare recipients, but it is not the entire solution.
- Although government trust funds arguably have some value as an accounting mechanism, their projected solvency does nothing to ensure that economic resources are available to cover program costs.
- The President's proposal to transfer general revenues to the Social Security trust funds would extend the funds' solvency from an accounting point of view but would not alter the underlying long-run imbalance between total federal revenues and spending.
- Changes in the budget process do not eliminate the need for substantive policy action.

The Current Outlook

This past summer, the Congressional Budget Office (CBO) projected that under current law, the federal government would accumulate total surpluses of about $3 trillion over the next 10 years. About two-thirds of those surpluses come from Social Security revenues that exceed the program's spending. Two important caveats apply to these projections:

- First, demographic and economic forces already in place are expected to erode the surpluses, renewing the federal government's fiscal imbalance of previous years. CBO's long-term projections indicate that under current policies, federal deficits will return by the time the baby boomers have fully retired, causing the federal debt and its corresponding interest costs to escalate rapidly as a percentage of national income.
- Second, deficits will reappear even earlier if the government spends more or taxes less than CBO projects. Developments since CBO's July update to *The Economic and Budget Outlook: Fiscal Years 2000–2009* suggest that the Congress and the Administration may identify more pressing priorities—increasing spending or reducing taxes—that conflict with devoting the entire projected surplus to retiring the federal debt.

The projected long-range fiscal shortfall is associated with three phenomena: the aging and eventual retirement of the baby-boom generation; increased life expectancy, which will lengthen the time people spend in retirement; and escalating per capita medical costs. Under the intermediate assumptions of the Social Security trustees, the number of elderly Americans increases by 80 percent over the 2010–2030 period while the population ages 20 to 64 grows by only about 2 percent. Those diverging growth rates mean that by 2030, there will be only two workers for every Social Security recipient compared with today's ratio of 3.4 to 1 (see Figure 1).

With demographic trends such as those, federal programs for the elderly will consume a sharply increasing share of national income and the federal budget (see Figure 2). The trustees project that spending for Social Security and Medicare as a percentage of gross domestic product (GDP) will rise from 7 percent in 1998 to almost 12 percent in 2030. Using similar projections, CBO expects that in 2030, the programs will constitute about 55 percent of total federal spending excluding interest, compared with about 35 percent in 1998 (see Figure 3). In addition, the Medicaid program will experience severe budgetary pressures in meeting the long-term care needs of increasing numbers of elderly people. Indeed, the ramifications of such demographics extend well beyond the federal budget to labor markets, private pensions, housing, and other sectors of the economy.

Social Security and Medicare compete with other federal programs for the government's resources, and that competition will become more acute over time. By 2014, Social Security benefits will outstrip payroll tax collections. Twenty years later, annual earmarked revenues will cover only about 70 percent of promised payments. The gap between revenues and benefits in 2030 is estimated at 1.8 percent of GDP, or about $160 billion in today's economy. An even larger shortfall—2.7 percent of GDP—is estimated for Medicare in that year. Addressing projected deficits of those magnitudes will require some combination of tax increases, benefit reductions, and cuts in other federal spending.

If left unchecked over many years, the budgetary pressures posed by an increasingly elderly population and burgeoning medical costs will lead to economic problems, because the resulting deficits crowd out private investment, slowing the growth of capital and output. High deficits would retard long-term economic expansion beyond the slowing of labor and capital growth that would occur in any case as people retire and draw down their savings. Thus, inaction on the budgetary problems associated with the population's aging risks a future drop in U.S. living standards.

Preparing for the Future

A strong and growing economy provides funds for the services that the federal government supplies. To fulfill the nation's promises to Social Security and Medicare beneficiaries, the government must acquire resources (through taxation or borrowing repaid by future taxation) from existing production when benefits are due. That is, in 2030, as in any year, pledges to the elderly as well as other federal priorities such as national defense, assistance to state and local educational agencies, public health services, and transportation projects will require the government to draw on economic production available at that time.

Additional capital accumulation, enhanced productivity, and increased work effort could help build a larger economy in the future. By implementing policies that promote capital accumulation, the nation could boost both its productive capacity and its wealth and essentially help prefund future consumption. But adding to the supply of capital requires less current consumption in exchange for more national saving and investment. One direct approach to increasing national saving is for the federal government to run annual budget surpluses. Strategies to encourage private saving might accomplish the same objective.

Economic growth would expand the capacity to fund future Social Security benefits and other federal commitments, and a larger economy could ease the transfer of additional resources to retirees. Strong growth swells revenues and reduces interest costs, improving the overall outlook for government budgets. Yet despite those benefits, growth is unlikely to eliminate fully the imbalances of the current Social Security program. The reason is that economic growth generally increases real (adjusted for inflation) wages, and under the current benefit formula, higher wages subsequently translate into higher Social Security benefits. Therefore, although the nation might be wealthier, it would still face a sharp increase in the budgetary resources necessary to pay for the Social Security and health care costs of the baby-boom generation during retirement.

TRUST FUND ACCOUNTING

The federal government's trust funds, including Social Security, are not trust funds in the usual sense but accounting mechanisms. They record the income from Social Security taxes, the expenditures for Social Security benefits, and interest that accrues on the difference. Private trust funds preserve assets for future use. Government trust funds do not do that because the government does not have financial assets to preserve. On the contrary, it currently owes the public $3.6 trillion. The government's ability to pay Social Security benefits depends ultimately on the total financial resources of the government—not on the balances attributed to the trust funds.

For much of its history, Social Security has been financed on a pay-as-you-go basis—current payroll tax collections fund current benefits. In recent years, however, tax collections have exceeded outlays, and trust fund balances have begun to mount. The Treasury credits a trust fund with nonmarketable special-issue bonds whenever the fund's income exceeds outgo; it redeems those securities whenever the fund's current income cannot cover current expenditures. To get cash for redemptions, the Treasury uses tax revenues or borrows money from the public.

In 1999, Social Security tax revenues exceeded benefits by about 14 percent. Moreover, interest and other intergovernmental payments boosted trust fund income so that the funds' total holdings grew by $125 billion, bringing total Social Security balances to $865 billion. Projections show those balances rising steadily over the next two decades, peaking at $4.5 trillion at the beginning of 2022 and then diminishing until the balances are exhausted in 2034. But the existence or absence of trust fund balances bears no relationship to Social Security's obligations or to the country's ability to fund benefits. The true obligations of the program are defined by its benefit structure and what the nation has promised to provide. As the President's budget states, "[T]he existence of large trust fund balances . . . does not, by itself, have any impact on the government's ability to pay any benefits."

Even as an accounting device, the Social Security trust funds leave much to be desired because the assets credited to those funds would cover only a small share of the future benefits promised under Social Security's current benefit structure. By contrast, a private pension plan is required to fund benefits on an accrual basis (as the benefit rights are earned); otherwise, solvency of the plan would depend on the uncertain viability of the plan's sponsor. Arguably, government retirement programs need not be held to the same standard because the government may extract the resources it needs to pay benefits by exercising its sovereign power to tax. If Social Security operated like a private pension plan—that is, it kept enough reserves on hand so that if the plan terminated and no new contributions were received, it could still pay all accrued benefits—its unfunded liability would total $10.4 trillion.

Another frequently cited measure bases the Social Security program's unfunded liability on the future revenue from and benefits to the population currently 15 years of age or older. The unfunded liability in that case would be $8.7 trillion. However, if the calculation assumed that revenues and benefits over the next 75 years continued as under current law, the estimated unfunded liability would be $3.1 trillion. From the narrow perspective of trust fund accounting, crediting the Social Security trust funds with a one-time infusion of government securities could eliminate the fund's solvency problem. But such an action does nothing to resolve the long-term problem of acquiring the resources necessary to meet benefit commitments.

Trust fund accounting practices have exerted an important influence on program financing and have at times signaled the need for corrective action. In 1983, the imminent depletion of the Old-Age and Survivors Insurance Trust Fund compelled the Congress and the Administration to agree on tax and benefit changes that restored balance in the program into the 21st century. Similarly, projected shortfalls in the Hospital Insurance portion of Medicare have spurred legislative action over the past two decades, with the Balanced Budget Act of 1997 being the latest installment. In contrast, growing trust fund balances could provide a sense of security unwarranted by underlying long-range fiscal conditions.

THE PRESIDENT'S SOCIAL SECURITY PROPOSAL

President Clinton recently proposed extending the solvency of the Social Security trust funds through 2050 by providing transfers from the general fund. The plan, which does not change the program's tax or benefit structures, differs from the Social Security framework in the President's budget because it does not include equity investments, Universal Savings Accounts, additional discretionary spending, or specific transfers to Medicare. It contains changes in Congressional procedural rules to make it more difficult to create on-budget deficits or to diminish on-budget surpluses. The proposal would impose no requirements on the Administration, such as submitting a federal budget without an on-budget deficit. Nor does it include any enforcement mechanisms such as sequestration. The plan also does not make the new Social Security transfers conditional on achieving actual surpluses, either in the on-budget portion or in the total budget.

The President's plan has been introduced as H.R. 3165 and contains the following main provisions:

- An amount equal to the interest on the cumulative Social Security surpluses from 2000 to each year during the 2011–2016 period would be credited to the Social Security trust funds. Those transfers would be added to the interest credited to the trust funds under current law. Social Security program actuaries estimate that such credits for the six-year period would total $951 billion.
- For each year from 2017 to 2044, the annual credit would equal the amount transferred in 2016.
- The points of order relating to Social Security in the Deficit Control Act would be extended through 2014.
- Any future legislation that decreased the new transfers to Social Security could not be credited as savings in pay-as-you-go calculations.
- A new point of order would be created to discourage any legislation that reduced on-budget surpluses or increased on-budget deficits.
- The President proposes to reserve one-third of the on-budget surplus that CBO projects for the 2000–2009 period to enhance Medicare solvency or provide a Medicare prescription drug benefit. A new point of order would be established to further that goal.
- The discretionary spending caps, with some increases, would be extended through 2014. Pay-as-you-go enforcement procedures would be extended through that year as well.

The Social Security actuaries estimate that on paper, the credits proposed by the President would postpone the trust funds' exhaustion from 2034 to 2050. The proposal would achieve that extended solvency without changing outlays or revenues of either Social Security or the budget as a whole. The President argues that the new accounting will reserve a portion of the on-budget surplus and make it more difficult to use those funds for most other purposes. (The two exceptions are transfers to Medicare and a new Medicare prescription drug benefit.) In effect, the proposal would commit future general revenues—to redeem the additional trust fund balances—when the funds are needed to meet obligations to future retirees.

Using general revenues to fund a portion of Social Security costs is not a new idea. The Social Security Amendments of 1983 contained a number of transfers, including payments for military wage credits and temporary payroll tax credits for wage earners and the self-employed. The general fund transfers under the President's plan, however, would be much larger than previous transfers, equaling one-sixth of total Social Security outlays during the 2011–2015 period.

Nor are the proposed transfers under the President's plan unique among recent Social Security proposals. Many other plans include general revenues as an element of a more fundamental restructuring of the Social Security program. For example, H.R. 1793, sponsored by Representatives Kolbe and Stenholm, would gradually scale back benefits but would also create payments from the Treasury to the trust funds. Under recent proposals by Martin Feldstein of Harvard University, the Treasury would transfer funds on the basis of assumptions about corporate income taxes. Another proposal earlier this year by Chairman Archer and Representative Shaw would essentially introduce general revenue funding for Social Security. Under that plan, income taxes equal to 2 percent of wages would go to individual accounts; when people were ready to collect benefits, the government would recoup those revenues and transfer them to the Social Security trust funds. (The proposals would redirect general funds much sooner than the President's plan.)

Shoring up government accounts such as the Social Security trust funds is often confused with maintaining fiscal soundness. For example, Medicare's Supplementary Medical Insurance (SMI) Trust Fund is frequently referred to as "actuarially sound" because the underlying law requires payments from the general fund of the Treasury to cover any costs not financed by enrollees' premiums. Thus, SMI may meet certain accounting standards for soundness, but those measures may have little relevance to the program's viability in the long run.

Assessing viability requires examining a program's resource requirements and society's willingness to provide those resources out of future production. Proposals like the President's to redirect general revenues to the Social Security trust funds address the narrow issue of trust fund solvency but not the broader one of overall fiscal soundness. Adding to the trust fund balances does nothing to ensure that the necessary economic resources will be there to support the programs; it simply shifts money from one government pocket to another. In fact, by relieving the most visible symptom of the program's fiscal distress, additional transfers from the general fund may lull the nation into overlooking the funds' less obvious problems. Such transfers could reduce the fiscal discipline imposed by the trust fund accounting mechanism and make it easier to delay the spending and revenue changes necessary to sustain the program in the long run.

BUDGET-PROCESS CHANGES AND SOCIAL SECURITY

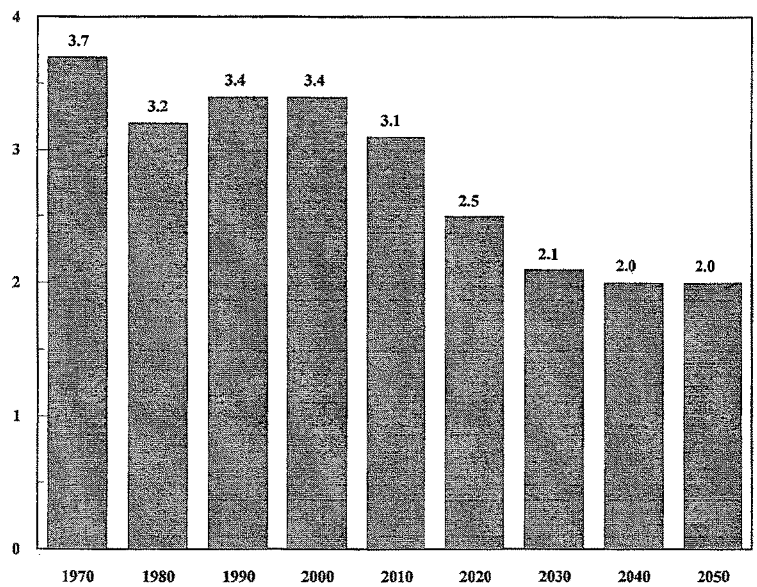
The President's Social Security legislation is the latest in a set of proposals designed to ensure that publicly held federal debt shrinks by at least the amount of the Social Security surpluses. Like the other budgetary mechanisms proposed during this Congress—the so-called lockboxes—the new procedural hurdles that the President proposes would limit Congressional action on future legislation that might reduce projected on-budget surpluses. Advocates of such mechanisms argue that making it more difficult for future Congresses to increase spending or reduce taxes would help prevent the erosion of recent improvements in the budget's bottom line. The perceived need for such constraints reflects the view that the federal government finds it difficult to operate effectively with persistent surpluses. Unless the mechanisms actually influenced behavior, however, they would have no direct effect on taxes and spending or on the economy. Nor would they ensure that the stated goal of debt reduction was, in fact, achieved.

CONCLUSION

Addressing the long-term budgetary impact of Social Security and Medicare outlays requires making difficult choices about the federal government's tax and spending policies. What are fair and appropriate levels of benefits for the elderly? How are the costs for those benefits best allocated among workers of different generations? Should benefit formulas for Social Security be scaled back, should eligibility criteria be tightened, or should Medicare reimbursement practices be made less generous? Should tax increases be scheduled to raise additional revenue? Plans that shift funds from one government pocket to another do nothing to address those programs' actual financing problem—the underlying imbalance between federal spending and taxes—and in fact could postpone corrective action.

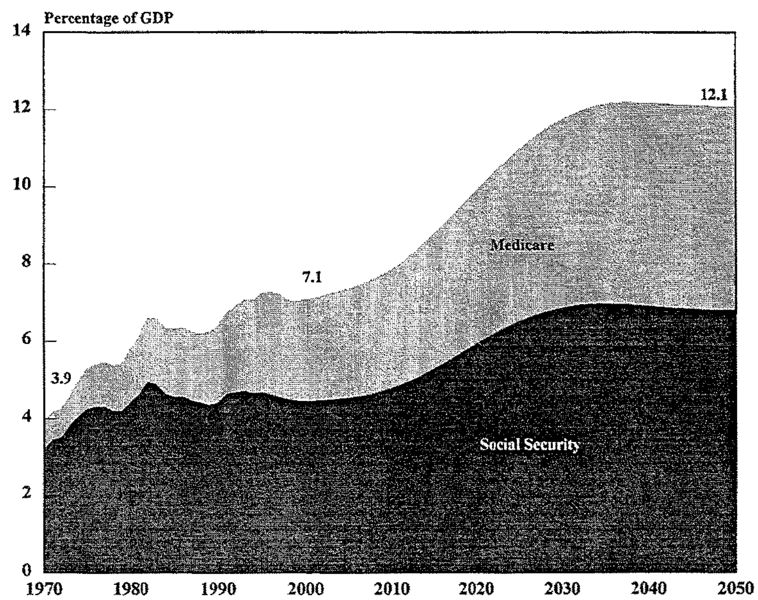
Such a postponement would have implications beyond those for the federal budget. Changes enacted in the near future need not be as drastic as the changes that would be necessary if action was delayed. The promises made under such programs as Social Security and Medicare are often a substantial part of people's financial arrangements for the future. By announcing significant policy changes well before their actual effects would be felt, the federal government would allow people to plan more effectively for their retirement.

FIGURE 1. NUMBER OF WORKERS PER SOCIAL SECURITY BENEFICIARY



SOURCE: Congressional Budget Office based on Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, *Annual Report* (1999).

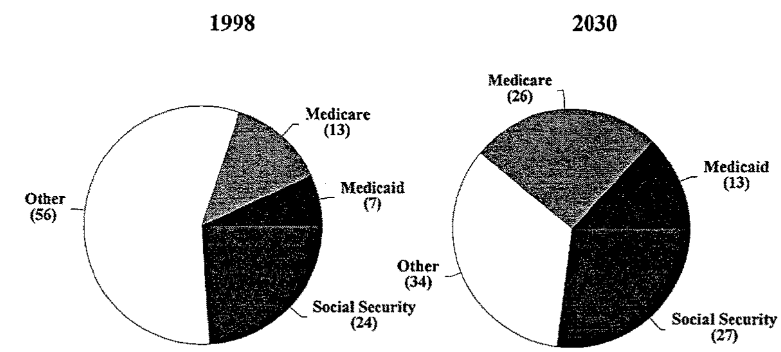
FIGURE 2. SOCIAL SECURITY AND MEDICARE SPENDING



SOURCE: Congressional Budget Office based on Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, *Annual Report* (1999); and Board of Trustees of the Federal Hospital Insurance Trust Fund, *Annual Report* (1999).

NOTE: GDP = gross domestic product.

FIGURE 3. SOCIAL SECURITY, MEDICARE, AND MEDICAID SPENDING AS A PERCENTAGE OF NONINTEREST FEDERAL EXPENDITURES



SOURCE: Congressional Budget Office.

NOTE: Based on measures from the national income and product accounts.

Chairman ARCHER. The Chair thanks both of you for, I believe, an objective analysis of where we are and where we are going.

Dr. Crippen, I am fascinated by your chart over here which is really the telling point over the long term for our grandchildren, and that is what percent of GDP are we committing? And that is why I mentioned in my last comment to the Secretary that I think that we have to be very, very concerned about these obligations and we also have to have 75-year plans to compare one to another as to where we are going to be in these outyears.

Now, if you were to overlay on your Social Security presentation the Archer-Shaw plan, what would be the percentage of GDP in the 75th year?

Mr. CRIPPEN. I can't make a definitive statement because, as you know, we haven't priced that plan specifically. But my best assessment at the moment is that the numerator would stay the same but the denominator would grow. Because the plan would increase net national savings, productivity and economic growth would be higher, consequently, Social Security would account for a smaller fraction of GDP.

Chairman ARCHER. The obligation of the Social Security Trust Fund would be reduced without cutting benefits?

Mr. CRIPPEN. Correct.

Chairman ARCHER. And that would therefore, according to your analysis, increase the denominator? Is that what you are saying? Or do you decrease?

Mr. CRIPPEN. It would increase the denominator. The economy would grow.

Chairman ARCHER. Which would mean that we would be taking a smaller percentage of GDP. All right.

Mr. Walker.

Mr. WALKER. Mr. Chairman, there are two ways to look at it. One, as you know, in your proposal you maintain a commitment to the current benefit structure. It is the way that you fund that commitment, that is changed, but the gross benefit commitment as percentage of GDP is the same. The government's net commitment would, however, be less in your proposal because of the increased rates of return that would be achieved through a diversified portfolio investment.

Chairman ARCHER. That is just another way to put it. The obligation of dollars that have to flow out of the trust fund would be reduced.

Mr. WALKER. The net, correct. The gross would be the same, but the net would be lower. The net is what matters to the trust fund but the gross is what matters to the economy.

Chairman ARCHER. And that is the dollars that the trust fund would be obligated to pay, even though we don't cut benefits.

Mrs. Johnson.

Mrs. JOHNSON of Connecticut. Thank you. This is an extremely important point that the Chairman has just made and that your chart, Dr. Crippen, makes. In your testimony, instead of looking at percent of GDP, you also look at it from the point of view of a percent of total spending that it would take to fund Medicare and Social Security if we do nothing to either program. Now, that is no prescription drugs, right?

Mr. CRIPPEN. Right.

Mrs. JOHNSON of Connecticut. That is no change in current spending, no enlargement, no coverage of cancer clinical trials which I have been fighting for, no change; and yet in just 31 years, 2030, in 31 years Medicare and Social Security would consume 55 percent of our national revenues. Now, you mentioned in the next line that Medicaid would add to that. Do you have any figure how much Medicaid would add to that because, of course, that is all the long-term care costs?

Mr. CRIPPEN. I think we have a chart that shows that as well. It is another——.

Mrs. JOHNSON of Connecticut. In terms of percent of Federal revenues as opposed to GDP. I think GDP is harder for people to understand.

Mr. CRIPPEN. The Federal Government's revenues are currently about 20 percent of GDP. If you assume they stay at about that level, we are using well over half of revenues (12 percent of the 20 percent) for Social Security and Medicare.

Mrs. JOHNSON of Connecticut. Well over half. So with Medicare——.

Mr. CRIPPEN. With Medicaid, it is 15.7 percent; 16 percent, roughly, of GDP—compared with 20 percent total government revenues.

Mrs. JOHNSON of Connecticut. So 55 percent of general revenues would probably go up to at least 60 percent. I think that is a very serious matter. And in looking at all of the plans, Mr. Walker, did you look at the plans from the point of view of their impact on generational equity?

Mr. WALKER. Yes, we did.

Mrs. JOHNSON of Connecticut. Which plans had the biggest—the least impact on generational equity?

Mr. WALKER. I think what you have to look at is a package. You can't just look at one element because there are pros and cons to every plan. Obviously to the extent that you don't change the benefit structure at all, there is no impact on generational equity. The President doesn't change the benefit structure whatsoever. His plan represents a financing proposal and it basically doesn't do anything about the generational equity.

Mrs. JOHNSON of Connecticut. Except what you say, those financing proposals that depended on general revenues aggravate the general equity problem because they make the workers pay more for the same benefits, and more of the budget goes for people over 65 and less is available.

I mean, the difference between what is available in 31 years for education and day care and all of those things, it is about 20 percent less.

Mr. WALKER. An important point here, Mrs. Johnson, we have done a projection as to what the Federal budget would look like, a simulation, in the year 2030 if we did not save the surplus.

Now, keep in mind the no-action scenario, we believe, is unrealistic because it assumes that the caps hold, that we have no emergency spending and that every dime of the projected surplus is saved.

If we didn't save the surplus, there would be no money left for any discretionary spending at all in the year 2030. That means national defense, the infrastructure, education, the environment, children's, programs, and our judicial system. Now, that is not going to happen but it just remphasizes the importance of being prudent about what we do with the surplus and to get on with entitlement reform because it is going to crowd out other spending if we don't.

Mrs. JOHNSON of Connecticut. I guess what I am trying to get at is if we solve the Social Security problem, say, entirely with general revenues, then—I mean, without any change in the plan, Social Security and Medicare are going to absorb 60 percent of our general revenues by the year 2030. If we solve Social Security entirely by adding new general revenues, then what percent of our public resources would be absorbed then?

In other words, if it is 60 now, would it be 70? Would it be 75?

Mr. WALKER. I don't have the exact number but I think the bottom line is this: We need to look at it differently, not just at the trust fund level. The trust fund is an accounting mechanism. It has legal significance, but it doesn't have economic significance. We need to look at percentage of the economy, the percentage of the budget, and other important milestones to gauge these programs.

Mrs. JOHNSON of Connecticut. So there is—it is important for us to look at where do the resources come from? Do they come from restructuring the program to reduce its costs and better distribute the benefits, perhaps, as in some of the proposals before the Congress; or if we generate them from investment in the market, as also some of the proposals do, so it comes from outside the tax revenues. All of those things will matter in terms of whether or not we will have the resources necessary to meet the needs of the next generation in terms of public program and public support.

Mr. WALKER. That is correct.

Chairman ARCHER. The gentlelady's time has expired.

Mr. McCrery.

Mr. MCCRERY. Thank you, Mr. Chairman.

Gentlemen, I would like to explore one of the principles of the President's plan on Social Security, and it was reiterated time and again by Mr. Summers, and that is we cannot use—we cannot run an on-budget deficit; in other words, we can't use any of the Social Security surplus.

We have got to sock away, we have got to retire publicly held debt, with every penny of the Social Security surplus. We can't use any of that because if we did we would have an on-budget deficit.

If we do that, if we subscribe to that, then you would have to say that we can't use any of the Social Security surplus to save Social Security. In other words, we couldn't use any of the Social Security surplus to finance a transition to a different Social Security system that might avert these kinds of numbers in the outyears.

That doesn't make a whole lot of sense to me, unless you say the best way to save Social Security is to plow every penny of the Social Security surplus into buying down the publicly held debt, and that is going to somehow create an atmosphere that will grow the economy enough to save Social Security.

Now, maybe that is a plausible scenario, but I think it is essential that we as policymakers, along with the administration, consider alternatives to that scenario. If the Archer-Shaw plan, which does use some of the Social Security surplus to finance the transition to their plan and in effect runs an on-budget deficit for some years, does a better job of getting those numbers on your charts down, saving Social Security, providing a defined benefit for seniors that we think now is substantial and adequate, then we ought to choose that over the administration's proposal to just sock it all away into buying down the debt.

Am I wrong? Have I missed something in that analysis or is that essentially what we are looking at?

Mr. CRIPPEN. I think there are two points to be made, Mr. McCrery. One is that there is no guarantee under the President's proposal that the debt will be reduced in the first instance.

Second, though, and to your fundamental point, even if Federal debt is reduced, it will help economic growth, but it is not the whole solution. You can't grow your way out of this problem. Particularly with the current benefit structure, Social Security tends to grow along with real wages and the economy. So economic growth will help alleviate the problem some, but fundamental reforms will be needed to solve the problem completely.

Mr. WALKER. The least risk in approach is a combination of two things, paying down debt and engaging in real program reform. Ultimately, you need to do both. You can't just pay down the debt. And most reform proposals require some use of general revenues. It is a matter of how much and when they use general revenues, and I think you need to look at the economic substance of it. That is what is most important.

Mr. MCCRERY. So are you both saying that the administration is not necessarily correct in their approach; that perhaps we should examine, using some of the Social Security surplus, spending some of the surplus, on a transition to a different Social Security system rather than just buying down debt with it?

Mr. CRIPPEN. Obviously neither of us can speak for them. I don't know that they would have that as a condition or not. As with the Medicare reserve, they say we don't want to spend this part of the surplus for Medicare—or for anything other than Medicare—so it would be available for prescription drug coverage or other reforms. They may have the same attitude about Social Security. I just don't know.

Mr. MCCRERY. It doesn't sound like it. That is not their proposal. Their proposal is to put every penny of the Social Security surplus into buying down debt held by the public, and then transferring some portion of the general revenues, the on-budget surplus, into the Social Security Trust Fund. So then that is——.

Mr. WALKER. The original plan is to pay down debt and then in addition to paying down debt, crediting to the Social Security Trust Funds an unearned grant equal to a portion of what they paid down the debt.

Mr. MCCRERY. Right.

Mr. WALKER. Their belief is—and you can agree or disagree with it—is that this increases the likelihood that debt will be paid down. They don't have to be linked and, frankly, one of the things that we have to do as a Nation is we have to look at how are we going to approach fiscal policy in light of budget surpluses instead of deficits.

We have just issued a report on how other nations have approached this because you have to think differently. You have to think in terms of how much debt you have as a percentage of GDP; the size of certain programs as a percentage of the overall economy and as a percentage of the budget, which are fundamentally different. But there are several different ways you can accomplish the objective.

Mr. MCCRERY. Thank you.

Chairman ARCHER. Mr. Shaw.

Mr. SHAW. Thank you, Mr. Chairman.

Mr. Walker, there is a word that has been thrown around all over the place through the course of this hearing. That word is "solvency," and it concerned me to the extent that I got the Webster dictionary out and looked it up. From an accounting standpoint, what is your definition of solvency? And then I will tell you what Webster says.

Mr. WALKER. Well, the way that it has been used in the Social Security context is to what extent are there trust fund assets available to be able to pay promised benefits.

Mr. SHAW. All right, let's stop there. Are the Treasury bills that are in the trust fund an economic asset?

Mr. WALKER. They are not a hard asset. They are a promise-to-pay. They are backed by the full faith and credit of the United States Government. They represent a first claim on future generations'——.

Mr. SHAW. Right.

Mr. WALKER [continuing.]—General revenues. Nothing more, nothing less.

Mr. SHAW. Then I would submit, using that definition and going forward, that we are facing an insolvency problem in the year 2014 when at which time there are going to be insufficient FICA taxes going into the Social Security Administration to take care of the obligation to pay benefits.

Mr. WALKER. I think your point, Mr. Shaw, is that in 2014 we turn a negative cash flow, and typically solvency is something that is associated with cash flow in the private sector. We have different definitions in the public sector. But 2014 has economic substance, there is no doubt about it.

Mr. SHAW. What really worries me about this whole thing is when you start talking about 2035 and 2050, everyone's eyes glaze over and they say, what is the problem?

Well, the problem is that the taxpayer is going to get skinned starting in 2014 unless this Congress and this White House act together to solve this problem. And this is what concerns me. It is the cash flow that we need to really concentrate on, because that cash flow, as soon as that cash flow is insufficient and we have no Social Security surplus and as a matter of fact we start a huge deficit, at that point it is going to be up to the Congress to levy sufficient taxes or cut something in order to take care of its obligation to pay the benefits, because that wonderful FICA surplus that we have had for the last 60, 70 years, all of a sudden goes away.

I think it is very important to all of us to realize and to face the fact that Social Security, as it was set up as a pay-as-you-go system, was a wonderful system and there wasn't anything wrong with it the way it was originally set up because you had over 40 workers for each retiree. Now we are down just a little over 3. Soon we are going to be down to a little over 2, and at that point you are going to have a huge, huge problem because you are just going to have a disproportionate enough number of seniors that the workers will be really struggling to try to support.

The problem is, and what we have to talk about is cash flow, and that is what I think is most important and I think we need to concentrate on.

Mr. WALKER. Cash is key. In addition, we have to look at what percentage of the budget and what percentage of the economy is represented by mandatory spending programs. Those are very real challenges.

Even if the President's proposal is adopted and debt held by the public went down to zero, total debt is not zero and debt held by the public will go up eventually. We have to be prudent about the surplus and we have to reform these programs.

Mr. SHAW. There is nothing wrong with paying down the debt, and I would be willing—I would be willing to take a look at that and take a sharp look at that, trying to find a solution. But the problem is we have got to build up some real wealth, some real economic assets, if we are going to get over this system as a pay-as-you-go system, because with the demographics out there today, with the population—we are living longer, which is a wonderful thing, but the problem is also that we are having less kids and we have got this huge group of baby boomers that is coming through the system that is going to absolutely knock the cash flow in the head and there will be no cash flow, and that is when we are going to have just a huge problem.

According to our projections under existing law, if we do nothing we are going to be running up about a $20 trillion deficit. That is a terrible thing to leave to our kids.

This is what really concerns me so much. So we really need to develop a hybrid system. You can't do away with the existing system because we have got too many people that depend upon it. So when you have an opportunity to leave the existing system alone, change nothing about it but just put together something on the side that is going to come to the rescue of the system, and where we can find, even though it is going to take some general revenue for a few years, starting in about 2014, 2015, but we can see that we have put in place a solution that is going to save Social Security for all time.

I think it is very important that people listening to this debate realize that when we are talking about 75 years, that is just because that is as far as the Social Security Administration will score these plans, but actually it is for all time. The surplus that we create under the Archer-Shaw bill continues to accumulate a huge surplus. So I think it can certainly be said that it saved Social Security for all time, and that would be a legacy that this White House and that this Congress could leave to the American people and to our kids and grandkids, and I think that is our responsibility to move forward.

Chairman ARCHER. It sounds like a good place to end this hearing, unless you two gentlemen want to make any further comments.

Mr. RANGEL. Mr. Chairman.

Chairman ARCHER. Mr. Rangel.

Mr. RANGEL. I would just like to make two comments.

First, I want to thank both of you for the good work you do for the Congress. We appreciate it. And Mr. Walker, I just want to make certain that your testimony is consistent with a statement that was attributed to you in your report. That is: that the Archer-Shaw proposal reduces the projected unified surplus and increases the projected unified deficit as a share of the GDP through the middle of the next century.

Is that accurate?

Mr. WALKER. Yes, through 2046. Beyond that it helps.

Mr. RANGEL. You also say that it results in higher levels of debt held by the public until the final years of the assimilation period.

Mr. WALKER. Yes. If it is all right, Ranking Member Rangel, I think that—let me mention four good things and four concerns, with regard to the Archer-Shaw proposal.

First, it achieves long-term solvency and sustainability of the program as far as you can evaluate it.

Second, it maintains current law benefits. Third, has possible payroll tax reductions in the outyears without tax increases. Fourth, it advance-funds, which could have some positive effect on intergenerational equity and on long-term savings.

On the concern side, it has major increases in publicly held debt and uses general revenues over the next 45-50 years. Over the very long range, it works out; it captures better rates of return. Third, it creates contingent liabilities if individual accounts perform poorly.

Finally, the offset structure could create an expectation gap among people who have these individual accounts, and there is not a time frame for implementation.

So, like every proposal, including the President's, there are pros and cons. But what is remarkable, Mr. Rangel, if you look at the substance of what the President has proposed, including his USA accounts, and Archer-Shaw and other proposals, there are a lot of common denominators here. There are a lot of common denominators.

Mr. RANGEL. That is where I hope that we can pick the ball up and move forward.

Dr. Crippen, to make sure that we are reading from the same set of books, and since there always appears to be a controversy about this—it appears that you indicated that the Republican budget actually is $17 billion into the Social Security Trust Funds. In response, the Republicans always pull out a letter where they suggested to you certain things you could say to show that their plan would not really violate the Social Security Trust Fund.

Having said all of that, with all of the information that you have available and with your responsibility to the Congress, both Republicans and Democrats, could you say with any degree of accuracy whether you believe that the Republican budget proposals violate or go into the Social Security Trust Fund?

Mr. CRIPPEN. Certainly, Mr. Rangel. Let me preface this by saying that these are all estimates of a $1.8 trillion budget in a $9 trillion economy. But by our lights, both the President's budget and the congressional actions to date have been about the same. That is, they blow the spending caps by over $30 billion and could end up borrowing from Social Security as much as $16 billion or $17 billion. That is the current state of affairs.

Again, these are estimates of what is going to happen over the next 12 months, and those estimates may not prove to be accurate.

Mr. RANGEL. Let me say, since you are the Congressional Budget Office and not the Presidential budget office, and since the President proposes and we make the final decisions, are you saying that what has been legislated, not proposed, in the Republican budget is about $17 billion over?

I mean, and you can bring anybody else you want in to help answer, in terms of legislation what is the answer?

Mr. CRIPPEN. Part of the conflict or controversy has been on keeping everything on the same basis. If we score the President's budget and congressional action on the same basis, the President and the Congress have both advocated and enacted spending—the President signed some of it already—that by our accounting could end up requiring the government borrow some money from the Social Security Trust Fund.

Mr. RANGEL. Listen, what is good for the Republicans is good for the President, too. With you being the Congressional Budget Office, I thought maybe that your primary concern would be what the Congress is doing, and that OMB and other administration people would be able to point out what the President is doing.

So I am not here in defense of the President because he may be doing worse than the Republicans, I don't know. Ultimately, we should ask you for your advice in terms of what he is proposing. But since we are legislating and since we have a Budget Committee, it is very important that we have it made clear that this legislative body, under the leadership of the Republicans, is $17 billion into the Social Security Trust Fund. Who knows what the President is, but one thing we do know, is that CBO is saying that with your estimates the leadership is $17 billion over.

This doesn't give the President a clean bill of health. That is not what I am trying to do. It is just that certain people recently on television are saying that you are saying this is just not so.

I am not prepared to say what you are saying about the President is not so. I am just saying that since you have a job and since your job has always had the support of a bipartisan Congress, I don't want on your watch for your position to be distorted, because we depend on you. We don't always like hearing what you have to say, as Democrats or Republicans, but we depend on you and you do a good job. I want to thank you.

Chairman ARCHER. Dr. Crippen, you mentioned exceeding the spending caps. Is emergency spending included——.

Mr. CRIPPEN. In the caps?

Chairman ARCHER [continuing.] Under law?

Mr. CRIPPEN. Under the law, the caps are adjusted upward to accommodate emergency spending.

Chairman ARCHER. All right. So are you then saying that even in correspondence with the law that adjust the caps for emergency spending, that we will be spending more than the caps this year?

Mr. CRIPPEN. With the adjustments, we are likely to be pretty close. There is about $25 billion in there.

Chairman ARCHER. Is it not also true that if the amount of spending exceeds the caps, that there is automatic sequestration by OMB?

Mr. CRIPPEN. Yes, and they use their numbers.

Chairman ARCHER. So if, in fact, we do exceed the caps, that spending will automatically be cut back by OMB and will not be permitted to exceed the caps?

Mr. CRIPPEN. Yes, if that's what OMB determines.

Chairman ARCHER. That is the law?

Mr. CRIPPEN. Yes.

Chairman ARCHER. OK. I think we have to be awfully careful as we state these figures, that we will spend a certain amount above the caps, which cannot happen under the law.Is that not correct?

Mr. CRIPPEN. Right, based on OMB calculations.

Chairman ARCHER. All right.

Mr. RANGEL. If the gentleman would yield on that. That would mean, if what you say is correct, that anything that they labeled as emergency doesn't count. So if they say the census which occurs every 10 years is an emergency, as far as you are concerned, it is an emergency.

Chairman ARCHER. The gentleman is correct. That is provided in the law, and the President——.

Mr. RANGEL. And the second thing that you are saying——.

Chairman ARCHER. When the President—I am not going to yield anymore because I want to close this hearing down.

Mr. RANGEL. Well, that sounds unfair, Mr. Chairman.

Chairman ARCHER. But second, under the law, the President and the Congress have to agree to the emergency designation.

Mr. Walker, how would you evaluate a dollar invested as to a dollar of debt reduced, comparatively?

Mr. WALKER. Well, first, in the context of the debate that we are having here, if you end up reducing debt, that has a sure-fire, absolute, positive effect on increasing net savings. You know you have accomplished something.

If you are investing it, you might be investing it in lieu of paying down debt. And then it depends upon what, if any, incremental rate of return you might be able to get. So it is possible that it could be better for the government and the budget to invest, but not for the economy.

Chairman ARCHER. The basis of my question was to make a comparison between the paying down of government debt to the public and having money in private savings accounts that would be invested, and that is a part of the puzzle that you did not mention.

First, paying down debt also means paying down a lot of foreign-held debt, which does not flow back into the United States necessarily to help our economy. It is not a dollar-for-dollar help to our economy.

On the other hand, if you take dollar for dollar and you put it into a personal savings account, that increases the personal private savings of this country, dollar for dollar. None of it is drained off into the foreign-held debt that is paid down.

In your analysis, I think you have got to also refer to the fact that it is not just the paying down the debt that helps the economy, but what we do in the Archer-Shaw bill is for every dollar that the President would pay down in debt, we see goes into personal savings accounts that are put into our economy.

Is that not at least an equal offset, if not a better offset, to the economy?

Mr. WALKER. A couple of things, Mr. Chairman.

First, I think both your proposal, as well as the President in his earlier proposal, acknowledged that there could be incremental benefits for the government through equity investing of some of the surplus. Yours does it through individual accounts. His would do it collectively.

Chairman ARCHER. No, no, but this is a different issue that I am talking about now.

Mr. WALKER. OK.

Chairman ARCHER. This is the macroissue of how you help the economy.

Mr. WALKER. I understand.

Chairman ARCHER. Paying down debt or saving and investing.

Mr. WALKER. I understand. The real question, Mr. Chairman, is how much, if any, offset might there be for individuals who are saving individually, where that might affect their behavior on whether or not they might save otherwise through personal savings or through private pension plans? You have to look at what, if any, effect that might have.

Now, the way that you have designed your proposal, as I understand it, you basically are maintaining the defined benefit promise under Social Security so people will get the same—they could get more but they won't get less—but you are using individual accounts as a way to try to use a financing mechanism to meet that defined benefit promise.

There could be incremental rates of return that would benefit the trust fund and the budget and, in fact, there should be incremental rates of return to the government that would reduce the net cost of Social Security benefits to the government.

Chairman ARCHER. But if you only take one side of the equation and you only talk about the benefit of paying down the debt and you ignore the fact that for every dollar that you would pay down the debt you are creating a dollar of personal savings accounts, which is wealth and investment, and you ignore that as any benefit to the economy, I don't think that you are properly evaluating the situation.

Mr. WALKER. I don't think we do ignore it. Nor do I think we should ignore it. I mean, it is a different element. In other words, one is dealing with the Federal budget. The other is dealing with savings and investment. For the budget, the higher returns would offset the government's cost of promised Social Security benefits. For the economy, however—excluding behavioral and other second-order effects—there is no difference between using a dollar of surplus to reduce debt held by the public and using a dollar of the surplus to fund individuals savings accounts.

Chairman ARCHER. OK. But the impression was created that because the President pays down the debt, that that is superior and ignores what is happening, which is a dollar-for-dollar offset of money that is being put into personal savings accounts, and then invest it in creating wealth. And that has to be a big, big plus that at least would offset, if not be better than paying down the debt, particularly inasmuch as a portion of the debt is held by foreigners.

Mr. WALKER. I understand what you are saying, Mr. Chairman.

Chairman ARCHER. OK. Thank you very much.

Gentlemen, thank you for coming and giving us the benefit of your input. The hearing is concluded and the Committee is adjourned.

[Whereupon, at 2:25 p.m., the hearing was adjourned.]

[Submissions for the record follow:]

Statement of American Farm Bureau Federation

PRESERVE INTEGRITY OF SOCIAL SECURITY

Farmers and ranchers support the preservation of the Social Security system as a safety net to provide workers and their families retirement income, disability protection or assistance because of the early death of a family wage earner. Farmers and ranchers are concerned, however, about the future and financial soundness of the Social Security system. Farm Bureau believes that reform is needed to preserve the integrity of Social Security for retirees and workers paying into the system.

Ninety-nine percent of farms are operated by sole-proprietors and or by family partnerships. As self-employed individuals, agricultural producers pay the full 12.4 percent payroll tax, usually as one lump sum along with their income tax payment. They are painfully aware of the high taxes needed to fund the current system and realize the urgency of saving the Social Security system.

CONCERNS ABOUT THE PRESIDENT'S PLAN

Farm Bureau opposes President Clinton's proposal for two major reasons.

First, it does not allow for an evolution of the current pay-as-you-go system to one that is pre-funded with a choice of remaining in the current system or shifting to one with personal accounts. While Farm Bureau supports preserving the Social Security system, we believe people should have the option of contributing to personal retirement systems. For years we have recognized each individual's right to participate in pension plans in addition to Social Security. We believe that people should also be able to invest in private plans within the Social Security framework using the same deposit percentages and withdrawal age rules as the regular Social Security program. People should have the right to choose to stay in the standard Social Security program or shift their Social Security taxes into personal retirement accounts.

Second, we are opposed to general revenue funding of the current system or increased taxes to fund the current system. We oppose any proposal to finance Social Security retirement income benefits out of general revenue. We oppose an increase in Social Security taxes. Social Security, either the standard plan or new private retirement plans, should be funded by payroll taxes. Social Security taxes should continue to appear as a separate deduction of Federal Insurance Contribution Act (FICA) taxes to make them clearly identifiable.

All employees, both in the private and public sector, should be included in the Social Security program. Employers and employees should continue to share equally in the payment of Social Security taxes. Low-income taxpayers should not be exempted from paying Social Security taxes because of their level of incomes.

SOCIAL SECURITY SURPLUS

Social Security taxes collected should be placed in a restricted interest-bearing fund to be used only for Social Security purposes. Because we support placing Social Security funds in interest bearing accounts and private retirement accounts, we oppose government investment of Social Security Trust Fund money in stocks of private companies. We support President Clinton's decision to no longer recommend investing in stocks of private companies in his Social Security plan.

BENEFITS

While the President's plan does not specifically address benefits, they have to be considered in any reform plan. Benefit levels should be preserved for retirees and those that are near retirement and, when in need of adjustment, should be changed based on a percentage of the annual decrease or increase in average wages. Benefits, both in the standard plan and in alternative private plans, should be based on an individual's contribution to the system. We oppose means testing as a way to limiting Social Security benefits for those that have contributed to the system. We oppose earned income restrictions for those receiving Social Security benefits.

The average age of farmers and ranchers is now 54 years old. This means that almost half of them are at, or near, retirement age. They are very concerned about the return they will receive on a lifetime's worth of Social Security taxes. The current system is a major portion of their retirement program. They must be able to rely upon Social Security in their retirement years.

SUMMARY

Farm Bureau supports reforms to the Social Security system. The integrity of the system must be maintained for retirees and near retirees while giving workers the opportunity to invest their Social Security taxes in personal retirement accounts. We oppose general revenue funding of the current system, tax increases and government investment of Social Security Trust Funds in equities markets.

Statement of Hon. Jim Ramstad, a Representative in Congress from the State of Minnesota

Mr. Chairman, thank you for calling this important hearing to review the President's legislation to preserve the Social Security program.

Seniors in Minnesota always remind me that as we address the financial concerns facing the Social Security program, we must strive to secure the long-term financial solvency of this vital program in a bipartisan, pragmatic way. I completely agree, and I appreciate this opportunity to thoroughly review the President's proposal and identify ways in which we may work with him to keep Social Security solvent for another 75 years.

My constituents have told me at town meetings, and through calls and letters, that they want real improvements to be made so Social Security is operating as promised for current and future beneficiaries. They do not want taxes raised or benefits cut, and they want reforms to ensure the solvency and viability of the program both for current and future beneficiaries -especially their children and grandchildren.

Most importantly, they believe financial soundness is paramount in the design of any new system. They don't want any more budget gimmicks. They don't want more IOUs in the Trust Fund.

These are some of the basic elements I will be looking for in the President's plan today.

Again, Mr. Chairman, thank you for holding this hearing today. I know we are all committed to saving this important program and I look forward to learning more today from our witnesses about the President's plan.

Statement of Hon. Nick Smith, a Representative in Congress from the State of Michigan

Since the 1998 State of the Union Address, the President has spoken of putting Social Security first. I applaud this sentiment, which has gone a long way toward elevating the Social Security issue and bringing it to the attention of the American people. There is mounting evidence, however, that the President's Social Security proposal does not put Social Security first and will not keep it solvent for current and future retirees.

THE SOCIAL SECURITY PROBLEM

Actuaries at the Social Security Administration now estimate that our Social Security system faces an unfunded liability of $9 trillion. The fact is that there will be only two workers paying taxes to support each retiree early in the next century—down from seventeen in 1950 and three today. These demographics will eventually force a restructuring of the program. Because of these demographic trends, the current Social Security system will collapse unless Congress takes steps to address the expected shortfall.

Social Security also faces another more fundamental problem. Changing demographics wouldn't be a problem if benefits were paid for with savings. That, however, is not the case. Congress needs to replace Social Security's current pay-as-you-go financing system—the cause of our present problems—with a system based on worker-owned and—controlled savings which is not subject to shocks caused by demographics.

The federal government guarantees Social Security benefits under law. That said, the government has no resources available to fulfill the promises it has made. This leads to the inescapable conclusion that unless we reform Social Security, the government will be forced to raise taxes or cut benefits to cover the $9 trillion shortfall. Further, the looming problem becomes increasing urgent and the potential solutions increasingly wrenching as time is wasted.

THE PRESIDENT'S PROPOSAL

How does the President propose to close the $9 trillion gap between revenues and benefits and honor the government's promises? The essence of the President's proposal is to credit budget surplus monies plus savings from reductions in public debt to the Social Security Trust Fund.

This sounds good, but actually does little or nothing to improve the situation. The government securities in the Trust Fund cannot be sold. Therefore, they are fundamentally promises that the government will provide money at some future time. It is, in effect, a commitment to increase taxes or borrowing in the future.

The point must be made that this proposal does nothing to ensure the government will be able to honor its promises. The law already guarantees benefits, so the addition of government account securities to the Trust Funds is redundant. The real questions

—which involve what the government will have to do to honor its promises—have been neatly sidestepped. The President's plan attempts to redeem government promises with more promises, all of which will have to be fulfilled by some future President and Congress starting in about fifteen years. The likely result will be tax increases on workers, which is the same solution that Congress imposed when it began to run short of tax revenues in 1977 and again in 1983.

THE KEY: PRIVATE INVESTMENT

The President's proposal is also unfortunate because it distracts attention from the demographic crisis and the fatal weakness of Social Security's pay-as-you-go financing system. A genuine solution to Social Security's problems has to address these issues. Fortunately, a variety of sound solutions have been proposed in Congress.

One thing that all these solutions have in common is worker-owned investment accounts. This aspect is fundamental because it dismantles the pay-as-you-go financing system. Instead of transferring money from people who are working to people who are retired, individual accounts allow workers to save for themselves.

Worker-accounts have additional advantages in that they raise the rate of return on Social Security taxes. Money held in the Social Security Trust Funds earns a paltry return, much lower than the long-term return we can expect on conservative investments in the bond and stock markets. This makes it possible to cover much of the $9 trillion shortfall without having to make painful choices of raising taxes or cutting benefits.

Although I will focus on my proposal (H.R. 3206) because I know it best, there are a number of sound proposals based on worker-owned accounts which are now pending in Congress. In particular, I would like to point to those offered by Reps. Kolbe and Stenholm, Budget Committee Chairman Kasich, and Chairman Archer and Rep. Shaw of this Committee.

MY SOLUTION: THE SOCIAL SECURITY SOLVENCY ACT

Today, each worker contributes 6.2% of his salary to Social Security which is matched by 6.2% from his employer for a total tax equal to 12.4% of the worker's salary. Under my proposal, workers would get back 2.5% of their paychecks starting in 2001 to put into an investment account for retirement. Over time, this contribution rate will rise.

The account will generate a hearty sum. Let's consider the case of a high school graduate who starts working on January 1, 2001 and has a typical career. He starts work at $20,000 a year and he gets a cost-of-living raise plus 2% a year. Let's assume he earns a 7% rate of return, after inflation, in his retirement account invested in equities. Seven percent may seem conservative in light of the 25% and more returned in the stock market over the past few years. However, this is the rate many experts use (including the members of the recent Social Security Advisory Committee) to reflect average returns over long periods of time.

Given these assumptions, this worker would have about $1,000,000 in his private account under the Social Security Solvency Act when he retires in 2046. He would also receive a reduced Social Security check from the government. His wife would have a private account of her own (whether or not she works) and a monthly Social Security check. The couple would also own and control the money in their accounts and would not have to rely entirely on government promises.

A worker earning less would still accumulate significant funds over a lifetime while retaining a large government Social Security benefit. For example, a worker earning the minimum wage—$5.15 an hour—would retire with $514,000 under this proposal.

We've talked about 18 and 20 year olds. What happens to those who've worked for a while? Like the younger workers, they will have two sources of retirement income: private accounts and government benefits. But because their personal accounts will be smaller because they've made fewer contributions and their savings have less time to compound and accumulate, they will receive higher government benefits. The precise level of benefits is dependent upon these factors and the worker' income. This proposal, though complicated, aims to treat workers equitably based on work and contribution histories.

PROTECTING SENIORS AND TAXPAYERS

Some have suggested that current retirees should accept lower benefits to facilitate the change to a new system. Frankly, I disagree. The Social Security Solvency Act maintains promised benefits for current retirees, including full cost-of-living increases. Retirees, many of whom have made retirement plans and cannot return to work, should not see their benefits cut.

I also believe that payroll taxes are already too high. Social Security taxes have been raised 38 times in rate or base since 1971. I want no part in raising them even higher. My plan also avoids the issuance of any new debt. We have already piled too much debt on future generations.

PAYING FOR CHANGE

Maintaining benefits for current retirees while building a stable Social Security system based on worker savings will have a cost. These changes are made gradually under the Social Security Solvency Act.

The best choice for financing the new system is to dedicate budget surpluses to this purpose. The bill would transfer $829 billion from projected government surpluses to Social Security over the next ten years. There is no better purpose for these surpluses than to build a brighter future for all American workers. The bill also includes stringent budgetary controls to help ensure that Congress doesn't spend those surpluses before they can be transferred.

In addition, the proposal slows down the growth rate in Social Security benefits. The average monthly Social Security check is now around $750. Because these benefits are adjusted to reflect wage growth—which has outstripped the Consumer Price Index—the average Social Security benefit will rise to between $1,100 and $1,400 in 1999 dollars depending upon the economy's performance by 2048. The Social Security Solvency Act will slow down this growth in benefits in exchange for private savings. Further, the changes in the benefit formulas are designed to spare our least affluent workers.

WILL IT WORK?

To answer this question, I submitted the plan to the actuaries at the Social Security Administration. They have analyzed my plan and have certified that it would restore the system's solvency for at least the next 75 years.

The Social Security Solvency Act is a comprehensive reform that will create a more secure retirement system for American workers. Its features include:

- personal retirement security accounts (PRSAs) to give workers control over their own retirement plans while increasing income and wealth at retirement;
- protections for women that include shared PRSAs for nonworking spouses and increased widow's and widower's benefits;
- the repeal of the Social Security earnings test;
- a safety net for low income and disabled workers;
- no benefit or COLA reductions for current retirees;
- no new taxes or new debt; and
- the restoration of Social Security's long-term solvency.

A wide variety of interested individuals and organizations have also looked at the proposal and lent their support. Federal Reserve Chairman Alan Greenspan, who also chaired the 1983 Social Security Reform Commission, has written me and expressed support for my approach. Organizations supporting the Social Security Solvency Act include the U.S. Junior Chamber of Commerce, the Seniors Coalition, and 60+.

This legislation is the culmination of six years of study since I came to Congress. Hundreds of experts and thinkers have contributed to it, many of whom I spoke to as I chaired the Budget Committee's Social Security Task Force. This is a proposal that can strengthen this vital program for the 21st century.