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# THE PRESIDENT'S BUDGET SUBMISSION FOR FISCAL YEAR 2000

## HEARING

BEFORE THE

## COMMITTEE ON THE BUDGET
## HOUSE OF REPRESENTATIVES

ONE HUNDRED SIXTH CONGRESS

FIRST SESSION

HEARING HELD IN WASHINGTON, DC, FEBRUARY 3, 1999

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# THE PRESIDENT'S BUDGET SUBMISSION FOR FISCAL YEAR 2000

**WEDNESDAY, FEBRUARY 3, 1999**

HOUSE OF REPRESENTATIVES,
COMMITTEE ON THE BUDGET,
*Washington, DC.*

The committee met, pursuant to notice, at 10:02 a.m., in room 210, Cannon House Office Building, Hon. John Kasich (chairman of the committee) presiding.

Present: Representatives Kasich, Chambliss, Shays, Herger, Franks, Smith, Nussle, Hoekstra, Bass, Gutknecht, Hilleary, Sununu, Pitts, Knollenberg, Thornberry, Ryun, Collins, Wamp, Green, Fletcher, Ryan, Toomey, Spratt, Rivers, Thompson, Minge, Bentsen, Davis, Weygand, Clayton, Price, Markey, Kleczka, Clement, Moran, Hooley, Lucas, Holt, Hoeffel, and Baldwin.

Chairman KASICH [presiding]. The committee is going to come to order.

What we are going to do first is the consideration of Mr. Crippen, and, as you know, June O'Neill is leaving the CBO, and Senator Domenici and I have met with a number of candidates along with Mr. Spratt and Senator Lautenberg, and, essentially, Senator Domenici and I have come up with a recommendation who is Dan Crippen.

Probably the single best thing about Dan Crippen is that he has his Ph.D. from one of the finest universities in the world, Ohio State University, and he has his M.A. from Ohio State also, so he got it right there and his B.S. from the University of South Dakota. He also is a principal in the Duberstien Group. He was Assistant to the President for Domestic Affairs from 1988 to 1989 and Deputy Assistant to the President from 1987 to 1988.

We think he will be a good CBO Director. He is not the director that Mr. Spratt or Mr. Lautenberg would have wanted, but this ultimately gets down to a decision that does get made by the majority even though this man has to operate not as a servant to the majority, and I think it is pretty clear that Dr. O'Neill—she didn't. [Laughter.]

So, anyway, we would just like to make a motion and get this approved. Mr. Spratt.

Mr. SPRATT. Mr. Lautenberg and I have met with Dr. Crippen twice. Dr. Crippen has assured us that he will maintain the independence and professionalism of the CBO and its professional staff.

We met with Dr. Crippen not because we doubted his competence but because he is in a sense cut from a different pattern than his predecessors in his position. His background and experience are more distinctly partisan than anybody who has ever held this position before.

Dr. Crippen has assured us that he will work with Democrats and Republicans alike on a nonpartisan basis, and, based on these assurances, I intend to support his selection.

Mr. Chairman, I would just like to say that it has been 25 years almost since Congress created the Congressional Budget Office. We created them to be neutral, nonpartisan, to give an independent, impartial estimate forecast. We haven't always agreed with their work, but I think we have respected their independence. They have earned the trust that they enjoy with most of us in Congress. And even if they haven't always been right, they have been basically honest and rigorous and professional in their work, and their virtues have served us well. The CBO has refused over the years to help us forecast the deficit away, and the discipline that they have held has helped us wipe out the budget deficit, and I simply hope and trust that Dr. Crippen will fight to maintain those independent goals.

Chairman KASICH. I would like to recognize Mr. Chambliss, the gentleman from Georgia, for purposes of offering the necessary unanimous consent request.

Mr. CHAMBLISS. Mr. Chairman, I ask unanimous consent that pursuant to section 201(a)(2) of the Congressional Budget Act of 1974, the Committee on the Budget recommends to the Speaker and the President pro tempore that Dr. Dan Crippen be appointed as the Director of the Congressional Budget Office.

Chairman KASICH. Without objection, so ordered.

I want to, first of all, thank Mr. Spratt, his staff, and the Democrats for the way in which we have been able to proceed through the rules package, and, frankly, we put something in the rule that I think will serve the Democrats—or I shouldn't say the Democrats—whoever would be in the minority for a period of time, and I think it will serve them well. It will make sure that there is adequate protection for the minority. In terms of Mr. Crippen, you can have a big fight over these kind of things, but they don't really serve us well. We are going to have enough to—hopefully, we won't have to fight, but we may have enough to fight about without having to look for one, and it is always nice to be able to have some bipartisan agreements as we proceed through some of these which I think are kind of formalities.

But let me welcome Jack Lew. I like that Jack's a guy who as Director of OMB he has made a heck of an accomplishment. I don't whether your mom—is your mom and dad still alive, Jack?

Mr. LEW. My mother.

Chairman KASICH. Your mom is? I mean, I don't know if she realizes that really through shear persistence and obviously talent Jack has been able to—it started with Leon isn't that right?

Mr. LEW. It started with Speaker O'Neill.

Chairman KASICH. Up here—well, OK, but then you got with Leon, isn't that right, and you became really his top assistant, and then when Mr. Panetta became the head of OMB, Jack went over and was involved in a lot of the negotiations, and the interesting story here is if you hang around long enough; if you have got talent and persistence, you can end up getting the top job. So, I think it is very exciting, and I am excited for you, and I hope your mom and your whole family—you know, a lot of times, they don't what the heck we are doing in this stuff, but I hope that sometime they will come to be able to truly realize what you have been able to accomplish being the Budget Director to the President of the United States. That is not bad, Jack; that is pretty darn good work.

So, I want to welcome you here this morning, and point out that 5 years ago few of us would have conceded to the opportunity to talk about surpluses, because when we were back in those days of trying to negotiate the budget agreement over there in the Capitol offices, we were struggling for literally every penny that we could get. You know, the famous phrase there "Brother, can you spare a dime?" because we didn't know how we could make this all add up to balance in 2002, and, low and behold, within a very short period of time, here we are with surpluses which is really wonderful news, because I think it gives us an opportunity to really leverage this good news into more good news. Last week, the CBO of course projected that we could have almost a $2.6 trillion surplus over the next 10 years. I suspect that maybe those numbers may even be low.

I mean a $2.6 trillion surplus, that is just amazing, and, frankly, I think it comes about for three reasons: one is I think that the benefits of the business community becoming a lot more efficient has allowed them to have higher levels of productivity without inflation, with minimal amounts of inflation, and, at the same time, I think it also reflects the fact that a trade-oriented export policy is very beneficial to a country, and, at the same time, it was just like yesterday when Dr. Greenspan was here and said that if you can put together a credible plan to balance the budget, the interest rates can come down two points, and if there is anything we have learned it is that interest rates are the driving engine of what happens with the economy; the lower they are, the better we do; the higher they are the worse we do. And as a result of the hard work that everybody did in 1995 and in 1996 and in 1997, we feel up here and working with the administration we were able to put together a plan that dropped those interest rates down and has given us the kind of economic growth that we would never have anticipated had any of us, Mr. Spratt or Jack or myself, been asked, "Is it possible that in 1999 we will be projecting a $2.6 trillion surplus?" We would have said, "There is something wrong with you."

CBO also tells us that lower projected Medicare spending will extend the life of the trust fund by possibly 3 years until 2010. We know we have a commission that is beginning to take a look at what we can do to extend it even further, but all this good news is the result in my judgment primarily of what we were able to do in 1997, and that meant at that point we had to work together.

Now, I think we face three or four new challenges: first, the coming retirement of the baby boomers who will put enormous strains on Social Security. We all know that the Social Security system is a matter of demography. We have a lot of baby boomers paying for our mothers and fathers; they are secure. The question is will the baby boomers and their children, us—will we be secure along with our children as the coming retirement approaches and the demographics start to work against us?

We all know we need to improve the quality of education in this country; that a trained workforce and smart kids are not only important to the economy but also, of course, those are the tools that give our kids a chance to grow up like Ed Markey did and become a Member of the United States Congress.

And we know we need to do these things while we have a growing economy that provides jobs and opportunities for everybody, and I think we all know that the number one issue before us is what can we do to make sure that the economy continues to grow, because if the economy continues to remain strong, the news continues to be good, and we can take the good news and leverage it for even more good news.

The President is looking at all these issues. Speaker Hastert has indicated that these issues are issues that Congress will be focusing on. We are looking forward in areas where we can get some things accomplished in a bipartisan fashion. Jack, I am interested in your USA accounts. As you know, I called for something along this line last year, and, in fact, I had suggested that we take the surplus and we begin to divide it up among all the people who paid payroll taxes, and I have with me today a passbook, and the passbook will be distributed to all the Members of the House to show them how much money they would have in a personal savings account that they would be able to direct like Federal employees and how that money could grow and what it can mean in terms of the concept of personal savings accounts. I happen to believe with Social Security people ought to have 2 percent of payroll in an account, and they ought to direct it, and I don't think we need any political appointees to tell us where that money ought to go. I think we can do it on our own, but until the day comes when we can get to the 2 percent or 3 percent of payroll, the notion that people ought to have these personal retirement accounts is one that I think is very positive. It would get Americans to understand the value of having personal retirement account and what that can do to enhance their retirement security. That is an area, Jack, maybe where we can reach some agreement in this year. I don't know, maybe we can do the whole deal, and we can get complete agreement, but, if not, it seems to me as though the retirement accounts are a good first step.

But I am disappointed, naturally, in some of the things that I found in the budget. Based on the count that we have made, this 5 year budget has about a $108 billion in new taxes and fees and over—this is pretty amazing—over $200 billion in new domestic spending; almost 40 new mandatory programs and almost 80 new discretionary programs. I don't know that Bob Clement would like all those new Federal programs. He would probably like to get a little bit more money back to Opryland, I don't know, but that is an awful lot of new spending, and the taxpayers will pay over the next 10 years about $22 trillion in taxes to the Federal Government. I think people are paying too much in taxes, and over here I believe that we will push and would like to see a very significant tax cut. I don't like the idea that we want to have governmental appointees investing our payroll taxes in the market. We believe that people ought to have the power to do that.

We also don't like the idea that we want to have control in Washington in terms of what we want to do with education, because we think that people will do better, our schools will do better, out children will do better if we can control education through our communities and our neighborhoods and our local school houses.

However, we are approaching the end of the century. We have certain obligations and responsibilities as we approach the new century, and all of our actions should be based on some fundamental principles. We need to have a commitment to each other based on our shared values. This will allow us to restore our society and our American family, and we must maintain a commitment to individual freedom. I believe we have to trust in and believe in the creative genius of individual citizens. I think if we do these two things, if we reach out to one another, we can have a great next millennium. And, so I am excited that you are here, Jack. Maybe there are some things we can do. Hopefully, as we go through the debate this year, even if we don't agree we can still be the friends that we have been over the years, and I now with great pleasure yield the podium to Mr. Spratt.

Mr. SPRATT. Thank you, Mr. Chairman. I want to join you in welcoming Jack Lew back to our committee. As you noted, he is no stranger to this committee or to the House. He spent a good piece of his career working for the Speaker of the House. He went to OMB with Panetta; he stayed over as the Deputy Director with Frank Raines, and now he has taken the reins from Frank Raines—if I can mix a metaphor—without any break in stride.

He has done a commendable job of carrying on, and today he comes to the Hill with a budget bound in black and white, the symbol of a new era. For the third year in a row, this budget is in surplus which is phenomenal. Mr. Chairman, that is a long way from 1992 when the deficit was $290 billion. In fact, if you look at the economic report President Bush sent over here in 1993, you will see that he projected a deficit this year over $300 billion if we had continued course. We didn't, so now we enjoy the fruits of our efforts. Because of the votes that we cast in 1990, 1993, and 1997, we have virtually wiped out the deficit in the unified budget, and we have come, as the President has expressed, to an historic juncture. The budget he is sending us rises to this occasion; it takes a high road into the next century. It commits the surpluses that we foresee coming to America's future. Sixty-two percent would go to make Social Security solvent for another 30 years; 15 percent would go to make Medicare solvent until 2020; 12 percent for an account, an idea that you yourself have proposed, Mr. Chairman, a Universal Savings Account so that every American can have a chance to save and invest and have a better retirement and so that we can increase the net national savings and boost the economy in the next century; and 11 percent, a modest 11 percent, would go to defense and nondefense priorities, because this budget, in addition to being a disciplined budget, also has some heart and soul. It has got some programs in here for education and community policing that we think work and that we think the American people want.

Before I conclude and turn the podium over to our witness, let me raise a word of caution. The surpluses that we foresee in the future stem from economists' predictions. If we have learned anything over the last 15 years, we have learned that economists sometimes make mistakes. Furthermore, the surplus they project this year, next year, and the following year, is a surplus in the unified budget. If we back out the surplus in the Social Security trust fund, there is, according to OMB, an on-budget deficit in 1999, in 00, and a mere surplus of $200 million in 2001. Not until 2002, 3 years from now, will both OMB and CBO see significant surpluses appearing. So, I think we should bear that in mind as we take up the budget and talk of bold tax cuts or big spending commitments, either one. The watch words should be caution and restraint. Let us not blow what we have accomplished. Thank you, Mr. Chairman, and thank you, Mr. Lew. We look forward to your testimony.

Chairman KASICH. I ask unanimous consent that all members who have opening statements, that those statements be permitted to be placed in the record. Without objection, so approved.

[The statement of Kenneth E. Bentsen, Jr., follows:]

PREPARED STATEMENT OF THE HONORABLE KENNETH E. BENTSEN, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. Chairman, I would like to take a minute to praise President Clinton for submitting another balanced budget—the third one in a row—and dedicating most of the projected budget surplus to strengthening Social Security and Medicare by paying down the national debt. Reducing the $3.7 trillion national debt should be our number one priority. We should pay down that debt while continuing the fiscal discipline Congress showed up until last year. As members of the Budget Committee, we should carefully review proposals for spending increases and tax cuts to ensure that they are fully paid for under Congressional budget rules.

Because of the strong economy and tough deficit reduction plans enacted in 1990, 1993, and 1997, the Federal budget will be in balance for 2 years in a row for the first time since 1957. The President has rightly proposed that we take advantage of this historic opportunity to buy down the huge national debt and strengthen Social Security and Medicare for the retirement of the Baby Boom generation.

As we know all too well, the Federal debt held by the public quadrupled between 1981 and 1993; interest payments on the debt doubled as a share of the Federal budget from seven to 15 percent.

Paying down the debt grows the economic pie and creates more wealth for all Americans. As this morning's Washington Post pointed out, there is a "shadow cost" to not paying down the debt. A tax cut or a spending increase, without offsetting spending cuts or tax increases, would add more debt, create future obligations, and create no assets new assets for the Trust Funds. A crushing Federal debt hinders gains in productivity, creates higher tax rates, and increases the cost of borrowing money. Unmanageable debt dampens economic growth.

In fact, a tax cut or large spending increase that resulted in more debt would most likely result in rising interest rates. There would be less money to invest, the debt's value would decline, and there would be a greater squeeze placed on the Federal budget to come up with funds to pay for Social Security and Medicare. This would also depress the value of the dollar, reducing its purchasing power and increasing inflation.

Finally, paying down debt will stop the government from eating up private savings. With less government bonds available for purchase, interest rates should decline and resources would shift to investments that are critical to improving productivity and raising our standard of living.

Public and private entities use debt to expand capital, but excessive debt squeezes out productive uses of resources. Paying down the debt is a less sexy but more efficient way of shoring up Social Security and Medicare. This alone will not solve the long term solvency issues of Social Security or Medicare, but it will certainly help.

The Administration's budget for the U.S. Army Corps of Engineers' Civil Works program calls for over $1 billion in new fees to be collected from our maritime industry through the a new proposal called the Harbor Services Fund (HSF).

1. Does the Administration anticipate shippers who typically utilize waterborne transport to move their products shifting to long-haul railroads in hopes ofoffsetting the increased transportation costs associated with the HSF?

2. The Port of Houston, which is located in my Congressional district, has a very large bulk commodities handling facility. Will the HSF have any negative impacts on our bulk cargo trade and in particular grain or coal?

3. What benefits does the Administration envision by abdicating its financial responsibility for dredging by including the entire Federal share of new construction projects under the HSF?

4. What studies has the Administration conducted regarding the possibility that international shippers may now try to divert their cargo through either Mexico or Canada to avoid the HSF?

5. Administrator Lew, Can you please describe for me the Clinton Administration's proposal to provide limited reimbursements for Medicare cancer clinical trials. As a the sponsor of legislation, H.R. 61, to ensure Medicare reimbursement for all types of clinical trials, I am very interested in learning more about your proposal.

6. Administrator Lew, As the representative for the Texas Medical Center, the largest medical center in the United States, I am very concerned about the Medicare reductions in the Fiscal Year 2000 budget. In a time when we are already asking our nation's hospitals to absorb more than $115 billion in Medicare reductions that were including the Balanced Budget Act of 1997, do you believe that these additional reductions are prudent and necessary?

[The statement of Bob Clement follows:]

PREPARED STATEMENT OF THE HONORABLE BOB CLEMENT, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TENNESSEE

Mr. Chairman, we have an historic opportunity. Instead of facing the $357 billion deficit that CBO projected in 1992, we are faced with our first surplus in three decades. The question we must now decide is what to do with it. Who should benefit from this suplus? Where do we put our priorities? Should we dedicate part of this surplus to a tax cut? If so, how much? Or should we conserve our resources to make sure that we can meet our future responsibilities to the American people?

I have asked my constituents where they think our priorities should be. Over and over again, they tell me that we in Congress should be working on paying down the national debt and on shoring up Social Security for the 21st century. This budget that the President has presented us allows us to do both. We can extend the life of the Social Security Trust Fund by 25 years and simultaneously lower the debt-to-GDP ratio from its current level of 44% to 7.1% by 2014, its lowest level since 1917. Some have suggested an across-the-board tax cut. I am not opposed to tax cuts. In fact, I have supported tax cuts and tax credits in the past. However, take a moment to remember what happened in the early 80's when we cut taxes but failed to cut spending. Our deficit ballooned to all-time highs. Is this the course we want to take? I think not.

I believe that the President's budget represents a strong framework for paying down the national debt and extending the life of the Social Security and Medicare Trust Funds. This budget is not a cure-all and it is not without its problems. There are still many tough decisions to be made in the future, but these reforms are an important first step.

Finally, I would like to commend the President for the courage and leadership he has shown in putting these proposals before us. We live in a nation that was built on ideas, and while we may not enact all of his proposals, the President has taken significant steps toward ensuring this country's continued prosperity.

[The statement of David E. Price follows:]

PREPARED STATEMENT OF THE HONORABLE DAVID E. PRICE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NORTH CAROLINA

*Proposed Analog Spectrum Fee*

I am concerned about a proposal in the President's budget to impose an "analog spectrum lease fee" of $200 million on television broadcasters. Television broadcasters already pay a number of Federal regulatory fees. In addition, there has always been an understanding among broadcasters that a "contract" exists between them and the Federal Government under which they provide statutorily required public service in exchange for use of the broadcast spectrum. What is the justification for this new fee, which according to the February 2, 1999 edition of USA Today could cost an average station $164,000 per year?

Is part of the justification for the fee to encourage stations to transition more quickly from analog to digital? Many of the smaller stations around the country already face a substantial financial challenge in meeting the deadline to convert to a digital signal. As the bigger stations convert more quickly to digital, will the smaller stations' share of the overall fee rise proportionately?

[The statement of George Radanovich follows:]

PREPARED STATEMENT OF THE HONORABLE GEORGE RADANOVICH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Mr. Chairman, thank you for scheduling this hearing today to allow us to review the President's FY 2000 budget. I am particularly concerned with issues relating to the Interior and natural resources. I would like for the administration to respond to the questions below. I appreciate the opportunity to submit this testimony.

*Lands Legacy Initiative*

Under this proposal, you envision converting this funding to mandatory next year. Why do you want to do this? Will it not have the effect of reducing congressional oversight?

Will not this proposal result in significantly increased maintenance costs and therefore add to your backlog?

National Park Service testified last year that its backlog alone was an estimated $6.1 billion in 1997, up from $1.9 billion in 1987. In light of this, what will be the impact of such significant land acquisition on eliminating or greatly reducing current backlog at agencies like the Park Service?

*PILT*

The Federal ownership of land is a huge drain on local resources, without comparable revenues as would occur with private ownership of land. One of the solutions is the PILT program. Why did you not increase Payments in Lieu of Taxes to the levels authorized under law in your budget?

*Cal-Fed Project*

Mr. Lew, how many agencies at Interior and across the government are involved in working on the California Bay Delta project? What is the total spending requested by the Administration this year what is last year's enacted level?

What are the expected future costs of water storage in the watershed?

Mr. COLLINS. Mr. Chairman.

Chairman KASICH. The gentleman from Georgia.

Mr. COLLINS. Mr. Chairman, I agree with Mr. Spratt that we have come along way since 1992, but I would like to amend that we have come along since January 1, 1995 too, sir.

Chairman KASICH. Well, we are off to a good start here. [Laughter.]

OK, I now recognize the gentleman—where are you from, Jack?

Mr. LEW. From New York.

Chairman KASICH. The gentleman from New York is now recognized. Do you think the Knicks, anybody on that team is going to pass this year?

Mr. LEW. I make predictions about the economy. I leave predictions about sports to others.

Chairman KASICH. All right, Jack, you have got the mike.

## STATEMENT OF JACOB J. LEW, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

Mr. LEW. Thank you, Mr. Chairman, Congressman Spratt. I appreciate the very gracious and generous introduction. Coming back to this committee is in a way coming home. I spent many years in this room. I look around at the pictures on the walls, and I can't imagine how many years have gone by, and I don't want to add them up.

If I might before going into my opening statement, make a comment on the first order of business, your vote on Dan Crippen as the head of the Congressional Budget Office. I have known Dan for the better part of 20 years. He was a very good and able adversary when I was in the Speaker's office and he was in the majority leader's office in the Senate. I look forward to working with him and congratulate him on his nomination today.

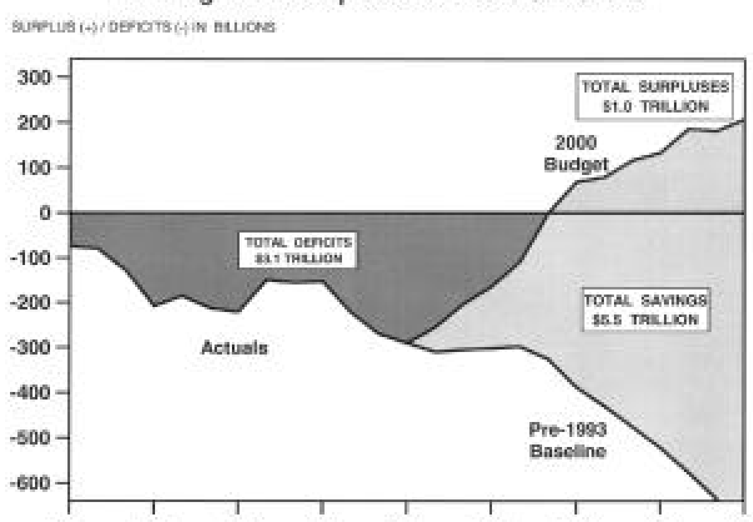
I also understand that today his deputy was named—and actually his deputy, Barry Anderson, most recently the most senior civil servant at OMB. He is first rate, and we miss him. We wish him and Dan well at CBO.

If I may, Mr. Chairman, I would like to submit for the record my formal statement and briefly summarize it in a few minutes. I would like to start, if I could, by taking a look at where we have come from and where we are going. This really is an historic opportunity, and I am proud to be here today to present the President's 2000 budget.

It is a document that is more than 1 year's budget. It really is a document that will shape the debate for the next decade as we go into the 21st century. The historic accomplishment of having a surplus of $117 billion in fiscal year 2000 and projecting $4.8 trillion in surpluses over the next 15 years is really remarkable.

When you remember where we started out in 1993 when President Clinton took office, we were looking at a sea of red ink. We were looking at deficits that would grow to $600 billion, $700 billion, $800 billion in a single year. There was a lot of fear in the country, and it was legitimate fear. The question was how could we run a deficit of $600 billion in a single year and meet all of our obligations and pay our bills? It took tough action in 1993 and, yes, in 1997 when we worked on a bipartisan basis to finish the job. The outlook for the next 15 years is very strong because of the tough decisions that we made.

**The Budget is in Surplus after Years of Deficits**



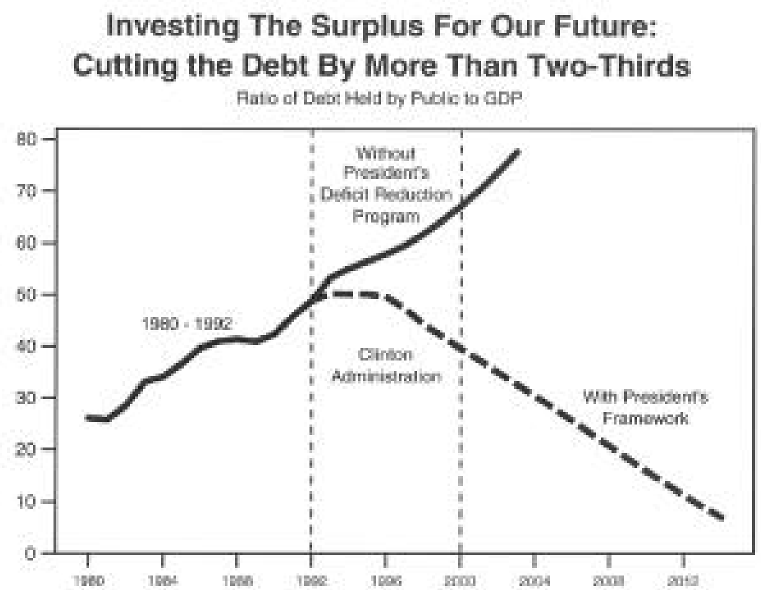
It is important to remember this history as we embark on the decisions that we have to make now. If we repeat the errors that we have sometimes made in the past, we won't have this kind of projection in the future. But if we continue the prudent decisions that we have made over the last several years, we really could lay a foundation for long-term economic growth.

Over this period it is important to note that the tax burden on American families has actually come down and not gone up. The success of balancing the budget has been by reducing the size of government. A typical family of four, a family that earns $55,000 a year, is now paying a lower share of its income in taxes than anytime in 23 years. A family of four with half the median income, roughly $27,000 a year, is paying the lowest share of income since 1965. Many, in fact most, are getting money back because of the earned income tax credit. Even a family of four with twice the median income, $110,000, is paying less than the combined income in payroll taxes than anytime since 1977.

And government has gotten smaller. Every year that President Clinton has been in office, every budget he has submitted, the government has taken less of the economy than in the preceding year, less of the economy than in either of the two preceding administrations, and that is no exception this year. The size of the government will fall from 19.7 to 19.4 percent of the economy.

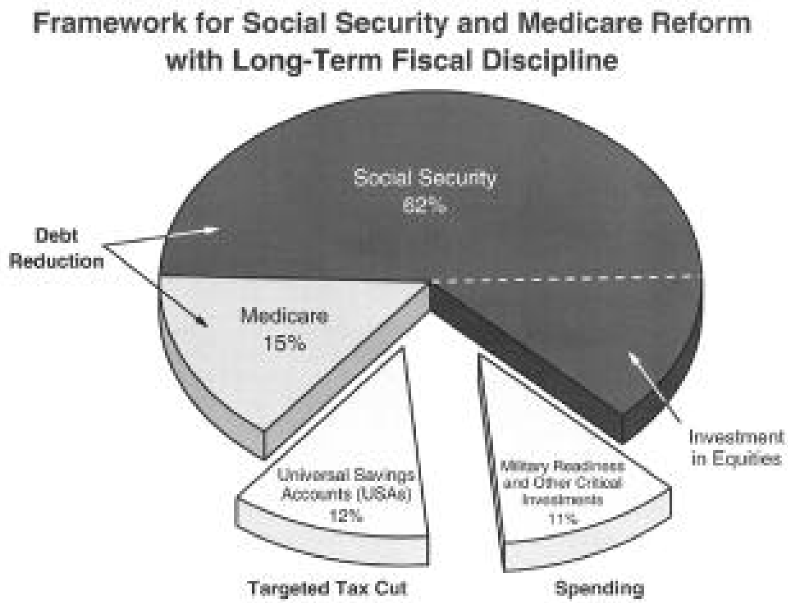
The key element of reducing government has been to reinvent government, and under the leadership of the Vice President, we have seen dramatic strides in having a smaller government that does more with less. The size of the Federal civilian workforce has declined by 365,000. As a percentage of the total workforce, the government is now the smallest it has been since 1931, and many of our agencies are doing a much better job serving their customers better than at any other point.

Before 1993, when we were looking at that red ink, the deficit was going to consume a larger and larger share of the economy. It was going to make it very difficult to have resources available for the Federal Government to do very many other things. What we have got now is the exact opposite with surpluses before us—and if I can change to the next chart, I think this tells the story of why.




This picture shows how the debt as a percentage of the economy will fall if the President's plan is adopted. When the President took office, the debt had climbed to 50 percent of the economy. Under the President's plan over the next 15 years, the debt held by the public will fall to 7 percent of the economy. This will bring the publicly held debt to the lowest percentage of the economy, 7 percent; the lowest it has been since 1917 before the United States entered World War I. The President proposes to do this with a framework for Social Security reform and long-term fiscal discipline.

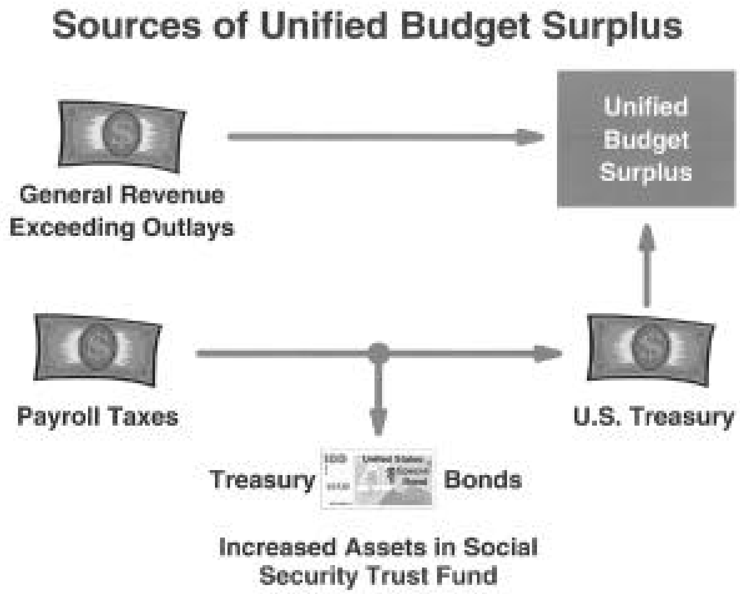
I want to begin by underscoring that the President's commitment last year and his commitment this year is fundamentally that we must save Social Security first. A statement of good intentions is not enough. We need to take action. The framework the President has put forward lays out a plan so that after we save Social Security, the next steps are clear.




And if you look at the green on this chart, the green shows both what the next step is and why that is a good step to take. After we have set aside 62 percent of the surplus for Social Security, the President has proposed that the next 15 percent of the surplus should go to Medicare. The reason it is green on that chart is that just as putting money into Social Security will reduce the debt, so will putting money into Medicare. And equally important, it will put the money aside to keep the promises that we have already made. The benefits are already due. It will put the money there to keep the promise to pay the benefits that are due in the next generation.

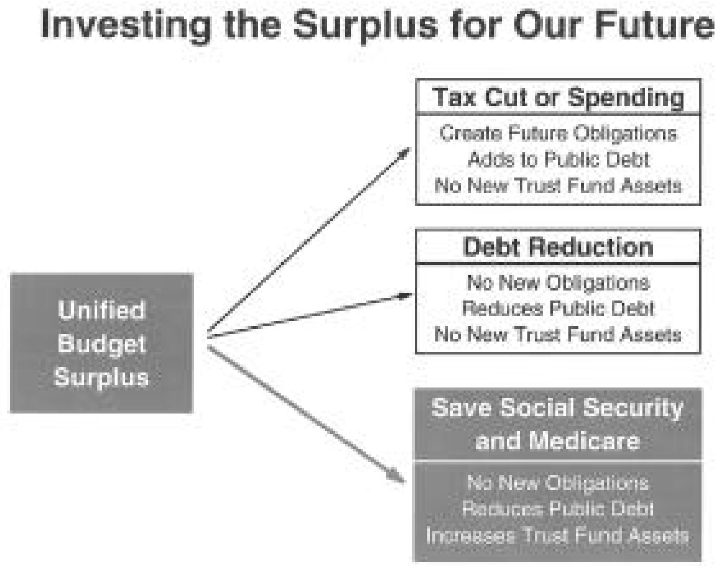
After we fix Social Security and Medicare, the President proposes a tax cut, and, as Chairman Kasich noted, it is the Universal Savings Account which I hope we can reach a bipartisan consensus on. Our view is that tax relief is appropriate, and it should be designed to encourage savings. It should be designed toward building retirement savings so that individuals can supplement Social Security and pensions with their own personal savings. After we have put 12 percent into the tax cut plan, the Universal Savings Account, the President has proposed that we put 11 percent of the surplus into discretionary spending to meet our national defense and urgent domestic priorities. I think there is a lot of bipartisan consensus on many of those priorities. I think we agree on a bipartisan basis that there is a need for more resources for national defense. I think we agree on a bipartisan basis that there is a need for more resources for education. If we are going to put more resources into defense and if we are going to put more resources into education, we are going to need to set aside some of the surplus to meet those commitments.

If we look at the next chart, I think it will help explain how the plan works.




A lot of questions have been raised about the accounting of the President's plan, and a lot of the complexity really relates to how we fund Social Security today and how we determine the unified budget surplus today. Right now, the unified surplus comes from two sources: every dollar that goes into the Federal Government in excess of expenditure for general revenue goes into the surplus. But just the same, payroll tax dollars in excess of benefits go into Treasury bonds, and they go into the Treasury as part of the surplus. The real question is not where the unified surplus comes from. The real question is what do we do with it?

Now, the President has proposed—and the next chart will make this clear—that we have three very real choices as to what to do with the unified surplus.




We could give the surplus back as either a tax cut or additional spending, but that will have three effects, and I don't think they are good: it will create new obligations for the Federal Government whether it is tax cuts or spending; it will add to the public debt; and it won't do a thing to extend the life of the Social Security or the Medicare trust fund.

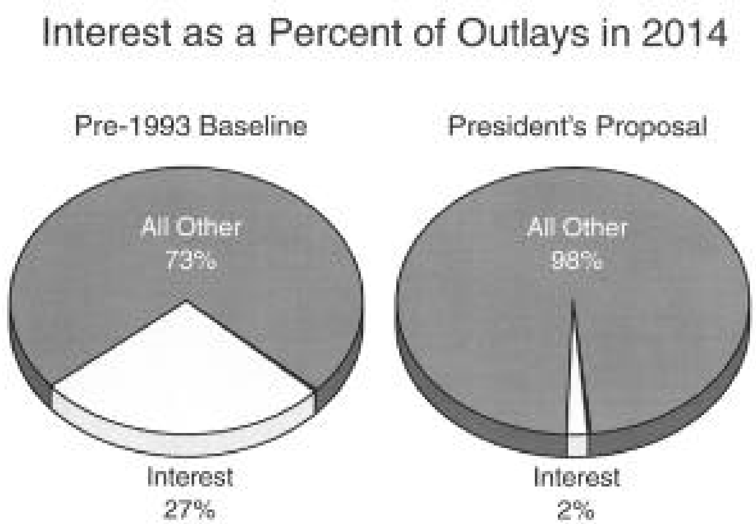
There has been a lot of debate in the last several weeks about debt reduction, and we applaud everyone who endorses debt reduction. We are for debt reduction. But it is important to note several things about debt reduction: it is good because there are no new obligations; it is good because it reduces the public debt. But on its own, it doesn't do anything to extend the life of the trust fund. And, perhaps, something that we need to consider equally importantly, debt reduction has never been a very popular political strategy. It has never been something that has rarely prevailed when compared to tax cuts or spending increases.

We have come up with a third option that we think is superior both in terms of its substantive detail and in terms of the likelihood of making the tough decisions and sticking to them. The President has proposed that we save Social Security and Medicare; we undertake no new obligations until we can pay for our old obligations; we reduce the public debt and get the benefits of a virtuous cycle instead of the vicious cycle that we have had for the last decade. We increase the trust fund assets, and put the money in the trust fund so that we can pay the benefits that people are now earning and that are due to them. We think that that is the best plan for using the surplus.

There has been a lot of discussion about the many initiatives in the budget, and we are very proud of them. We are proud of the initiatives that we have pursued over the last 6 years, and we think that they have made life better for the American people from Head Start to child care to education to the COPS Program. We have seen real effects in the investments we have made. We have a lower crime rate; we have a better set of health participants; we have better schools. We think that going forward we need to continue to make these investments, and, yes, we do need to make an additional investment in national defense. We need to make sure that going into the next century we continue to have the best fighting force in the world as we do today.

Overall, the President's fiscal year 2000 budget provides for important priority initiatives by achieving savings in programs. Everything in the 2000 budget is fully paid for. The President has not allocated a penny of the surplus for discretionary spending until 2001 to give us time to take action on Social Security reform and to take action on a broad plan to allocate the surplus. It complies fully with the current law spending caps, and it complies fully with the current law pay-go rules.

We have an historic opportunity for long-term prosperity if we rise to the occasion. By bringing down the deficit, balancing the budget, running the kinds of surpluses we are now projecting for the future, we have put our fiscal house in order. And if I might show you one more chart, I think it will show you—the benefits will be summarized very simply.




When the President took office in 1993, we were looking out to 2014—the 15th year of the plan that the President has put forward this year—and we were projecting that interest would consume 27 cents out of every dollar of the Federal budget. The current budget projects for the same year that interest will consume 2 cents out of every dollar in the Federal budget. Now, the difference is striking. The difference will give us the ability to pay our bills. It will give us the ability to pay Social Security, to pay Medicare, and, yes, to have some room for tax relief as the President has proposed.

What we must remember is that this didn't happen by accident. It happened because we took tough action in 1993 and 1997. We have fiscal discipline, and we have to maintain the fiscal discipline today in order to make sure that this projection becomes reality.

We look forward to working on a bipartisan basis, to going forward with a long-term policy of both fiscal discipline and investment in our future. We think that this is a once in a lifetime opportunity to for us to put down a marker for fiscal discipline and for economic prosperity for generations, and we look forward to meeting the challenges.

[The prepared statement of Jacob J. Lew follows:]

PREPARED STATEMENT OF JACOB J. LEW, DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

One year ago, President Clinton set the course of the Nation's budget policy with his charge to "Save Social Security First." The President recognized that we were entering a new era as we left behind the decades of large budget deficits. He was building the foundation for budgeting in this new era of surpluses.

*Fiscal progress has produced a strong economy*

The year 1998 was one of the most extraordinary in modern U.S. economic history. We enjoyed the first budget surplus in 29 years the largest ever in dollar terms, the largest as a percentage of the economy in more than 40 years. And this budget surplus was not the result of a temporary wartime policy, as was the last surplus in 1969. We will have a budget surplus again in the ongoing fiscal year at an estimated $79 billion, larger than last year's which will mark the first back-to-back surpluses in more than 40 years. The budget I present to you today proposes a third consecutive surplus the first time that will have happened in half a century. And our 1998 budget surplus was the sixth consecutive year of improvement in the U.S. fiscal position the first time that has happened in American history.

The private sector is the key to economic progress, but we have clearly seen in the decade immediately past that the Federal Government can either hinder or promote economic progress. If the Federal budget deficit is high, so that the cost of capital is driven up and the financial future is uncertain, the private sector cannot yield the progress of which it is otherwise capable. But if, instead, the Federal Government declares its intentions of responsible fiscal behavior, and lives by those intentions and if the Federal Government supplies the public investments that America needs then the economy is free to prosper. This is the path that this Administration has taken.

In 1998, we reaped the fruits of 5 years of fiscal responsibility. After the best sustained growth of business investment since the 1960's, the U.S. economy fueled that decades-absent budget surplus. And the economy itself defied the pundits, staying on a pace of solid, above-trend expansion, in the face of an international financial disruption that broke the stride of most other economies around the world. Unemployment and inflation both hit three-decade lows, with the lowest unemployment rates for African Americans and Hispanics in the history of those statistics; real wages continued to grow after more than a decade of stagnation, and a record percentage of adult Americans worked in those higher-paying jobs; the percentage of Americans on welfare fell to a 30-year low; the 10-year Treasury bond rate reached its lowest level in 30 years; and a higher percentage of Americans attained home ownership than at any time in our history.

The President deserves a great deal of credit for the virtuous economic cycle that we now enjoy. The announcement of a firm intention of fiscal responsibility in 1993 was greeted by a continued reduction of interest rates, which helped to trigger the investment boom that has proved central to sustained strong, non-inflationary economic growth. The two other pillars of the President's policy investing in our people and our technology, and opening foreign markets to U.S. exports complete this winning economic strategy.

*The 2000 Budget is a defining moment*

This extraordinary budget-and-economic performance with the budget setting historical standards and the resilience of the economy setting global standards tells us something. It tells us that we have developed a winning economic policy and that we must not turn back. We must not discard the economic philosophy that got us here, to this confluence of economic indicators that all sides now agree is the best in modern memory.

So in one sense, our budget policy now clearly should be built on continuity. We have achieved a sustained fiscal improvement, and we should continue to sustain that improvement. We have an economy that achieved a record sustained peacetime expansion, and we should continue to sustain that expansion.

But in another sense, we have stepped into a new world. Where our budget used to be written in red for so many years that people came to take it for granted now we are in the black. And this change has tempted some to throw away all of the policy principles that got us here.

For two decades now, there has been much discussion about fiscal discipline, restraint, and deficit reduction. Since 1993, we have taken action; and far beyond the expectations of even the most optimistic, we now have budget surpluses as far as the eye can see. But now, as the first surpluses appear, it is important that we not revert to the practice of cutting taxes and raising spending first, and thinking about the fiscal consequences later.

As the President suggested in his State of the Union address 2 weeks ago, this is a moment that will do much to determine the character of our country at the end of the next century. We can build and strengthen the fiscal foundation that first arose in these last few years. Or we can sweep it away, before it is firm and strong, and set our economy to foundering again. The choice is clear and the President is determined to pursue a balanced program of fiscal discipline and prudent investment for the future. This budget charts that course into an era of surplus.

*Fiscal policy since 1993 was pivotal to our current good fortune*

To see why fiscal responsibility matters, consider where this Administration started 6 years ago. In 1992, the budget deficit was $290 billion, the largest in the Nation's history. Between 1980 and 1992, the debt held by the public, the sum of all past unified budget deficits, quadrupled; it doubled as a share of our Nation's production, or GDP from about 25 percent to about 50 percent.

These adverse trends showed every sign of accelerating. Both CBO and OMB projected that, without changes of budget policy, growing deficits would add to the Nation's debt, and growing debt service costs would add, in turn, to the Nation's deficits. OMB forecast the 1998 deficit, in the absence of policy change, at $390 billion, or 5.0 percent of GDP; by 2003, we expected the deficit to be $639 billion, or 6.6 percent of GDP. And there was nothing in the forecast to indicate that this exponential trend would stop.

This threat was not turned back by accident. It required tough policy choices, which the Administration and the Congress took in 1993 and 1997. The President's initial economic program cut spending and increased revenues in equal amounts. Since that time, deficit reduction (and ultimately surplus increase) has more than doubled the estimates for the President's plan instead of the projected cumulative $505 billion, deficits have fallen by $1.2 trillion. That is $1.2 trillion less in debt that the American taxpayer must service forever.

And this deficit reduction has come as much from lower spending as from higher revenues. Spending has declined to its smallest share of the GDP in a quarter of a century. And thanks to the strong economy, receipts have grown beyond expectations, even though the tax burden on individual families is lower than it has been for about a quarter century:

The typical family of four with the median family income of $54,900 will pay a lower share of its income in income and payroll taxes this year than at any time in 23 years. Its income tax payment considered alone will be the lowest share of income since 1966.

A family with an income at one-half of the median level, $27,450, will pay the lowest share of its income in income and payroll taxes since 1965. Its income tax bill will be negative; it will receive money back because of the earned income tax credit. That was never the case before 1998.

Even a family at twice the median income level, $109,800, will pay less in combined income and payroll taxes as a share of its income than in any year since 1977. Taken alone, its income tax as a percentage of income will be the lowest since 1973.

Receipts have risen as a percentage of GDP not because of a heavier tax burden on typical individual families, but rather because of the extraordinary growth of incomes of comparatively affluent Americans (including capital gains and stock options that are not included in measured GDP); and because of the rapid growth of corporate profits.

The historic bipartisan balanced budget agreement of 1997 has reinforced expectations of Federal fiscal responsibility. This has had a favorable effect on interest rates, and the economy at large.

In the last 6 years, we have enjoyed an extraordinary economic performance because our fiscal policy was responsible and sound. If we want to continue to enjoy such strong economic performance, we must continue our sound fiscal policy. As the experience of the last 20 years clearly shows, budget problems are very easy to begin, and very hard to end.

Reducing debt burden is as important to the Nation as it would be to a family. The Nation must service its debt. If we gratify ourselves today by collecting taxes insufficient to cover our spending, and accumulate debt, our children and our grandchildren will have to service that debt. If, instead, we reduce our debt, our children and our grandchildren will be freed of the obligation to tax themselves more heavily in the future just to pay the interest on the debt they inherited.

The President's proposal will fully reverse the buildup of debt of the 1980's and then go further. By 2014, the end of the 15-year horizon of the President's program, the combined effects of the President's commitments to Social Security and Medicare will reduce the Nation's debt burden to an estimated 7 percent of GDP. This will be the lowest ratio of debt to income that the Nation has enjoyed since before it entered World War I. And as most experts would tell us, this will be one of the greatest gifts that we could ever give our children, as we exercise our fiscal stewardship of these United States.

The President's policy would devote more than three-fourths of future budget surpluses to reducing the Nation's debt through contributions to Social Security and Medicare; and would dedicate another 12 percent to household savings through Universal Savings Accounts. This is important to our economic performance for four basic reasons: First, it increases the Nation's savings rate, which is critical to productivity gains and economic growth. Second, it reduces the debt. Third, it improves the fiscal position of the country, and puts it on a stronger footing for whatever uncertainties might arise. And finally, it improves the retirement security of all Americans.

*The current challenge is to use the surplus prudently*

In 1993, we faced the challenge of eliminating projected budget deficits of $4.3 trillion over 10 years. Today we face the enormous opportunity of projected surpluses of more than $4.8 trillion over the next 15 years. The challenge is to use this surplus prudently to maintain our strong economic and budgetary performance.

We must save Social Security first. A statement of good intentions is not good enough for the millions of Americans, retired and working today, who rely on Social Security for their retirement security and for protection for their families against disability and premature death. From the beginning, this Administration has kept its eyes on the future, and taken policies that would benefit the Nation for generations to come. It has paid off. Saving Social Security first is precisely such a future-oriented policy.

The President's FY 2000 budget symbolically, as well as financially, "in the black" continues firmly on that successful path. The budget maps a course for the Federal Government after Social Security is reformed and makes its own policy recommendations for the beginning of the bipartisan Social Security reform process that the President inaugurated last year. But the budget also draws a line that this Administration will not pass without Social Security reform.

Thus, the FY 2000 budget is fully paid for within the existing budget law. Just as in every previous year, the President has specified his own priority initiatives, but has paid for all of them line by line, dime by dime with savings from elsewhere in the budget.

The President's policy calls for a bipartisan Social Security reform, this year. The President has already committed 62 percent of our projected budget surpluses enough to extend Social Security's solvency almost an extra quarter century, to 2055. We hope that this will launch a bipartisan process to address long-term Social Security solvency. We are gratified that several leaders from the Congress have already accepted this principle and hope that both parties, the President and the Congress, can follow through on this commitment and achieve sufficient additional reforms to extend the solvency of the trust fund at least through the traditional 75-year actuarial horizon.

If we achieve that objective, the budget makes further commitments of the surplus to priority National objectives in the future. The President proposes to dedicate 15 percent of the surplus to extending the solvency of the Medicare trust fund. This is a key element of the President's program, because the financial security of Medicare will be threatened even sooner than that of Social Security. In 1997, the President and the Congress, acting together, made Medicare financially sound through 2010. The President's 2000 budget would extend that lifetime 10 years further, to 2020. We see the commitment of the surplus as a vital step to facilitate an environment in which a bipartisan effort including the current Medicare Commission can go even farther; with the time horizon so short, even after the contribution of 15 percent of the surplus, we cannot delay Medicare reform. As the President stated, he wants to consider, as a part of this reform process, expanding Medicare coverage to include prescription drugs.

The President also proposes using 12 percent of the surplus to finance his new Universal Savings Accounts "USAs." This proposal includes seed money for Federal contributions, plus additional funds for matching contributions if individual workers contribute their own money. The matching contributions will provide a larger percentage inducement for low-wage workers. The goal is for all Americans to see the rewards of saving building up in these USAs and with this introduction to the power of compound interest, to begin to save further on their own. The President believes that this program, with its Government seed contribution, has the potential to reach even those who have failed to respond to the generous subsidies in the current-law Individual Retirement Accounts (IRAs).

The President wants a fiscally responsible tax cut. He believes that the USA is the right kind of tax cut targeted toward the future, and helping the many American families who have the most difficulty saving for their retirement. It strengthens perhaps the most neglected of the figurative three legs of the retirement stool personal saving, to stand alongside Social Security and employer pension plans—and for the many who have no employer plan, this initiative may be crucial. Most importantly, it is part of a plan that fixes Social Security first.

Finally, the budget proposes that the remaining 11 percent of the surplus be dedicated to other important priorities including education, National security, and health care. In last October's negotiations on the Omnibus appropriations for fiscal year 1999, Congressional leaders argued that our National defense needs had outgrown the existing discretionary spending caps and, indeed, defense received the largest share of the additional emergency funds made available in that legislation. Likewise, the American people have recognized that the quality of their children's education will determine how they progress in life and also the strength of the future economy. The President's budget is a sound, disciplined way to provide the additional resources for these priorities that both sides recognize will be needed if our country is to survive and prosper in the next century.

*The President's framework for Social Security reform and long-term fiscal discipline works*

The President's contribution of the surplus to Social Security will use many of the existing financial management tools of the Federal Government. It will be in addition to the accumulation in the Social Security trust fund that would occur with no change in the current law.

After the trust fund is credited for all of its own receipts, exactly as in current law, the Treasury will be left with the unified budget surplus. Each dollar of that unified surplus can be used only once for cutting taxes, increasing spending, or buying down the debt. The President has brought the debate right to the point: What should we do with that surplus? Or to put it another way: If we were to look back fifteen years from now, or at the end of the next century what would we want to be able to say that we had accomplished with this opportunity? The President wants to leave a legacy of building for the future: saving Social Security and Medicare; encouraging Americans to save for their own futures, build wealth, and prepare for retirement; investing in education; ensuring our National security; and making other key investments.

So the President started by committing 62 percent of the surplus to save Social Security first. Most of the share committed by the President to Social Security will be used to buy down the publicly held Federal debt through the periodic debt refundings of the Treasury Department, in exactly the same way as debt was retired last year. That same amount will be credited to the Social Security Trust Fund, in the form of Treasury securities. This same procedure will be followed for the President's contribution to the Medicare trust fund.

This commitment will significantly extend Social Security solvency. At the end of 1999, the currently estimated combined balances of the OASDI trust funds is about $850 billion. Through 2014, we estimate that additional contributions to the trust funds under the current law, including interest, will total about $2.7 trillion, leaving a total balance of about $3.5 trillion. The President's program would contribute an additional $2.8 trillion to the trust funds over the next 15 years. Taking into account additional interest earnings, that would leave a balance in the trust funds of more than $7 trillion instead of the approximately $3.5 trillion under the current law. The President's program will more than double the balances in the trust funds over the next 15 years—without accounting for higher earnings on the portion of the surplus invested in corporate equities.

Because the President's plan will reduce the public debt, the total obligations of the Federal Government will not increase. We are already committed to paying benefits beyond 2032, when the trust fund is now expected to be exhausted. The President's proposal would deposit assets in the Social Security trust fund to pay these obligations, and reduce by an equal amount the debt borrowed from the public. Interest payments will go to the trust fund, to cover future Social Security benefits, rather than to banks, individuals and other investors in Government bonds.

A small portion of the President's commitment to Social Security (21 percent of the commitment) will take the form of holdings of corporate stock. Because the Social Security trust fund will need that amount of the cash surplus to purchase the shares, this contribution will not reduce the public debt. However, it will improve the Federal Government's implicit balance sheet to the same degree, but in a different way. While the reduction of debt will reduce the Federal Government's liabilities, the corporate shares will increase the Federal Government's assets. The salutary effect on the Government's balance sheet will be the same, but it will appear on the other side of the balance sheet.

Thus, the President's policy in no way increases the total obligations of the Federal Government. In fact, by retiring part of the public debt, it strengthens our economy in exactly the same way that reducing the budget deficit, and avoiding the accumulation of debt, has helped the economy over the last 6 years. The President's program does shift the Federal Government's commitments to Social Security, however, and in that way improves Social Security's solvency for the next century. This will give Social Security a first call on the economic benefits associated with long-term reductions in publicly held debt.

The President believes that budgeting in an era of surpluses requires a focus firmly on the future. We must put money aside against our current obligations before we incur any new obligations. The President's program does that, by retiring debt and accumulating assets against the Social Security commitments that we already have.

*We must balance fiscal discipline with prudent investments for the future*

In addressing these priorities, the FY 2000 budget builds upon the investments in our people and our technology that were set in motion by past budgets.

Last year's budget implemented the Balanced Budget Act of 1997, maintained fiscal discipline reserving the surplus until we save Social Security first and provided a strategy of targeted investments to help sustain economic growth. For example, last year's budget provided resources for:

The first year's investment to reduce class size by hiring 100,000 new teachers. Smaller classes ensure that students receive more individual attention, a solid foundation in the basics, and greater discipline in the classroom. In this year's budget, the President proposes investments in this area, ultimately to reduce class size in the early grades to a national average of 18.

Investments to protect our economic interests at home by responding to international economies in turmoil. The disruption in financial markets last year lead to economic dislocation in Asia, Latin America and the Soviet Union. This, in turn, hurt American exporters, farmers and ranchers, who found that markets overseas were beginning to dry up. With President Clinton's leadership, Congress approved nearly $18 billion for the International Monetary Fund, a stabilizing force in the world economy.

A guaranteed, record-level investment for the next 5 years in the Transportation Equity Act for the 21st Century to continue rebuilding America's highways and transit systems, which are essential to continue the growth of modern commerce. This legislation also funds programs for highway safety, transit and other surface transportation, while safeguarding air quality, and helping former welfare recipients get to their jobs.

Over the past 6 years, the President also worked with the Congress to establish and build upon significant investments in education and training, the environment, law enforcement and other priorities to help raise the standard of living and quality of life for average Americans both now and in the future. For example, the President's commitment to fund key domestic investments has:

Advanced cutting-edge research, putting the National Institutes of Health on a path to doubled funding for research including intensified work on diabetes, cancer, genetic medicine, and the development of an AIDS vaccine.

Established the children's health care initiative, the largest investment in health care for kids since Medicaid was created. Last year, 47 states began programs designed to provide meaningful benefits to as many as five million uninsured children.

Increased Head Start's ability to provide greater opportunities for disadvantaged children to participate in a program which prepares them for grade school. Last year, a boost in Head Start funding put 835,000 children into the program, making further progress toward the President's goal of putting a million children in Head Start by 2002.

Invested in public schools to help States and communities raise academic standards, strengthen accountability, connect classrooms and schools to the information superhighway, and promote public school choice by opening 900 charter schools.

Protected and restored some of the Nation's most treasured lands, such as Yellowstone National Park, and the Everglades; provided the funds to conserve others; and accelerated toxic waste clean-ups.

Built the COPS program to support community policing. This year COPS will reach the goal of putting 100,000 more police on the streets of America's communities. COPS has helped reduce violent crime for six straight years. The 21st Century Policing Initiative proposed in this budget will expand on the number of police and provide other law enforcement tools to the community.

This year's budget builds on the President's efforts to invest in the skills of the American people. It continues his policy of helping working families with their basic needs raising their children, sending them to college, and expanding access to health care. It also invests in education and training, the environment, science and technology, law enforcement and other priorities, to help raise the standard of living and quality of life of Americans.

Families and Children: For 6 years, the President has sought to help working families balance the demands of work and family. In this year's budget he proposes a major effort to make child care more affordable, accessible and safe by expanding tax credits for middle-income families, and for businesses to expand their child care resources; by assisting parents who want to attend college meet their child care needs; and by increasing funds with which the Child Care and Development Block Grant can help more poor and near poor children. The budget proposes an Early Learning Fund, which would provide grants to communities for activities that improve early childhood education and the quality of childcare for those under age five.

Education: The President has worked to enhance access to, and the quality of, education and training. The budget takes the next steps by continuing to help States and school districts reduce class size by recruiting and preparing thousands more teachers and building thousands more new classrooms. The President proposes improving school accountability by funding monetary awards to the highest performing schools that serve low-income students, providing resources to States to help them identify and change the least successful schools, and ending social promotion by funding additional education hours through programs like the 21st Century Learning Centers. The budget also proposes further increases in the maximum Pell Grant to help low-income undergraduates complete their college education, and more funding for universal reemployment services to help train or find jobs for all dislocated workers who need help.

Environment: This Administration proposes a historic interagency Lands Legacy initiative to both preserve the Nation's Great Places, and advance preservation of open spaces in every community. This initiative will help address sprawl and air and water pollution, through land acquisition, preservation efforts, environmental protection and local growth management. The Administration also proposes a new financing mechanism, Better America Bonds, to further creation of open spaces in urban and suburban areas. The Better America Bonds initiative is an example of our use of targeted, paid-for tax cuts to achieve the Nation's priority goals. In addition, the budget would restore and rehabilitate national parks, forests, and public lands and facilities; expand efforts to restore and protect the water quality of rivers and lakes; continue efforts to double the pace of Superfund clean-ups; and better protect endangered species.

Defense: The President is committed to maintaining world military leadership to provide for the safety of American citizens and the primacy of American Armed Forces. To ensure America's Armed Forces are fully prepared to meet the challenges of the next century, the President proposes a long-term, sustained increase in defense spending to enhance military readiness, improve recruitment and retention, and provide the most modern and effective weapons. In addition, these resources will reinforce the ability of the Defense Department to counter emerging threats such as terrorism, reduce threats from weapons of mass destruction, maintain the nation's nuclear deterrent, and provide humanitarian and disaster assistance.

Health Care: The President has worked hard to expand health care coverage and improve the Nation's health. The budget gives new insurance options to hundreds of thousands of Americans aged 55 to 65, and it advocates bipartisan national legislation that would reduce tobacco use among the young. The President's budget proposes initiatives to help patients, families and care givers cope with the burdens of long-term care; and it helps reduce barriers to employment for individuals with disabilities. The budget also enables more Medicare recipients to receive promising cancer treatments by participating more easily in clinical trials. And it improves the fiscal soundness of Medicare and Medicaid through new management proposals, including programs to combat waste, fraud and abuse.

Embassy Security: The bombings of U.S. embassies in Kenya and Tanzania highlight the dangers faced daily by Americans who work in U.S. facilities abroad. The budget proposes an increase to the State Department's operating budget to ensure protection of embassies and other facilities, and the valuable employees who work there. The budget also includes a request for $3 billion in advance appropriations for a multi-year security construction program.

*The 2000 Budget saves the surplus until we fix Social Security first*

The President's FY 2000 budget is fully paid for, in compliance with the discretionary caps and the pay-as-you-go budget rules. The budget allows for appropriations for important domestic and national security priorities by limiting other discretionary spending and achieving mandatory savings. Offsets to discretionary spending include the President's tobacco policy (which would reimburse the Federal Government for tobacco-related discretionary health care costs), FAA user fees, health care savings, Superfund receipts, student loan savings and the recall of additional Federal fund reserves at lending guaranty agencies, and reform of the existing harbor maintenance excise tax. With the use of these offsets, in keeping with longstanding budget practice, the 2000 budget complies with the discretionary spending caps.

The budget provides targeted tax reductions, financed by the elimination of tax loopholes, and inefficient or obsolete tax subsidies. Important tax cuts and incentives, in addition to the President's USA retirement savings program, include the tax credit for long-term care needs, the public school construction and modernization bonds, the expansion of the child and dependent care tax credit, the new Better America Bonds, extension of the R&E tax credit, the work opportunity tax credit, the welfare-to-work tax credit, and the tax incentives for reductions of carbon emissions that cause global warming. Important mandatory initiatives include child care, the Medicare buy-in, disability and cancer clinical trials programs, and extension of health-care programs to immigrants. Taking all of these policy steps together, the budget complies with the pay-as-you-go rules, and the tax cuts and mandatory initiatives are fully paid for.

*We need adequate resources for a strong defense and critical domestic priorities*

For future years, the budget includes the discretionary resources contemplated as a part of the plan for Social Security reform. While these funds will only be available if Social Security reform is enacted, the Administration's policy is categorically defined including those resources. Social Security reform is one of the President's highest priorities for this year and we must work on a bipartisan basis to accomplish this important goal. The comprehensive framework for allocating the surplus will also provide these critical discretionary resources.

The President believes that his discretionary priorities are important to economic growth, and to the Nation's well being and quality of life. Some have disagreed, and have argued that Federal spending in general is too high. This debate requires some perspective.

First, and perhaps most fundamentally, consider the record. Over the years 1980-98, Federal spending averaged 21.9 percent of GDP. But Federal receipts averaged only 18.5 percent of GDP. Thus, the Federal budget averaged a deficit of about 3.4 percent of GDP. When this Administration set out to cut the budget deficit that we inherited, our original plan called for roughly equal spending cuts and revenue increases (with spending cuts in fact slightly larger). While the results of this plan have been far beyond what we ourselves anticipated with the deficit falling by more than twice as much as our original estimates they did maintain the balance between spending cuts and revenue increases.

In balancing the budget, this Administration has controlled Federal spending well beyond the record of its predecessors. As a percentage of GDP, spending in every year for which President Clinton submitted a budget has been lower than in any year of the two preceding Administrations. In every budget year from 1994 through

1998, Federal spending as a percentage of GDP fell. Spending as a percentage of GDP in 1998, at 19.7 percent, was the lowest in almost a quarter century.

Some argue that "Federal spending is still going up." In the simplest terms—total dollars with no discounting for inflation, no allowance for the growth of the economy, and no allowance for the growth of the population government serves—that is true. But even in this format, the analysis tells a great deal about the record of Federal spending under this Administration.

From 1993 through 1998, 31 percent of the simple dollar increase in Federal outlays came because more elderly people retired on Social Security benefits, and prior retirees received cost-of-living increases; 26 percent arose because of additional beneficiaries and higher costs under Medicare; 18 percent arose because, even with a rapidly declining budget deficit and by 1998, a budget surplus there was more debt to service, and so net interest costs went up; and 10 percent came from increased costs under Medicaid, more than two-thirds of which went for the expenses of the indigent elderly, blind, disabled, and mentally retarded, many of those in long-term care.

Thus, there has been almost no spending growth in programs other than Social Security, Medicare, Medicaid, and net interest. Spending of the entire remainder of the Federal Government over 1993 to 1998 shrank by 5.4 percent in inflation-adjusted dollars, and fell from 11.5 percent to 8.8 percent of the Nation's GDP.

This shrinking of core government operations cannot go on forever if government is to accomplish the missions assigned to it. We all take for granted the obligation to maintain critical core functions like the FAA, the FBI, and the administration of Medicare. As we consider how to budget in this era of surpluses, we must consider carefully the resources available for these 1often-anonymous functions that the Nation has a right to expect its government to perform well.

A key element in the Administration's ability to expand strategic investments, while balancing the budget, is the reinvention of government doing more with less. Efforts led by Vice President Gore's National Partnership for Reinvention have streamlined government, reduced its workforce, and focused on performance to improve operations and delivery of service. And these efforts, by reducing the cost of government operations, have improved the bottom line and contributed to our strong economy.

Since 1993, the Administration, working with Congress, has evaluated and eliminated hundreds of unnecessary programs and projects. The Administration has cut the size of the Federal civilian work force by more than 365,000 people, creating the smallest work force in 35 years and, as a share of total civilian employment, the smallest since 1931.

The Administration, however, is working to create not just a smaller Government, but a better one a Government that best provides services and benefits to its ultimate customers, the American people. It has not just cut the Federal work force, it has streamlined layers of bureaucracy. It has not just reorganized headquarters and field offices, it has ensured that those closest to the customers can best serve them.

For 2000, this Administration once again is turning its efforts to the next stage of "reinventing" the Federal Government. It plans to dramatically overhaul 32 Federal agencies to improve performance in key services, such as expediting student loan processing and speeding aid to disaster victims. It also plans to tackle critical challenges, such as ensuring that Government computers can process the year 2000 date change, and making more Government services available electronically.

Under the 1993 Government Performance and Results Act, Cabinet departments and agencies have prepared individual performance plans that they will send to Congress with the performance goals they plan to meet in 2000. These plans provided the basis for the second Government-wide Performance Plan which is contained in this year's Budget. For the first time in 2000, agencies will submit to the President and Congress annual reports for 1999 that compare actual and target performance levels and explain any difference between them.

*We have an historic opportunity for long-term prosperity if we rise to the moment*

There is much to be proud of in America today. By balancing the budget, we have not just put our fiscal house in order; we have left behind an era in which the budget deficit, as the President said recently, "came to symbolize what was amiss with the way we were dealing with changes in the world." Today we have risen to the challenge of change by preparing our people through education and training to compete in the global economy, by funding the research that will lead to the technological tools of the next generation, by helping working parents balance the twin demands of work and family, and by providing investment to our distressed communities to bridge the opportunity gap.

If the deficit once loomed over us as a symbol of what was wrong, our balanced budget is proof that we can set things right. Not only do we have well-deserved confidence, we have hard-earned resources with which to enter the next century.

As the President said, what we do now after having balanced the budget will shape the character of the next century. We can build upon our newfound firm economic foundation; or we can squander it.

The President has brought the debate right to the point: What should we do with the surplus? Or to put it another way: If we were to look back fifteen years from now, or at the end of the next century what would we want to be able to say that we had accomplished with this opportunity?

The President wants to leave a legacy of building for the future: saving Social Security and Medicare; encouraging Americans to save for their own futures, build wealth, and prepare for retirement; investing in education; ensuring our National security; and making other key investments.

There is no more pressing issue facing us as a nation than the need to guarantee that Social Security will be there for generations to come. And there is no better time to act than now while the system is still strong. This is truly an exceptional moment in America the economy is prosperous, the budget is in balance, and the President's commitment to national dialogue has created conditions for constructive action. We must seize this moment.

Chairman KASICH. Mr. Lew, let me—thank you for your testimony—let me just get in just two quick areas because there are members that have questions, and I don't want to—I had a chance to make a long opening statement. Alan Greenspan, when he was asked about the board that you want to create investing in the markets—first of all, the notion that we can use the capital markets to be able to solve a large portion of the problem for the baby boomers, I believe is right on target. The question is, of course, who gets to control it? Do we have a board of smart people or do we just let—you know, we call smart people—I know I could never get appointed to a board like that—or do we let individuals be able to manage their own retirement? I tend to think, Jack, that as much as I like you that you worry about your retirement a lot more than I worry about your retirement, number one, and so I think you ought to have the maximum control to invest your payroll taxes rather than I getting on a board and investing your money for your retirement, because I think you care about it more than I do. It is kind of like what Federal employees get to do. We don't have any smart persons board that invests the Federal employees' money; we invest it ourselves, and I think everyday Americans are just as smart as Federal employees when it comes to planning for their own retirement. But Greenspan said in the notion of having a political board investing in the market, he said, "Even with Herculean efforts, right, I doubt it would be feasible to insulate over the long run the trust funds from political pressures, direct and indirect to allocate capital to less than its most productive use." In other words, this board would be subjected to political pressures, and so somebody would be making—some board would be making a political decision about our retirement when we don't get the return we ought to get because they are considering political pressures of political concerns. Wayne Angel, Bear-Stearns, warned that the proposal "enlarges the role of government dictating to the private economy to a degree that many of us would find unacceptable."

Jack, what is wrong with the notion that individuals, you and me, should have control over our payroll taxes to be able to direct those payroll taxes into investment opportunities that provides for our retirement? Why do we need to give this opportunity to some board who get appointed by a President? What is the thinking there?

Mr. LEW. Mr. Chairman, I hope we agree more than we disagree, and we begin with the notion that Social Security is the foundation for retirement and that individuals should be guaranteed benefits as they are today. They shouldn't be subject to the risks that if market were to somehow fall the day they retire that they would be penalized for the rest of their retirement, but there should be that foundation where we have a shared societal——

Chairman KASICH. Everybody agrees on that.

Mr. LEW [continuing]. Everyone agrees on that. We think that investing the Social Security fund to a very modest extent in equities is a good idea. We think it gives the Social Security fund the upside potential that all private pension plans and State and local government pension plans have today. What we have suggested—and we took very seriously the considerations that Chairman Greenspan discussed with you—is that it be a truly independent board that is insulated from political pressure.

We suggested that it should not be picking and choosing. We do not want any branch of government picking and choosing what equities to invest in. We want to have a broad market basket of investments with a little bit of everything, where there is an independent board, private managers, the same people who manage money market funds, putting these assets into literally the entire stock market. That means that we will not be picking and choosing; we won't be making the kinds of markets decisions that we agree the government should not make.

The risk that Chairman Greenspan has pointed out is one that I think we do have to take seriously. The plan we have put forward we believe meets the criteria that he set out. The question is would we stick to our guns 5 years, 10 years, 15 years from now to resist the temptation to change the plan? I have confidence that the same way we have left the Federal Reserve Board as independent as it is because that is the right thing to do, we would leave this independent board independent for its entire life. That would be the right thing to do, and that is what we are proposing.

As far as individual choice goes, the Universal Savings Accounts give individuals the ability to make decisions on their own retirement. We wouldn't be telling individuals how to invest that money. They would have choices. We need to work through the administrative detail, because there is a little bit of a tradeoff. Total free choice has very high administrative costs. In our Federal retirement plan, we have modified choice. We have limited options that dramatically reduce the administrative costs. What we hope to work through as we work on the Universal Savings Account is a way to give individuals choice with the lowest possible administrative costs.

Chairman KASICH. Right, well, why wouldn't individuals be able to have the same limited choice, nevertheless choice, to direct their own money? Why should Federal employees have that right, but yet I don't have that right if I am not in the Federal Government?

Mr. LEW. What we are proposing for the Universal Savings Accounts——

Chairman KASICH. I am talking about—no, I am talking about for the payroll taxes.

Mr. LEW [continuing]. Well, the problem with the payroll tax being handled that way is that markets go up and markets go down. They don't always do it at times that are convenient for an individual person's retirement. If it is a small part of the total Social Security trust fund, we can handle those kinds of fluctuations in a way that an individual could not handle it. Our concern is if you take out an annuity on a day when the stock market went down 10 percent, you are losing 10 percent of the value of your savings for the rest of your retirement. That is something where if you waited a month, if you waited a week, certainly, if you waited long enough it would rebound. And if we share those risks, then we are protecting individuals from having the bedrock of their retirement, their Social Security benefit, fluctuate.

Chairman KASICH. But an investment made by a board is subjected to the same changes in the economy as if I am controlling it. In other words, a Federal employee has that option. They get to an invest in a series of risk managed accounts, and what you are saying is—and the other thing is, of course, we are not talking about people putting their money in an annuity tomorrow and taking it out the next day. We all know that the power of investing in the American economy is that over a significant period of time, over decades, the economy is going to return you about 6, 7, or 8 percent as compared to a government bond. So, we are not talking about in and out.

But let me just ask you this, Jack, to get to the bottom line: Is there any way that this administration over the next 2 years would permit the individual to be able to direct their—you know, the 2 percent of payroll—the way that they see fit in a government-approved account without this board? Is there any way that we could reach agreement on that or do you think that that is impossible?

Mr. LEW. Well, we have made very clear that keeping the current payroll tax to fund the current benefit system is key. We think that it would be risky to do anything other than that, but we have opened the discussion on giving the individuals the choice on how to invest for their own retirement with the Universal Savings Accounts.

Chairman KASICH. Right, but, in other words, the notion that we take 2 percent of payroll and allow the everyday American to be able to direct it in some board-approved accounts like Federal employees do, we cannot reach agreement on that in this Congress, is that correct? This is a very important point.

Mr. LEW. It is an important point, and what I want to be very clear about is that we are very committed to the current structure of a guaranteed benefit.

Chairman KASICH. OK, the answer is no.

Mr. LEW. And the guaranteed benefit sounds to me perhaps to be incompatible with what you are suggesting. I would like to look at a specific proposal before giving you a clear answer.

Chairman KASICH. Well, you know specifically what we are talking about, the Feldstein proposal. I mean, any one of them, Domenici; any of them, I mean, where you get 2 percent of payroll, and you get to direct it. You would not want the individuals to be able to do that, is that correct?

Mr. LEW. A lot of these proposals have had many lives, and the reason I am reluctant to give you a blanket answer is that I don't know exactly which one you are referring to. To the extent that some of these proposals spend the surplus to give these options and don't take the money out of the current payroll tax, it may be more like our Universal Savings Account and it may be a tax cut.

Chairman KASICH. No, we are talking about taking it out of the current payroll.

Mr. LEW. And I think you understand our view on that.

Chairman KASICH. That is what I was afraid of, the answer would be no, so that all these people walking around saying, "I think we can get the administration to go along with an agreement that individuals ought to be directing some of their payroll taxes" isn't going to happen, and I think we need to know that, because that then tells us how we are going to look at Social Security and how we are going to look at other parts of the surplus.

Mr. SPRATT. Mr. Chairman, they are proposing exactly what you yourself were proposing last year.

Chairman KASICH. What you have to understand, Mr. Spratt, is that is a weigh station. What I suggested is if can't go to 2 percent of payroll because there is paranoia about the fact that everyday Americans can't figure out how to invest their own payroll taxes, then what I would like to do instead of that is to give some of this surplus to individuals to put it in an account above and beyond Social Security so they can realize what gains they can make through market-oriented investments. But that isn't my solution. My solution is that 2 percent to 3 percent of payroll was that we can direct in government-approved accounts that can give us a growth of 7 or 8 percent that can get us out of this problem. So, I am just looking for an interim step, something that we can all agree upon that can use the magic of the American economy to be able to get us into a better position.

One last question, Mr. Lew, I know that the President in his speech in Buffalo—the Washington Post, one of my favorite newspapers—and we have got one of their great reporters here today—has quoted the President as saying of the surplus "we can give all back to you and hope you spend it right. The conclusion being that we can't take a chance on that; therefore, we have got to have all these targeted tax programs, because if we give it to you, you might not spend it the way we want you to spend it." Doesn't it make sense to give people broad-based tax cuts and allow them to direct it toward what their needs are rather than to have all the targeted tax cuts so that we force people to go through a maze in order to get their money once they come out the other side?

Mr. LEW. Mr. Chairman, we think there is a very clear choice. We think that we have gotten a fair amount of bipartisan agreement that putting 62 percent of the surplus aside for Social Security is a good idea. We may have differences to what it means to put 62 percent of the surplus aside, but I think we have a general agreement that that is the first step.

When you go beyond that, we think the next step is Medicare. We have current commitments to Medicare and over the next 10 years we will put $350 billion aside of the surplus to keep the commitments we already have. On the question of putting that money into a tax cut, I think one has to ask about the alternative. If there is an alternative plan that would extend the Medicare trust fund to 2020 that could reach bipartisan consensus, we would like to see it. We think that it is very difficult to cut benefits, it is very difficult to reduce payments to providers, and it is very difficult to come up with an alternative plan for Medicare that is attractive and meets with quick bipartisan approval.

So, the choice is not just a choice between a tax cut and nothing, it is a choice between a tax cut and putting the money aside to meet our commitments to Medicare. We think that is the right choice. It is a debate that we understand we are going to be having, and it will be a heated debate. We look forward to the debate because we think that is the right kind of debate to have when we have a surplus. Our view is that we have to be able to pay the bills for the commitments that we have today before we undertake new commitments——

Chairman KASICH. Yes, I am not talking about Medicare; I am talking about your targeted tax cuts as opposed to the notion that they ought to be broad-based and let people make their own choices.

Mr. LEW [continuing]. As far as the choice between the Universal Savings Accounts and an across-the-board tax cut, I think that that is a debate that we should have. We think that the right way to get tax relief is to encourage savings, to help people build the important leg on the retirement stool—personal savings. They now get Social Security. Some get a pension. They should also have savings. The alternative could be an across-the-board tax cut. We think that the distribution of a Universal Savings Account would help working people put money aside for their own retirement. We think that the benefits of an across-the-board tax cut would tend to go to higher income, wealthier people. This is the kind of debate that we could have reasonable disagreements on. We think those are choices that we should make. Our view is that Universal Savings Accounts are the right way to give tax relief, and we would welcome within the framework where 12 percent is allocated to a tax cut having that debate.

Chairman KASICH. Thank you, Director. Mr. Spratt.

Mr. SPRATT. Jack, let me just read from the record what Alan Greenspan said: "The President's approach to Social Security reform is a major step in the right direction, because it would ensure that the large surpluses projected over the next 15 years would be a positive contribution to national savings." I think it would be useful if you picked up where you left off in your testimony and took us step by step through how you propose to take the trust fund for Social Security from around $800 billion today to eventually over $6 trillion.

Mr. LEW. I would be happy to, Mr. Spratt.

Chairman KASICH. Even though the natural accumulation is probably half that amount. How do you do that and at the same time that you build up the assets in the trust fund how you would buy down the national debt from $3.7 trillion held by the public to $1.3 trillion?

Mr. LEW. Mr. Spratt, I think that we have to begin by reminding ourselves what happens in the trust fund if we do nothing. If we do nothing over the next 15 years, the trust funds will accumulate $2.7 trillion in additional assets. Those assets sit in the trust fund in the form of Treasury bonds which have the full faith and credit backing of the Federal Government just like a series-E bond or a bond bought by a corporation or a bank does. What we are proposing is to put more assets into the trust fund and have the increase go from $2.7 trillion to $5.5 trillion, doubling the additional assets in the trust fund over the next 15 years. And, as you pointed out, there is already almost a trillion dollars of assets in the fund. It would bring the total to over $7 trillion.

The question really is, what happens when those bonds come due? How do we pay the bills? When we came in in 1993, looking at the year 2012, when the Social Security Trust Fund was going to start to redeem the bonds to pay benefits, everyone was worried. They were worried because we were looking at a deficit in 2012, not at a surplus. The question was: if you can't pay your bills in 2012, how are you going to pay back the bonds? Well, we're not looking at a deficit in 2012 anymore; we're looking at a surplus. And because we have a surplus, if we lock in the surplus, we will be able to pay those bills in 2012 through 2055. And the point I made earlier about interest—perhaps a useful way to think about it is that a dollar of interest paid on a Treasury Bond that's held by a bank, or a private investor, is a dollar that goes from the Treasury outside. A dollar of interest paid to the Social Security Trust Fund is passed along in a benefit. So the dollar of interest has a very different end if you're paying off debt held by the public than if you're paying off debt held by the Social Security Trust Fund in the form of assets. We're saying that those dollars should be preserved so that we can pay our Social Security benefits without having to make drastic reductions in benefits, without needing a big tax increase.

We think it's prudent. We think it's only common sense. Unfortunately, government accounting is complicated, so it does take a little while to explain and to understand. But we think it is the most prudent way to carry forward the fiscal policy that's brought us the remarkable results that we're now enjoying.

Mr. SPRATT. What happens today with payroll taxes received by the Treasury is that the Treasury ends up holding the cash and the Social Security Trustees end up holding a special government bond?

Mr. LEW. That's correct.

Mr. SPRATT. What you're proposing is to take the cash that the Treasury holds and buy outstanding debt with it, and, in effect, transfer that debt in addition to the Treasury special bonds so that you will augment the Trust Fund twice?

Mr. LEW. That's correct. And instead of having that money go out in the form of either spending or a tax cut, let it build up.

Mr. SPRATT. Then, we build up to nearly $7 trillion; that includes the earnings on the money invested in the market and the earnings booked to the Treasury Bonds, and around 2020 we need to start drawing down that debt. At that point in time, instead of having several trillion dollars in outstanding debt held by the public, the

Treasury will owe maybe $1.3 trillion, according to your projections. Debt service will have fallen from 13 percent of our budget to 3 percent of our budget, and the Federal Government will be in far better fiscal condition to redeem these bonds so that the Social Security Trustees can meet the obligations of the beneficiary. Is that the scheme?

Mr. LEW. That is exactly right. And the choice we make today in terms of writing down the public debt is the key. If we let the public debt go back up, then our interest payments will go back, and we will lose the benefits that we've now projected for the future. We need to lock in what we are calling a virtuous cycle; it gives us the compounding effect of reducing debt to replace the vicious cycle that was eating us alive from 1981 to 1993.

Mr. SPRATT. Now, these USA Accounts are not strictly related to Social Security. They are supplementary to Social Security. The would be paid for, at least in part, by voluntary contributions and by government inducements that particularly moderate income citizens would enjoy. You have not yet defined all of the details, but don't you anticipate allowing each individual holder of one of these accounts at least the choices that Federal employees now have—either put it in a bond fund or a government bond fund or a corporate bond fund or a stock market index fund?

Mr. LEW. Yes, Mr. Spratt. First of all, it's independent from Social Security, and that's a point we really want to underscore. We don't think it should be mingled with Social Security.

We're working on the details and we're very concerned that as we define the details, we have as many good consequences as possible. We want to encourage current pension plans to continue to provide pensions. We want to encourage individuals who are currently saving to add to their savings, not just replace their savings. And we want to give them options, but we want to make sure we balance unlimited options with the cost of unlimited options.

One concern we have is that administrative costs can grow if there's unlimited option. The current Federal system gives us, all of us who are putting our retirement savings into it, a limited range of options, where we can put our retirement savings into a bond fund, into an equity fund, or into a government bond fund. We probably will want more options than that.

One of the things we hope to work out as we go through this legislative process is thinking through the consequences and how to draw the line in the right place. I don't think it's magic. I don't thing three options is magic. Unlimited options equally is not magic. Somewhere in the middle is the right balance, and I think we need to work together to try to define it so that individuals get the benefit of having the maximum return on their dollar go to their retirement and not go toward administrative expenses.

Mr. SPRATT. Thank you very much. One last question for clarification on another subject. Some of the press coverage of the budget yesterday and some of the criticism made of it by our colleagues across the aisle has indicated that there are significant tax increases in this particular budget, which seems odd at a time when we are looking forward to significant surpluses down the road.

As I look through the budget, I see a redistribution of tax benefits, from largely corporate taxpayers, who are enjoying what you call unwarranted tax benefits, over to individuals such as mothers and fathers who have children, with a dependent care day care credit; and mothers and fathers who have parents who are elderly and homebound—there will be a credit for them too—a thousand dollar credit for their long-term care requirements. It's a redistribution there of about $33 billion.

The New York Times yesterday included the recoupment from the tobacco recovery—a recoupment of what the States will be getting—$19 billion as a tax increase, but that's not a tax increase. You've got the reinstatement of a Superfund tax, which is just the renewal of the tax. You do have a $5 billion item for recasting the way we charge for using the airlines and the airways and the airports. But other than that—and, of course, your tobacco tax, which may or may not be a starter. I've got my doubt that it will go anywhere, but in any event, other than the tobacco tax is there any significant tax increase in this particular budget?

Mr. LEW. Mr. Spratt, I think you've got it exactly right. We have proposed a variety of revenue raising provisions to pay for a variety of tax cuts. We think that closing loopholes for sham transactions is something that we can agree is good policy. There are always people who benefit from those loopholes who oppose it, but that's the kind of normal battle we have to try to make the tax code work right.

What we've proposed in the form of tax cuts, we think are very important benefits—whether it's for long-term care or for building schools in our inner cities, or for providing for environmental bonds to be issued. These are all important investments that we think warrant the difficult choices in terms of closing loopholes.

Now with regard to the tobacco tax—we do have a tobacco policy in our budget. I know that it is a policy that not all of us agree on, but we feel very strongly that, first and foremost, it's good public health policy.

Last year, the President put forward a tobacco policy that was designed to increase the price of smoking to reduce teen smoking. Every day, 3,000 kids start smoking. Half of them develop tobacco-related illness. Our goal is to raise the price so that we will reduce in half the number of kids who start smoking every day.

And we are not imposing a burden in a vacuum here. Today, tobacco-related illness is imposing a burden on the Federal Government. We spend $8 billion a year in discretionary programs—the veterans' health program, the Department of Defense health programs, our own Federal employee health program, and a bunch of other smaller programs—to treat tobacco-related illness.

We would get $8 billion in excise taxes from the tobacco proposal, and it would just pay us back. The tobacco companies would pay us back for what we're spending as a Federal Government on discretionary spending for tobacco-related illness. We think it's only fair that that burden should be borne through the tobacco tax and not by the general taxpayer; that it shouldn't go to corporate profits, and it shouldn't go toward the benefit of the companies that are selling cigarettes.

The policy is controversial. We understand that, and we readily acknowledge in the budget that this makes it easier for us to fund other health priorities and other important programs. But what we're doing is we're getting back the money that we're now spending on tobacco-related illness, which we think is only fair.

Mr. SPRATT. Thank you very much.

Mr. CHAMBLISS. Mr. Lew, I thank you for being here this morning. As a new member of this committee, I look forward to working with you as we go through this process and hopefully reach an accord on this budget. I think it's interesting though that you say that there are no new taxes other than a tobacco tax when, in fact, as I look at your numbers, you are looking at increased fees for Coast Guard navigational services, $701 million; fees on international travelers, $1.6 billion; Medicare processing fee, $495 million, which doctors will pay when they process a Medicare claim, which means our Medicare patients will pay; FAA user fees, $7.1 billion; Federal Railroad Administration, $440 million; FDIC, $458 million; FCC fee, $1 billion, and on and on and on. That's about $11 billion over 5 years. If that's not a new tax, I don't know what it is.

I want to talk to you about a couple of different areas. On the first one, you know agriculture has always been the backbone of the economy of this country, and ag folks all across this country are in trouble right now. Nineteen ninety-eight was truly a disastrous year.

We need to make some solid, long-term changes in agriculture policy. The best way that we can do that, and certainly I think the President agrees with us based upon what he said in his State of Union Address, is to come up with a good, solid crop insurance program. In order to do that, we've got to basically throw out what we've got in place right now and start over with a new program.

The President said in his State of the Union that he wanted real crop insurance reform this year. Unfortunately, when I looked at this budget, I see absolutely zero dollars in the President's budget to be applied to crop insurance reform. Would you address that question, and tell me exactly how you plan to reform crop insurance and not pay for it?

Mr. LEW. Congressman, the budget, as the State of the Union does, acknowledges the very important need to revisit our crop insurance program and to reform crop insurance this year.

As you noted in your question, changing the current system is part of what one will have to do to create a new crop insurance system. Our experience in looking at this is that it is necessary to engage in a bipartisan discussion. We propose to engage in that discussion over the year, to make some of those tough choices, which are tradeoffs within the agriculture community and between different priorities of the agriculture community. The budget is a tight one. The fees that you described are the kinds of fees that we've been proposing for several years now in order to enable us to make the important investments that we need to make in areas like agriculture. The fees we've proposed in agriculture haven't all been accepted, which does make it difficult to provide the resources for new programs. I think we need to work together. We need to look at what our options are, and we need to make some touch choices. It's clear, the President made very clear in the State of the Union, and we made very clear last year in our response to the agricultural crisis last year, that there was a need for action. But these are tough choices, and they are choices that I think really are better made in a process where we're working together than when we're just putting competing plans out.

Mr. CHAMBLISS. Well, I still don't understand why you're not willing to fund crop insurance reform, but, be that as it may, it's interesting that one of the user fees that you're talking about is a fee that's going to be put on livestock processors. Now, when Mr. Nussle's hog farmers take their livestock to market, what's going to happen is that his farmers are the ones who are going to wind up paying that livestock processing fee. So, instead of helping agriculture in that respect, you are going to be reducing income to farmers across this country by the increase in the livestock processing fee.

The second area that I want to cover with you is in the area of national defense. I think we all agree that we've not been spending enough money in this area, and even the President in the State of the Union said that he wanted to spend additional monies in defense. He has come up with a figure of $12 billion, which, frankly, is a lot of smoke and mirrors—about $8 billion of that I think you would agree is just a redirection of current funds and a change in projection for inflation. So, we're really talking around $4 billion.

Of that $4 billion, if we're talking about a pay increase of 4.4 percent, we're looking at roughly two and a half billion dollars. If you pay for Iraq and Bosnia out of that, you're talking about another $3 billion, so you're already over that $4 billion in new money that the President is willing to put into defense.

Now, when the service chiefs testified before the Armed Services Committee they said that in order to bring every service branch up to par, not put us where they'd like to be, but to bring us up to par, it would take seventeen and a half billion dollars this year, not including the two and half billion for the pay increase. Why in the world, if the President wants to make a real commitment to defense, doesn't he listen to his service chiefs, who say we need $20 billion just to bring our services up to par?

Mr. LEW. Congressman, the President has listened to our service chiefs. We've been meeting regularly over the last year. From the moment that they identified a growing readiness problem, we took it very seriously. The President took it very seriously. He met with the service chiefs back in September and listened to what was really a very different kind of message than he had gotten before. It was a message that said things were changing. They were changing quickly. And it really required a response.

We worked very hard from September until we put this budget out first to add resources in the appropriations bill last fall to get a head start, and then to put together a plan that would take care of the highest priorities and all of the immediate needs that they identified.

Yesterday, Secretary Cohen testified at the Armed Services Committee at length on this issue, and I won't try to repeat all the details he went through. But I think it's fair to say that in his testimony and General Shelton's testimony, they agreed that what we've put forward in this budget is the program that we need to make sure that we take care of the immediate problems in terms of retention of personnel and in terms of readiness.

With regard to the arithmetic on the increase, I would beg to differ with your analysis of it. The inflation savings are very real savings. In a normal year, when the Defense Department sees inflation coming down, the funds that they are going to use go down because they are not spending a total number of dollars. They are buying a certain mix of goods and services. And if the cost of buying a helicopter goes down, then that money would not stay in the Defense Department budget in an ordinary year. By leaving that money in the Defense Department budget, we are permitting them to buy more—to buy more helicopters, to give a bigger pay raise. It's very real money.

In the out years, there is an element of projection here, and, as Secretary Cohen testified yesterday, we think the projection is a fair one, a reasonable one, and it reflects a commitment to policy. But we will follow it on a year-by-year basis. We're committing here to a program, a policy level, and if the inflation estimate for the future changes, we will have to reconsider the total resources required.

As far as the composition of our increase goes, a quarter of the increase in 2000 goes to personnel. That's to pay raises and to retirement benefits for the most part. The rest of the 75 percent really goes into readiness in the first year—spare parts, things like that. The procurement budget builds up as we go through the 5-year period. It's a very aggressive program. It's the largest defense increase in decades. We welcome the debate about the composition of it. We have gone through a process with the Pentagon and with the chiefs that has been a very, very important in terms of making sure that we give the best armed forces in the world the resources they need to remain the best armed forces in the world going into the next century.

Chairman KASICH. In the order in which people come in is how we recognize them, and the gentleman from Nashville is recognized.

Mr. CLEMENT. Thank you, Mr. Chairman.

Jack, good to have you here today, and I want to say to you on behalf of the American people, I think everyone appreciates very much the Clinton administration being bold and courageous in putting a lot of new ideas and new initiatives on the table. I just hope—and I really say this in all fairness to all the Republicans and the Democrats—I think we should give it every consideration—those ideas and new initiatives. And let us not have it dead on arrival simply because President Clinton proposed these new ideas, because people are concerned about the future of Social Security, the future of Medicare; about new incentives on savings, a stronger national defense, reducing the debt, education—all these are critically important.

Now I had the opportunity last week to speak with Chairman Greenspan, and I asked him about the tax cuts. And I know there are many that want tax cuts, substantial tax cuts. And I've sure voted for them in the past, and I am sure I'll vote for them in the future.

But I asked him about the tax cuts, about the timing of it, about right now. He responded to me, "Congressman, I am a Republican. Republicans like tax cuts. But our forecasts haven't been real good in the past. As a matter of fact, we should be still running hundred billion plus deficits rather than surpluses. I think we should pile those surpluses up for the future.'' You respond?

Mr. LEW. Congressman, when Chairman Greenspan testified, we actually were very heartened by his comments, because we viewed them as being really an endorsement of the basic approach that we've taken, which is, buy down the debt first. The best thing that we could do would be to buy down the debt and to be able to pay the bills for Social Security and Medicare that we're already going to owe for benefits that people have already earned.

Now, I think when he was asked the question as between tax cuts and spending increases, he gave the kind of answer that you described. But he was very clear: the best thing to do would be to buy down the debt.

By putting the money into Social Security and Medicare, we think that that's the best way to lock the surplus up, to lock it in for a good future, for an economic future and budget future, that we all will be proud in 15 years to look back and say we contributed to.

Mr. CLEMENT. Jack, last year we had some major wins for TVA, and our Chairman of the TVA Caucus, Zack Wamp, and Van Hilleary, who's on this budget committee, too—but the fact is we've been zeroed out, and a lot of us don't understand why because if you're on the Ohio river system, the Mississippi river system, Colorado river system, Missouri river system, you get taxpayer dollars for flood control and navigation. And, yet, here we're in the Tennessee Valley Area, and we're not going to get a penny. We rate payers are going to have to pay that.

Now I know there's a misconception that other parts of the country are subsidizing our power rates, but nothing could be further from the truth. Why should we be zeroed out in the Tennessee Valley Area?

Mr. LEW. Congressman, last year when we addressed the question of the Tennessee Valley Authority in the Omnibus Budget bill, there was a long-term policy decision made which we think gave lasting benefits to the Tennessee Valley Authority, which made it unnecessary to have a direct appropriation. There was a conversion of debt that the TVA owes to the Federal Government that permits the Tennessee Valley Authority to pay less interest because it rolled over loans that were at a higher interest rate to be repaid at a lower interest rate. If you look at the benefit over the period of time, it year by year replaces the appropriation. And, in a sense, it gave TVA benefit at least for the next 10 years, so that it wouldn't be subject to the year to year appropriations process. It was not actually meant to be zeroing out the TVA; it was more of a conversion of the form in which the assistance to the TVA is delivered.

Mr. CLEMENT. My last question pertains to Medicare, and I know your proposal is transferring 15 percent of the unified surplus into the Medicare Trust Fund. In order to further extend the life of the Trust Fund, the budget includes additional cuts in Medicare payments amounting to $9.5 billion over 5 years. I don't know about the rest of the country, but in Tennessee, 38 of our 127 hospitals lost money in 1997. It appears that 45 hospitals will lose money in 1998. And the Balanced Budget Agreement of 1997 hasn't even been fully implemented yet. What is the reasoning behind these cuts? Are they really necessary?

Mr. LEW. Congressman, the Medicare savings fall into two categories. A number of them are proposals that we've made in the past to deal with some problems that we tend to generally call fraud and abuse. They are to clamp down on overpayments and things like that. I don't think that's the portion of our savings that you are referring to. I think what you are referring to are the reductions in the provider payments, which are about half to two-thirds of our saving.

Nationwide, hospital profit margins have been very high, even after the Balanced Budget Agreement. We understand that there are pockets in the country—some rural areas and others—where that hasn't been the case. We need to look at what the impact of our proposals would be and to make sure that as we work through the policy, we don't have unintended consequences. It really was an attempt to put savings in the program so that we don't have Federal reimbursement resulting in higher profit margins than before the BBA, but at the same time, to put resources back into healthcare programs, to increase benefits so that people can buy into Medicare between age 62 and 65, to make sure that HCFA has the kind of reform and stable funding stream so that we can run a good Medicare program into the next century.

We look forward to a debate on these issues. And I would underscore that it is separate from this proposal on the 15 percent of the surplus. Regardless of what we do on the proposals for immediate change in Medicare, we think it's necessary to put the 15 percent of the surplus in because if this is an indication of how difficult it will be to make the program savings necessary to put $500 billion back into Medicare, it means we better save the surplus, and we better use the surplus to try and shore up the Trust Fund, because we're talking about the concerns raised with $9 billion of savings. Imagine what the concerns would be if we have $500 billion of savings.

Mr. CLEMENT. Thank you, Mr. Chairman. Thank you, Jack.

Mr. LEW. You're welcome.

Chairman KASICH. Mr. Hoekstra.

Mr. HOEKSTRA. Thank you, Mr. Chairman. Good morning. There are a couple of areas I'd like to ask some questions in. In the State of the Union speech, the President talked about the $15 billion that the Federal Government invests in our public schools, and he also talked about the need to support what works and to stop supporting what's wasted.

In your budget proposal, have you outlined specific areas where you believe we have been wasting Federal education dollars and how we would reallocate those funds?

Mr. LEW. Congressman, the budget sets forth a general statement of policy. We will be sending forward an Elementary and Secondary Education Act legislative package that will be more detailed.

What we have tried to do is put together a package that would encourage schools to end the process of social promotion. We put a lot of money into after school and summer programs. We need to create an alternative to the current cycle where there's no choice but to either leave the kid back or to have a social promotion, because they don't have an option that helps them catch up and stay in grade.

We've tried to put incentives in for schools to encourage the kinds of performance and excellence that I think we all agree should be universal in the schools. Sometimes our Federal programs help move things in the right direction. Sometimes they don't. We've put a package forward, and, as you know, the ESEA proposals will come forward in much more detail very shortly.

Mr. HOEKSTRA. And that will include an analysis of the programs and the types of approaches that have not worked in the past so that we can better learn from those programs and influence what we should be doing in the future?

Mr. LEW. Well, I think I've noted one of the major concerns we have. We think social promotion has been a very big problem. We think that the job of the schools is to make sure that we promote kids and that they are able to perform at grade; and when they graduate, they are able to go into the workforce and take jobs. I don't think we disagree on the goal. We may disagree on the mechanisms and that's what we hope to work through in the process of ESEA reauthorization.

Mr. HOEKSTRA. Well, that's what I am trying to get at. I am wondering if you've taken a look at the entire Federal role. One of the things that we are concerned about is the multitude of programs and the number of different agencies that are dealing with the area of education. I am wondering whether the administration has taken a look at whether creating a number of new programs with additional strings is the most effective way to improve education. At other times, the administration has talked about more flexibility for local schools and more discretion as to what they can do with Federal dollars. I am just wondering as to the administration—which way are you going to go—more programs with more strings or fewer programs with more dollars and more flexibility back at the local level?

Mr. LEW. Congressman, this year is a little different than other years because of the reauthorization of the major education programs. And I think we will be proceeding both with the funding of the initiatives that we have worked very hard on, from charter schools to after school programs; and working on the basic programs, to make sure that the basic programs are reformed or changed in a way to make the education dollars that we've put out more effective.

I think the question of either/or isn't the way we look at it. We have a number of goals. We have specific goals that we accomplish through these individual programs, and we have broader goals in terms of the very large dollars that we've put out through the basic education programs, which the school districts themselves mostly control. And we're going into that debate with the goal of preserving the independence of the local schools. This is a partnership. This is not a case where the Federal Government comes in and tells States, cities, and local school districts exactly how to run their schools.

But it is fair, when so many billions of dollars of Federal money are going into the schools, for us to ask some tough questions, and for us to challenge the schools to do better in certain areas.

We hope to do this in a cooperative way. We don't view this as the Federal Government coming in and taking over. It's a question of getting the balance right.

Mr. HOEKSTRA. I think that is exactly right: getting the balance right. And our experience would say that there are many at the local level who believe we might be getting out of balance.

On a different front, have you included a projection of the level of the gross Federal debt over the budget window in your budget proposal. I mean, is the debt, the gross debt going to increase or decrease?

Mr. LEW. We do have projections of both debt held by the public and the gross debt. This gets into an area that is complicated, and I apologize for using language that's more technical than I like to. But the debt subject to limit is a larger number than the debt held by the public, because all of the dollars that are in the Social Security Trust Fund in the form of Treasury bonds are subject to limit. The existing accounting rules are confusing because we save money and we call it debt subject to limit.

The important measure for the purpose of the economy is the debt held by the public. The question of whether or not the Federal Government is crowding out private investment really has to do with what's happening to the debt held by the public. We will be reducing the debt held by the public from 40 percent to 7 percent of GDP over the next 15 years, which means we're freeing up dollars for private investment and to lower interest rates. And we think that is a very good thing for the economy.

Mr. HOEKSTRA. I am interested in the gross debt. I mean a debt owed to Social Security is not necessarily a lot different than a debt owed to the public. You and I may disagree on that, so the gross debt does go up?

Mr. LEW. It does, but Congressman, the reason it is different is that the benefits that Social Security owes—that's the real debt. We have that debt today. It's not debt subject to limit. But it's a moral debt. It's a promise that we've made, and I believe it's a promise we will keep.

When we put assets in the Trust Fund and the debt subject to limit goes up, the only reason it's going up is that we're putting money behind the promise to pay the benefits that people are already entitled to.

Mr. HOEKSTRA. But it's still debt?

Mr. LEW. Yes, technically, those Treasury bonds are debt.

Mr. HOEKSTRA. This budget still has gross debt increasing during the time frame of your budget proposal, is that correct?

Mr. LEW. It's correct, but it's increasing for a good reason, because we're holding on to those assets.

Mr. HOEKSTRA. Good.

Mr. SMITH. Will the gentleman yield?

Mr. HOEKSTRA. Thank you. I'll yield for a minute, yes.

Mr. SMITH. Just noting that I noticed CBO in their estimate didn't have an increase in total debt.

Chairman KASICH. A compassionate man like I am. The gentlelady from Oregon is recognized for 5 minutes.

Ms. HOOLEY. Thank you, Mr. Chair.

Chairman KASICH. For 5 minutes and 15 seconds.

Ms. HOOLEY. Thank you, Mr. Lew, for your presentation.

I want to go back to Medicare. We've talked a lot about Social Security. I mean, I've read a lot in the paper about it seems there's some agreement that we're going to put 62 percent into Social Security. Medicare is a much more immediate problem, and where we're going to run out of money much quick in Medicare. And I, too, am concerned about some of the cuts that are proposed in there. I mean, again, I was talking to some of our hospital people yesterday and some of the small hospitals because of the reduction they are already facing in a 6-month period ended up being in serious trouble. So I am concerned about that.

But I am also concerned about what do we do if we don't put this 15 percent into Medicare. What's our next step if that doesn't happen? Do we increase payroll taxes? Do we decrease benefits? What are some of the alternatives without that 15 percent?

Mr. LEW. Congresswoman, that is the important question, because what we're proposing today is a budget that has many choices in it. When we say put the surplus aside for Medicare, we're looking at the alternatives. The alternatives are very large increases in payroll taxes or very large reductions in benefits.

Ms. HOOLEY. Tell me what you mean by large increases? What are we looking at?

Mr. LEW. Just the Medicare portion of the payroll tax, which is currently 2.9 percent. It would have to be 3.4 percent starting in fiscal year 2000. That means raising payroll taxes by .5 percent just to provide the kind of additional resources that we're talking about here. That's an 18 percent increase. We would be doing a bad thing to the economy if we put that kind of a tax increase in place right now. No one has proposed it, but if we don't set the money aside from the surplus, we have to be honest with ourselves about the choices. The choices are those kinds of payroll tax increases or benefit cuts or reductions to providers.

And, as I said to Congressman Clement, we understand that $9 billion of savings forces us to make tough decisions. It forces us to ask questions about whether your healthcare providers are being treated fairly or not, and we certainly do want to treat them fairly. To come up with $500 billion would require choices that are just enormously difficult. We saved $130 billion in the Balanced Budget Agreement. This is much bigger than that. And we think before we make any new commitments, whether it's to a tax cut or to large spending increases, we have to pay the bills that we owe. And that's why we put this plan forward.

Ms. HOOLEY. Thank you.

Chairman KASICH. But let me ask you a question. You can make no programmatic changes in Medicare, none, if you don't raise the payroll taxes. You don't reduce benefits. What you do is put a bunch of bonds in and say you've extended the live of Medicare, isn't that correct?

Mr. LEW. Well, we have put more assets in the Trust Fund. There's only three ways to extend the life of the Trust Fund. You can raise taxes, you can cut benefits, or you put more money. And we are putting more money in. We think that's the right thing to do.

Chairman KASICH. You can put more money, but you put more bonds in, which draws against the public. I mean you didn't put any money in there. You put the bonds in there. We have to honor Social Security. But we didn't put any money in there. That's a bookkeeping entry.

Mr. LEW. What we're saying is that those bonds have first call on Federal revenues, and that's the right thing to do. It's the right thing.

Chairman KASICH. Right. But you've made absolutely no programmatic changes in Medicare at all that would control any of the spending. You just say we're going to have more bonds in here, and so that can be drawn down on our kids. I mean——

Mr. LEW. Mr. Chairman, we agree that there's a need for serious programmatic reform. What the President said in the State of the Union and what he will be saying today again is we need to start by putting 15 percent of the surplus aside. We then need to go through the process that the Breaux Commission is going through. We will need to go through together to make the kinds of tough choices. And as we make those tough choices, we need to find savings. We also need to look at some real problems in terms of the benefit package. We need to have that kind of a discussion. But this will only make it easier. Any alternative has the burden of coming forward and answering the question, how would you extend it for 10 years if you don't save 15 percent of the surplus.

Chairman KASICH [continuing]. Right. But my only point is you presume that there is an infinite drawing down on our paychecks. And you have done nothing to make one single change in the Medicare program. You're just saying I am going to put bonds in here that our kids are going to pay, and we're going to pay. And we got all these bonds in there on Social Security that we're going to pay and we're going to draw down on. I don't know if the Democrats understand this, but there is no guarantee we're going to have enough money to pay all these things down.

Mr. LEW. Mr. Chairman.

Chairman KASICH. But to say we're going to put more IOUs in an account, and that extends the life of the program. I mean that's what we're talking about. We're not talking about one single choice that changes one crossed T or dotted I in the program. We're just saying there's more obligations to Medicare. And I agree with you, Jack, we're going to have to get the point where this commission's going to have to come through. But to say that we got more bonds in this fund, that should make us more all feel better is—I don't think that's leveling with folks.

Mr. LEW. Mr. Chairman, the real choice is what we do with the projected surpluses. If we, for example, have a large tax cut, that large tax cut will reduce revenue in the future. We're saying that rather than reduce——

Chairman KASICH. Of course, now that's a matter of opinion.

Mr. LEW [continuing]. Well, that's what most economic analysis shows: when you give a tax cut, you have less revenue.

Chairman KASICH. Well, that's not what is shown on capital gains. It's actually generated a heck of a lot more revenue. In fact, that's one of the reasons why we've had the big spurt in Treasury collections.

Mr. LEW. The choice that we're suggesting is that rather than have the revenue first be given back to a tax cut, we should put the money aside so that the first call on the surplus is to pay these bills.

Chairman KASICH. Right. Right.

Mr. LEW. And that is a choice. We understand there's a choice. It's the kind of debate we should be having.

Chairman KASICH. It's a first call, but it's not the money. Show me the money. I'll recognize the gentleman from New Hampshire, Mr. Sununu.

Mr. SUNUNU. Thank you very much, Mr. Chairman. Thank you for being here, Mr. Lew. I appreciate your taking the time. I know it's not easy. You follow in distinguished footsteps. Mr. Raines, I think always was very willing to enjoy the give and take and be forthcoming with information, and I think you've done the same.

You were very candid about the user fees and the tax increases that are part of this budget proposal. And you talked a little bit about some of its targeted tax relief, the very narrow targeted tax relief. The summary that I've seen—the total is for those taxes that are increased—it's about $82 billion in tax increases; about $26 billion in user fees over 5 years. I think the tobacco tax increase is one of the bigger of the tax increases. What is the 5-year total of the tobacco tax increase?

Mr. LEW. The 5-year total on the tobacco increase is about $33 billion.

Mr. SUNUNU. OK. So, $33 billion in tobacco——

Mr. LEW. Excuse me, $34.5 billion.

Mr. SUNUNU [continuing]. Thirty-five billion in tobacco tax increases is obviously a big chunk of the total tax increase. And the ranking member of this committee doesn't think that tax increase is going to go anywhere. Now, I am sure the administration feels very good about its ability to change minds, but I submit that when the ranking member of the Budget Committee doesn't think that the biggest part of your tax increase proposal is going to go anywhere, then you might have problem moving this budget package forward. What's your reaction to that?

Mr. LEW. My reaction to that is really to go back to what the purpose of the tobacco policy is. We feel very, very strongly that the tobacco policy is the right policy for the country. If we want to reduce smoking, if we want to improve public health, we know that the most effective way to do it is to raise the price. We also know that the tobacco companies have been raising prices on their own and increasing their profits, and that that's wrong. We shouldn't be raising the price for the benefit of the producers of cigarettes. We understand it's a debate that is going to be tough, but we're anxious to get into that debate. We think it is the right debate to have. And we think the American people will be well served if we prevail.

Mr. SUNUNU. You think you're going to win. You think you're going to be able to increase tobacco taxes this year.

Mr. LEW. We're going to try hard.

Mr. SUNUNU. You also included some money from the tobacco settlement with the States. I take it, you've run that idea past the States' governors?

Mr. LEW. Well, we were very careful with regard to the States to try and lay out a framework for working together with the Congress and with the States. There's nothing in the fiscal year 2000 budget that presumes an agreement on our proposal for using the Federal portion of the States' settlement. What we've said is we want to work with the States and with the Congress to identify a list of common Federal and State priorities so that we will identify Federal costs that the States would pick up as part of the settlement. Now, obviously, that would reduce the burden on the Federal Government, and it would free up resources for other purposes. We think that that's only fair. Medicaid is a Federal Program. Half of the Medicaid dollars are Federal dollars. The tobacco settlement gave all those dollars back to the States. We understand it's going to be tough, but we think it's the right thing to do.

Mr. SUNUNU. Once again, I think you're going to have a very tough time getting the support of the Nation's governors who I think have taken the lead on this issue; but, moreover, probably feel very strongly about keeping those funds to spend or to invest locally. And certainly, we've seen that a lot of local governments, States, municipalities tend to be more efficient than the Federal Government in whatever kinds of investments they make.

Mr. LEW. I should point out, though——

Mr. SUNUNU. I don't have much time. It's just a comment. That's not a question. And I would like to talk about the user fees, because you've got a few, quite a few.

And Mr. Chambliss began to read through the list, but I think it bears repeating because it is a lengthy list. There was a suggestion earlier that the tax increases in this budget represent a redistribution of wealth. And I think that's accurate. I suppose the assumption is it's a redistribution of wealth from the good taxpayers to the bad taxpayers; or, from the bad taxpayers to the good taxpayers. And that suggests I guess that some people, Americans, wouldn't be affected by the tax and fee increases. And I'd like to read through those user fee increases that are in your budget proposal: food safety inspection fees; animal-plant health inspection fees; grain inspection fees; Forest Service fees; navigational fees; fisheries management fees; patent and trademark fees; trade promotion fees; healthcare financing fees; Food and Drug Administration increased user fees; physician fees; managed care fees; provider certification fees; claim submission fees—all of these are user fees of the Medicare program—bankruptcy filing fees; alien certification fees; Coast Guard fees; hazardous material transportation safety fee—we're all for safety; customs air and passenger fees; customs access fees; commercial accident investigation fees; rail safety inspection fees; pesticide registration fee; analog spectrum fee; Social Security claimant fee; Federal Aviation fee. This is an interesting one. We changed the harbor fee to a harbor tax; or, rather a harbor tax to a harbor fee. I am not sure what the impact there is. We have bank exam fees, and finally Medicare premiums.

Have we left anyone out? It seems there can't possibly be anyone in America that's not impacted in one way or another from an increase in a user fee on an activity that they might rely on weekly, monthly, or everyday of their life.

Mr. LEW [continuing]. Let me, if I can, distinguish between three different categories. There are certain loophole closers which—I don't want to use ther terms "good" and "bad"—are closing down loopholes that shouldn't be there. I don't think that we would have a disagreement if we identified a sham——

Mr. SUNUNU. These aren't loopholes.

Mr. LEW [continuing]. No, no, I understand.

Mr. SUNUNU. These are all user fees to be clear.

Mr. LEW. I am just trying to identify the different categories. I don't think any of us would want a tax incentive for a sham transaction. We do have the tobacco tax——

Mr. SUNUNU. I didn't mention the tobacco tax, either. These are all user fees.

Mr. LEW [continuing]. I am trying to separate——

Mr. SUNUNU [continuing]. These are not taxes.

Mr. LEW. I am trying to separate the categories.

Mr. SUNUNU. They are not loopholes.

Mr. LEW. The user fees—which I think you have sort of merged with these other proposals in terms of the total numbers you've used—are really different in kind. And we believe that when the Federal Government provides a service, whether it's at a port of entry or at a food inspection station, that the industry that gets the benefit of the service should pay for it.

You use the example of the harbor fee. I realize that no one who represents a port city will be grateful that there's a harbor service fee proposal. But the Supreme Court struck down the former harbor fee that Congress passed because it was technically flawed. What we've put forward is a proposal that is technically not flawed, which reflects the policy that was already there. They are not all new fees. That's one of the larger ones. Many of the ones you used as an example are very, very small. That one is quite large. User fees are not popular by the users. Users would like to get services for free. Industries would like to get corporate subsidies. Chairman Kasich has taken the lead in identifying the need to close corporate loopholes and to do all that we can to make the government not provide unwarranted benefits.

The user fees mostly fall into that category. And, when you take them one by one, I think we probably could agree on more of the policy than we could the politics.

Mr. SUNUNU. Well, I appreciate your answer very much. I've tried to be clear, and the user fees there represent $26 billion. And you are right to distinguish that from the tax increases that are separate and above that $26 billion. Thank you very much. Thank you for your patience, Mr. Chairman.

Chairman KASICH. You're very welcome. The gentleman from Pennsylvania is recognized for 5 minutes. Mr. Hoeffel, yes. That would be you.

Mr. HOEFFEL. Thank you, Mr. Chairman.

Chairman KASICH. Where are you from in Pennsylvania?

Mr. HOEFFEL. I am from the suburbs of Philadelphia, which is what I want to ask my question about. Many of us from the suburbs are interested in the livability proposal that the administration has come forward with. Some say that the proposed spending would be helping social planners save or get involved with buying up open space. And the critics of the program seem to think that it's not an effective way of managing resources, controlling growth, or actually improving economic opportunities. Could you address some remarks to how the funding mechanism, which seems to be a Federal tax credit for investors in local and State bond issues that would generate the funding, would be used for open space and growth management programs. Could you address how that's going to actually improve the quality of life in the suburbs and improve the economic growth in the suburbs?

Mr. LEW. Congressman, we have a number of initiatives in the area of lands, what we call the Lands Legacy and the Livability Agenda. The green bonds that you are referring to are one component which would provide additional access to capital at a lower rate for environmentally sensitive investments, both in preserving open spaces and in improving the use of existing spaces that are not open spaces. We think that if you look at the combination of the initiatives in terms of preserving large public spaces, the Lands Legacy, encouraging the process of local planning to preserve open spaces, and providing access to capital so that the preservation of open spaces and the cleaning up of spaces that are currently used really answers a need that many Americans feel strongly about as we enter the new century.

Around the country, there is a growing concern that we're living in pretty good times right now. We have an obligation to take a view that's a little bit longer, and ask what are we going to do to leave behind cleaner waters, more open spaces, cleaner air. And we've tried to put together a program that's not big government; that doesn't say we're going to come in and tell local communities what to do. We're not going to come in and tell industry what to do. But we're going to give mechanisms, broad mechanisms, so that the grassroots movement, which is very strong—this is us responding to the American people, not the American people responding to us—has the tools to do more of what they are doing already.

And we're hopeful that this is an agenda that will have bipartisan support. It does seem to me to respond not just to the interest of suburban Americans, but urban and rural Americans as well.

Mr. HOEFFEL. You seem to be addressing the problems of sprawl, of unregulated growth that sort of leapfrogs out from the urban centers and replicates new infrastructure and new schools and new highways. And we keep building and building further and further out without reinvesting in the already populated areas, and, in the process, we use up a lot of open space and farmland and spend a lot of time in traffic gridlock.

This has never before been viewed as a Federal problem, and I applaud the administration for recognizing the role that the Federal Government can play in promoting some funding mechanisms but also elevating the problem to a national level.

Mr. LEW. You've actually pointed out one element that I left out, which is using our transportation programs to encourage the kind of planning that really is important. We have to be able to get to and from the places we need to do business and live without encroaching on our remaining open spaces.

Mr. HOEFFEL. On another subject, just quickly. You mentioned Chairman Kasich's proposal for corporate welfare reform in the last Congress. And I recognize the administration has identified unwarranted tax benefits in this budget proposal. I used a number of the Chairman's proposals in my campaign. I thought they were right on target. Have you reviewed what he called for, and is there some common ground there?

Mr. LEW. Well, we've had more ability of reaching agreement on the concept than on the details. [Laughter.]

There are some items on that list that I think we do agree on. There are other items where I think we consider it important investments in technology, where he would put it on the list as a corporate subsidy. There are important questions to ask. If you look at our user fees, if you look at the loophole closers, I think there's a shared objective of trying to make sure that we don't squander government resources with subsidies for private interests that don't need them. The devil is in the detail.

Mr. HOEFFEL. Right. OK. Thank you very much. Thank you, Mr. Chairman.

Chairman KASICH. Just for the information of the committee, we do intend to have a hearing on corporate welfare before we do anything with the budget. It will be coming up, and it should be interesting. I don't know who all will be there, but I know that Mr. Nader will be there, so it should be interesting. And I'll bet we will have a few press people in attendance for that one. Jack, you can come, too, if you want.

Mr. LEW. I'd be delighted.

Chairman KASICH. OK. Anyway, my—I think one of my heroes, Jim Ryun, is recognized for 5 minutes.

Mr. RYUN. Thank you, Mr. Chairman. I want to go back to a subject that was discussed a little bit earlier, but I'd like to get into it in a little more detail with regard to national security. I appreciate the President's interest in increasing pay as well as the benefits. And yet, I want to read a quote from the House Armed Services Committee regarding the military personnel and their concerns. Two top reasons that they are leaving: number one, I am tired of working extended shifts due to lack of help; and I am tired of being away from my family. Now, while we recognize that there's a need for pay increases—just this morning General Reimer recognized that he needs as much as $5 billion, but he's going to do well to have $2.4 billion. And part of the reason he needs that money is that a lot of these people have left; a lot of his NCOs have left, and it's weakened our military forces. In part, I want to send a message to the President to urge him to consider increasing the amount of money that is being set aside now for military, especially recruitment, because we are at a point where retention is very, very difficult.

But part of my question is going to go back to base closures. Robert Bell said earlier this year that he felt that there could be billions of dollars saved as a result of base closures, and yet the DOD has indicated that it would actually be a net cost of roughly $2.4 billion. Does this administration really think that they can save money through base closures that would contribute to the budget in some way?

Mr. LEW. We very much believe that base closures do contribute to long-term savings. The problem in terms of bringing the budget and the policy together are that in the short term base closures cost you money. In the long term, they save you money.

If we start with the premise that when the military identifies resources they don't need—bases that are not serving a useful purpose—we all worry about the dislocation, and whether we will need those resources in the future. We need to go through a careful process to balance these considerations. But once the decision has been made—once a BRAC-like process has concluded that a facility is no longer needed—if we spend the money to do it right in a short term, 10 years from now, the savings will be very substantial. Defense is not a 1-year kind of budget. The defense budget is done over 6-year periods of time. They take very seriously the year to year and multi-year impact of the decisions. There are only about three or four places in the government where multi-year planning is so important. I think because of that, looking at BRAC not as a contributor to savings this year or next year but perhaps as a cost and as a contributor to savings for the next decade for the first decade of the next century is really the right way to do it. By 2008 or 2010 the savings are very real.

Mr. RYUN. I am not totally convinced of that because if we are already in a spot, in a real problem with the number of people that we're sending out, we're deploying so often our troops are weary—if we're going to reduce the number of bases, and I am still not convinced it's going to be savings. I would just like to simply express my concern over that and ask the President to reconsider that. Mr. Chairman.

Chairman KASICH. Well, I want to thank you, Mr. Ryun. I wanted to let you know, I want to congratulate you on being the second American to break the 4-minute mile. I was actually the first one. I did it in a school-yard behind my house. Mine wasn't "finalated." I just didn't tell anybody, Jim. [Laughter.]

OK. Oh, Mr. Price from North Carolina is now recognized for 5 minutes.

Mr. PRICE. Thank you, Mr. Chairman. Mr. Lew, let me add my welcome and ask you to elaborate on a couple of aspects of your testimony.

In some ways, this first question picks up on the line of questioning Mr. Hoekstra was pursuing. It has to do with the debt reduction, which I think most people agree is one of the strongest features of your proposal—the great strides that you're proposing to make in paying down the publicly held debt, from $3.7 trillion to $1.2 trillion, or from 42 percent of GDP to 7 percent by 2015, under current assumptions.

Why have you chosen the mechanism that you have of transferring 77 percent of the surplus over the next 15 years to these trust funds—to the Social Security and Medicare Trust Funds—in order to accomplish this purpose? Why do you choose that? I understand that part of the reason is the political appeal, of course, of addressing the long-term trust fund shortfalls, but I think we do need some elaboration on exactly how this is going to work, because you are essentially moving that debt into the trust funds. As you said, the debt subject to limit is going to remain, but I also understand you to say, and now your—the last chart you showed a moment ago about the implications, those two kinds of debt have very different implications for annual interest outlays and thus for our capacity in the future to meet those obligations to those trust funds when those bonds come due. So could you elaborate on that, because I do think there's some confusion on the point of exactly what this debt reduction entails.

Mr. LEW. Congressman, I would be happy to elaborate. Usually I start with the substance, and then I go to the politics. But I think in this case, it may make sense to start with the politics.

It's very important that we actually accomplish the debt reduction. The notion of reducing the public debt is a difficult concept, but a very important one. And in the past, when the choice has been presented to pay down the debt held by the public or spend money on a tax cut or on other popular programs, it has been very hard, very, very hard, to sell debt reduction as a policy against a tax cut or a spending increase. So the politics is very much connected to the substance. To get to the debt reduction, I think we need more than just a passive debt reduction. We need to have a reason to do it.

The substance is very important as well. Debt reduction doesn't really do anything to extend the life of the trust fund. Yes, it means that we can pay the trust funds what they are currently due, and that's very important because it really is the first part of our plan—to make good the promises we've already made, the Treasury bonds that are in the trust fund now will be paid more easily just by simple debt reduction. But we want to increase the assets in the trust fund. We want to say that come 2020, there should be more Treasury bonds in the trust fund, and there should be more dollars being committed to Social Security rather than losing those dollars to a tax cut or spending increases. That is a substantive difference of great importance. That's why our plan goes from 2032 to 2055 in terms of trust fund solvency. The Social Security actuaries have looked at it. They've written a letter, which I would be happy to submit for the record; that it has that effect; that our plan would extend solvency to 2055. And that would not be true of simple debt reduction. Debt reduction is not bad, but we think that what we propose is better.

[The letter referred to follows:]

OFFICE OF THE DEPUTY CHIEF ACTUARY,
SOCIAL SECURITY ADMINISTRATION,
*Woodlawn, MD, January 26, 1999.*

HARRY C. BALLANTYNE,
*Chief Actuary*

LONG-RANGE OASDI FINANCIAL EFFECTS OF THE PRESIDENT'S PROPOSAL FOR STRENGTHENING SOCIAL SECURITY—*Information*

The President's proposal, presented in the State of the Union address on January 19, would require that transfers be made from the General Fund of the Treasury of the United States to the Old-Age, Survivors, and Disability Insurance (OASDI) trust funds for each year 2000 through 2014. The amount of transfer for each year would be specified in law as a percentage of the OASDI effective taxable payroll. In each year 2000 through 2014, 21 percent of the transfer would be used to purchase stock and 79 percent would be used to purchase special interest-bearing obligations of the Treasury. All dividends would be reinvested in stock until the market value of all stock held by the OASDI trust funds reached 14.6 percent of total OASDI trust fund assets. Thereafter, the percentage of total trust fund assets that is held in stocks would be maintained at 14.6 percent.

The proposal would extend the estimated year in which the combined OASDI trust funds would become exhausted by 23 years, from 2032 to 2055. It would reduce the size of the estimated long-range OASDI actuarial deficit by over one half, from 2.19 to 0.76 percent of taxable payroll. (Due to interaction among provisions, a complete elimination of the actuarial deficit will require additional OASDI changes that would reduce the present law deficit by up to 1.0 percent of taxable payroll.) These estimates are based on the intermediate assumptions of the 1998 Trustees Report and other assumptions described below.

If transfers were invested only in government bonds, the estimated year of trust fund exhaustion would be extended by 17 years, from 2032 to 2049. The estimated long-range OASDI actuarial deficit would be reduced from 2.19 to 1.20 percent of taxable payroll. This result also provides an indication of the sensitivity of the estimates to variation in the expected yield on stock. If, for example, the actual yield on stock over the next 50 years is no greater than the expected yield on government bonds, the estimated year of trust fund exhaustion would be extended from 2032 to 2049, rather than to 2055 with expected stock yield.

Stock investments would be managed by several brokerage firms, selected by competitive bid. Stock investments would be required to reflect the composition of all publicly-traded stock in the United States (for example, the composition of the Wilshire 5000 index).

Transfers from the General Fund of the Treasury would be made each year 2000 through 2014. The estimated amount of transfer for each year is shown below, based on the intermediate assumptions of the 1998 Trustees Report.

Estimated Amounts To Be Transferred to the OASDI Trust Funds

Billions of Current Dollars

| | | | | | |
|---|---|---|---|---|---|
| 2000 | $81.4 | 2005 | 117.4 | 2010 | 256.4 |
| 2001 | 67.2 | 2006 | 148.6 | 2011 | 280.0 |
| 2002 | 88.3 | 2007 | 174.8 | 2012 | 300.0 |
| 2003 | 87.2 | 2008 | 203.2 | 2013 | 316.0 |
| 2004 | 105.6 | 2009 | 232.5 | 2014 | 324.4 |

Amounts transferred would indirectly reflect values for years 2000 through 2014 that are about 62 percent of the expected unified budget surplus estimated by the Office of Management and Budget for the President's Fiscal Year 2000 Budget. Actual transfers for each year would be specified as the product of (a) the values computed under these budget projections, expressed as a percentage of OASDI effective taxable payroll, and (b) the then-current estimated taxable payroll at the beginning of each year of transfer. Revisions in amounts transferred each year would be made as estimates of taxable payroll for the year are finalized.

*OASDI Trust Fund Assets in Stock*

The 1994-96 Advisory Council on Social Security requested estimates assuming that the total annual real yield on stock investments would ultimately average about 7 percent, approximately the average (geometric mean) yield on stocks so far this century. (Total yield includes dividends as well as capital growth.) Estimates for this proposal are based on a more conservative assumption for the average ultimate total annual real yield of stock at 6.75 percent. The nearly four-percentage-point difference between this assumed ultimate real stock yield and the Trustees' 2.8-percent assumed ultimate real yield on government bonds held by the trust funds is assumed to be maintained throughout the 75-year projection period.

The table below provides the estimated percentage of OASDI trust fund assets that would be held in stock at the end of each year 2000-14. The stock holdings are estimated to reach the level of 14.6 percent of total trust fund assets at the end of 2014, after which point this percentage would be maintained under the proposal.

Percent of OASDI Trust Fund Assets in Stock, End of year

| | | | | | |
|---|---|---|---|---|---|
| 2000 | 1.7% | 2005 | 6.6% | 2010 | 11.2% |
| 2001 | 2.8% | 2006 | 7.6% | 2011 | 12.1% |
| 2002 | 3.9% | 2007 | 8.5% | 2012 | 12.9% |
| 2003 | 4.8% | 2008 | 9.4% | 2013 | 13.7% |
| 2004 | 5.7% | 2009 | 10.3% | 2014 | 14.6% |

If the average yield on stocks is greater or less than assumed over the period 2000-14, the year in which the specified level of 14.6 percent of assets in stock is reached would be sooner or later than the end of 2014.

The portion of the total value of publicly-traded stock in the United States that is held by the OASDI trust funds will depend not only on the yield achieved in the market, but also on the rate of growth in the total market value of all stock. The total value of stock represented in the Wilshire 5000 index (a fair representation of all publicly-traded stock in the United States) was $9.3 trillion at the beginning of 1998. Assuming that the total market value of publicly-traded stock will rise generally by the rate of growth in GDP after 1998, the trust funds would hold less than 4 percent of the total market value, on average, over the next 40 years.

Average Percentage of Total Stock Market Value Held by OASDI

| | |
|---|---|
| 2001-14 | 1.9% |
| 2001-20 | 2.9% |
| 2001-30 | 3.7% |
| 2001-40 | 3.7% |
| 2001-50 | 3.4% |

STEPHEN C. GOSS,
*Deputy Chief Actuary.*

Mr. PRICE. Now, you are paying interest on the debt held by the trust funds as well as on the debt held by the public.

Mr. LEW. That's correct.

Mr. PRICE. But as I understand it, the interest payments have vastly different implications for year-to-year outlays. Can you explain that?

Mr. LEW. In the Federal budget, we usually look at net interest. That is, the interest paid to the public. And if you look at the path of a dollar, I think it is crystal clear what the difference is. If a bank owns a Treasury bond and cashes it in, then the Federal Government will pay the bank interest on the Treasury bond. If the Social Security Trust Fund owns the Treasury bond, then the Federal Government will pay the Social Security Trust Fund the interest on the bond.

Now, I think the difference between a dollar of interest for the private holder of a bond and a dollar interest for the Social Security Trust Fund is the difference between night and day. The Social Security Trust Fund will take that dollar and pay a benefit that is currently owed. We're not increasing benefits. All we're saying is make sure the dollars are there to pay the benefits that we've already promised. I think if we have a choice to look back 15, 20 years from now and ask ourselves, are we paying more debt to private holders of government bonds, or are we paying more debt to pay Social Security benefits? We will feel a lot better if the dollars are there to pay the Social Security benefits and we don't have to make the cuts in benefits, and we don't have to increase taxes. That's a choice. It's a choice which I think is made crystal clear when you look at the alternative of what you do with the unified surplus. A tax cut or large spending increases lead you one way. Paying down the debt and putting the money into the trust funds lead you a very different way.

Mr. PRICE. Thank you. My time is about to expire. Let me ask you one further, quick question about the tax cuts that are contained in your proposal. I understand that there are a number of tax cuts. I think we all think, one way or another, when we're in surplus we should take advantage of that to return money to the American people. There is significant disagreement about exactly how we do that. But you're talking about childcare tax credits for stay-at-home parents. You're talking about incentives for employers to provide childcare on site. You're also talking about school construction. A lot of people don't understand it. That is a tax provision—the school construction. The long-term care tax credit. And then finally these USA accounts.

Since we are about out of time, perhaps the two you could focus on would be the school construction and the USA accounts, because I don't think it's generally understood that those are, in fact, tax incentives. How would they work?

Mr. LEW. Well, they are very different. The tax provision for the school construction program would make the investment in bonds that would finance school construction treated preferentially for tax purposes so that the interest wouldn't be subject to tax. It would make it easier to raise capital and would leverage the Federal investment, so that every dollar that we put into the tax expenditure for a school construction bond would bring many more dollars into school construction. It's a very efficient way to bring a lot of dollars into school construction that we probably couldn't do in a direct Federal appropriation.

It's fully paid for. We have offsets of $33 billion in our budget, of loopholes closers and other unwarranted benefits. That would be a paid-for proposal that we could go forward on today before we deal with Social Security.

The USA account is part of our framework for Social Security and the surplus. And we very much believe the USA accounts are the right way to give tax relief, but first we have to fix Social Security. So, first we have to put 62 percent aside for Social Security. Second, we want to put 15 percent aside for Medicare. And we think it does come first: keeping our obligation to Medicare comes first, even before the USA account.

Then, after we've done that, after we've taken 77 percent of the surplus and dedicated it to paying the bills for Social Security and Medicare, we think there should be a tax cut. And the USA accounts would be an incentive for individuals to save for their own retirement. Moderate- and low-income individuals would get a Federal tax credit, which would start them off in savings. Any dollar above that amount would be matched. Middle-income taxpayers, higher-income taxpayers would get less of a credit and more of a match. It would be very progressive. It would be a way to bring everyone into retirement saving so that it's not just something that the few have, but it becomes a basic, standard part of planning for the future.

It has several very important effects. It would increase national savings, whereas many tax cuts would not. It would help individuals get into the habit of saving and hopefully save more than the amount that we help them save through the USA accounts. And most importantly, it would give the kind of tax relief that I think there is a broad consensus that we need to think about in a very targeted way that would benefit the economy and benefit working Americans, as opposed to squandering it or spreading it in a way that might be less fair.

Mr. PRICE. Thank you, Mr. Chairman.

Mr. CHAMBLISS [presiding]. We want to give as many members as possible an opportunity to ask questions. So, if you will, let's abide by the 5-minute rule. And, Mr. Lew, when you see the red light come on if you would please speed up your answer. The gentleman from New Hampshire, Mr. Bass.

Mr. BASS. Thank you. I am sort of in the never-never land between microphones. Thank you very much, Mr. Lew, for appearing here today. And I want to make a general comment that I think I personally believe that the President has moved forward, especially in the area of Social Security, to begin a bipartisan dialogue toward dealing with the issues of both solvency as well as structural reform of the system that does give Americans the—a little more say over their retirement plans. And we do have some major disagreements. But I think it's a major start—or a significant start.

I share Mr. Sununu's concern about the issue of user fees, not only the idea that the user fees on aviation will have a significant impact, in my opinion, on aviation safety, but also on another area: on the concept that taking it—trying to loop what is, in effect, a settlement for tobacco—damages that occurred between States Attorneys General and the tobacco companies and the Federal Government somehow would try to grab a portion of that for its own damages, I think is wrong.

I guess my question—I've been a long-time advocate of special education. And reading in the budget here, you have a significant decrease in special ed. Now, I understand that you advance fund in the fiscal year 2001. I was just wondering if you could explain to me why you cut special ed funding from $5.1 billion to $3.1 billion, and then advance fund it back in fiscal year 2001, $1.9 billion, calling that the academic year. Is it not true that ultimately what you're really doing is taking money in the year 2001, in the very beginning and putting back into the year 2000 in order to make it look like you're staying within the budget caps, and, in effect, what you've really done is cut special education by $2 billion.

Mr. LEW. Congressman, what we've done in special education mirrors what the appropriators did last year with Title I. Last year, I believe it was a total of $6 billion of advanced appropriations, and we've said in the area of special education, in order to make room for the kinds of increases that we think are necessary in 2000, we should do the same thing. It doesn't do what I think you suggested in the question which is cut special education. Just as we're providing the full dollar of program benefits in the Title I program, we would be providing the full dollar of program benefits in the special education program. It's an accounting issue as to what year you attribute it to, and by attributing it to the portion of the fiscal year that matches up with the school year, it does give us the ability to spread it over 2 years, and then continue that going forward.

Mr. BASS. But the academic year begins in September, not October. I am going to quibble with you on a month there. And what you're really going to have to do—I understand that this is an accounting gimmick. But why don't you just put the money in the proper fiscal year, which begins on September 1 and admit the fact that what you're really trying to do is to redirect priorities to your other spending programs at the expense of special education and use a—I—sometime the chickens are going to come—I hate using cliches—they are going to come back to roost here. And then the next fiscal year, you're going to have another advance. You're going to do the whole budget with advanced—I am not going to support or give credit to advance appropriations. I don't agree with it in Title I, either. But the reality of it is why not just put the money in special ed and not cut it by $3 billion, $2 billion?

Mr. LEW. As I said, Congressman, we're not cutting it. What we're doing is we're financing it in a different way. So it's not a cut.

As far as the advanced appropriation question goes, it's a fair question to ask. And there have to be limits on how much of it we do, and I agree with you that it can't be done infinitely.

Last year, the House Appropriations Committee faced spending limits that were very difficult in the area of Labor-HHS. The House never passed a Labor-HHS appropriation bill. What the House committee did, I believe, was eliminate programs. I believe it eliminated the Low-Income Home Energy Assistance Program. It eliminated the Summer Jobs Program. And that was something that we had a pretty heated political debate about.

The Senate took a different tack. The Senate did put these advanced appropriations in, and it was a way to accommodate a broader set of priorities within the budget rules. It's not a perfect solution to tight caps. But it is a solution that works under the budget rules as long as we do it in a careful way.

I would argue, as with many of the choices we're discussing in terms of the surplus, it's compared to what. And we think that the advanced appropriation has no programmatic effect. I wouldn't reduce a penny of benefits in the year that they are needed. And that is the important programmatic issue.

As far as budgeting goes, I agree that we have to be very careful. And we are being very careful.

Mr. BASS. I appreciate. We will not only say that I believe that special education—that an increase in funding for special education should be a priority before we start discussing the new spending bills, the new spending proposals which, not only in new programs but in existing programs, equal well over—all right, I'll make it up—$1.5 to $2 billion in the next fiscal year. And I yield back, Mr. Chairman.

Mr. CHAMBLISS. Thank you. The gentleman from New Jersey, Mr. Holt.

Mr. HOLT. Thank you, Mr. Chairman. And it's good to see you here this morning. Thank you.

Mr. LEW. Thank you.

Mr. HOLT. What particularly pleases me about the budget you're proposing is the emphasis on the long term. And you, I would say, have resisted the temptation for immediate gratification in order to invest in things that will be with us for a longer period of time, or so that they can be with us for a longer period of time—Social Security, environmental protection, and so forth.

I'd like to look for a moment, though, at what we need in order to maintain our long-term productivity growth, and that would be education and research and development. And I am particularly pleased to see that you're talking about employer provided educational assistance as well as workplace literacy and that sort of thing.

I wanted to get a sense of how many people will be affected by these programs? What long-term effect this will have on the quality of our workforce?

Mr. LEW. It's difficult for me to give an exact number of the people affected, but the goal behind our literacy initiative is twofold: first, there is a big problem that we have a lot of people who have graduated high school and come into the workforce without the basic skills that they need. And that's not fair to them. It's not fair to society. We need to address that. We need to address it in terms of adult education. We need to make sure our schools produce results so that we don't have that problem in the future.

We also have an awful lot of immigrants who are here as legal immigrants, who deserve the same chance that many of our parents and grandparents got to learn English and to get into the workforce and make the contributions that we've always relied on immigrants to make in this country. And we've been very, very fortunate. Generation after generation has. Our adult literacy initiative really deals with both of those challenges. I'd be happy to get back to you with the exact numbers.

[The numbers referred to follow:]

According to the Department of Education, 5.712 million adults would be served under the adult literacy program if it were funded at the fiscal year 2000 budget request level. This is an increase of 1.249 million over the fiscal year 1999 appropriation.

Mr. HOLT. But just to get a sense, I would appreciate further information on how much of our workforce this could be expected to help.

And on the question of research and development, what do you see the effect of your budget having on our overall research and development effort.

Mr. LEW. Yes, we've had a very aggressive funding commitment to research and development for a number of years, and we've reached the point where, in some areas, we have gotten ahead of the schedule that we set out. We're now ahead of the schedule to double NIH.

We've tried in this year's budget to have a balanced approach, to make sure that basic science gets the funding increases in areas like NSF, and the Department of Energy, where some of the core theoretical science is done. There are slightly larger increases in those areas than in NIH, not because we don't support NIH, but because it was time to have a little bit of catch up on that kind of basic science. NIH benefits greatly from the basic science research done at NSF. And I think the percentage increase is about 7 percent in NSF, and we've kept NIH equal with inflation. That is ahead of schedule to getting to the doubling of NIH that we proposed over the last few years. We think it's a very important commitment and it is an investment in the future.

It's very difficult in the area of science to predict very accurately what you're going to get for each dollar you put in. We've worked very hard with the departments and the agencies that do science research to focus their dollars well, but to leave them the room through the process of peer review panels that they use to choose the best recipients for research dollars, not to micromanage and think that we know what breakthroughs they are going to find. We haven't been disappointed. The pace of scientific discovery only increases, and we're proud that our investments have been part of that.

Mr. BASS. Thank you, Mr. Lew. I yield back the balance of my time. Thank you, Mr. Chairman.

Mr. CHAMBLISS. Thank you. The gentleman from California, Mr. Herger.

Mr. HERGER. Thank you very much, Mr. Chairman. And thank you, Mr. Lew, for being with us.

I'd like to take just a little bit different tack. One is to compliment the administration on at least what in general we're hearing that would at least on the surface give the impression that we're not spending wildly; that we are being responsible; that, to use the terminology of the previous inquirer, that we're not seeking immediate gratification.

But my concern is when we look at the fine print of President Clinton's budget. And I am reminded of an editorial that was in one of our city newspapers here just a couple of days ago, which shares my concern. It had tax and spend, tax and spend, tax and spend. Now that's very, very different than the spin than we seem to be hearing. We're talking about these large surpluses that we have. But yet, under these large surpluses, looking at your document that you've put, put out by the Executive Office of the President on Management and Budget. And we look at even with these projected surpluses, we look at what happens to the national debt. And I notice that you try to differentiate between government and public debt as though somehow there's something different there, but most of us out in—at least where I come from—a debt is a debt is a debt—and it's something that someone someday will have to pay for—probably our children or grandchildren. But just looking at your numbers on page 389 of his document, where it shows what our debt will be. For 1998, $5.4 trillion, to 1999, $5.5 trillion; 2000, $5.7 trillion. I could continue reading for each of the next 5 years, not only with our projected surplus; not only does this debt not come down, it goes up. And it's increasing each and every year by your own document, despite what you may be saying, to the tune of $1.3 trillion increased debt over the next 5 years.

Now, I am concerned about that. When I go to my town hall meetings, the people I represent in northern California are concerned about this. And I notice that you have attempted in the last couple days—over in the Senate and here as well—to somehow make a different—to differentiate between the debt we owe out to the public and what the government owes; that somehow that differs.

And I'd like to have you explain to me how it's different? Is it not true that this debt is something that future taxpayers, i.e., our children and our grandchildren, at some point down the line will have to pay for? And isn't it very disingenuous to be talking about how we're really taking care of things when, in essence, we are increasing the debt on the heads of our children each and every year over the next 5 years by a total of $1.3 trillion?

Mr. LEW. Congressman, I have been trying to distinguish between debt held by the public and the debt subject to limit, because I think it's a distinction that really does make a big difference. A dollar of interest paid on debt held by the public is a dollar that is going to an investor in a bond, and that's fine. It's a good thing to pay investors——

Mr. HERGER. A taxpayer out—they are receiving some money for that?

Mr. LEW [continuing]. Yes, a bank, a corporation, an individual. I don't mean it as a pejorative. It's going to someone who's invested in a Treasury bond and we're paying it. But the dollar is gone as far as the Federal Government is concerned.

Mr. HERGER. Into the hands of a real, live person.

Mr. LEW. A dollar paid to the Social Security Trust fund is going to pay a dollar of benefits that's already owed. When we calculate the debt, we don't add into that calculation all of the Social Security benefits that are going to have to be paid that aren't already funded.

We're not increasing the moral debt of the country by a dollar when we put a dollar in to the trust fund and say that we're going to pay that dollar of benefits that we already owe. And because of government accounting, the debt subject to limit does go up when we put those assets aside. But our moral commitment is there.

The fact that we put a bond in the trust fund is the second step. The first step is we've made a promise, generation to generation, and unless we plan to break that promise, we're going to need the dollars in the future to keep it. What we've said is you can't keep that promise if you also spend the money today, on either a tax cut or a spending increase. And yes, it does commit future dollars. It says the first call goes to Social Security. The second call goes to Medicare. Those are promises we've already made. Before you make any new commitments, let's keep the promises we've already made.

Mr. HERGER. OK, in other words what you're saying—let's follow your reasoning through. Right now, I think about two-thirds of our Federal budget is going to some type of entitlement. People are entitled to this. It's already by law spoken for. So, in essence, what you're saying is that we're just going to increase that percentage so that our children some day, who are the only ones who are going to pay for this—I mean, this isn't funny money. It doesn't somehow come out of thin air. Someone is going to pay for it, and the real difference is, as I hear you explaining this in real world terms, is that the difference is that rather than give somebody this interest today, some real world individuals out here, what we're going to do is indebting our children and grandchildren; and yes, it would first call, but still we are an indebting—a debt is a debt is a debt—we're indebting somebody to pay this taxpayer somewhere down the line. Isn't that—well, let me just make a statement. In my mind, that is immoral what you are doing. That is basically lying to the American public at a time when we have surpluses and leading them to believe that everything is OK. We're taking care of your problem. When, in reality, just exactly the opposite is true.

Mr. LEW. If I could just respond briefly, Congressman. We think exactly the opposite. We've already made a promise. We've made a promise, and all of our projections in terms of the share of the Federal Government that goes to Social Security and Medicare assume that we're going to keep the promise. We're just putting the money behind the promise and saying let's not make new promises until we put the money aside——

Mr. HERGER. As long—you're—a debt you're putting behind it. You not putting money. You're putting something that will be paid by some future taxpayers, is that correct?

Mr. LEW [continuing]. Well, if we don't spend——

Mr. HERGER [continuing]. Isn't that what it is. Isn't that what a bond is?

Mr. LEW. If we don't spend the money on a tax cut or a spending program today, those dollars will be there in the future.

Mr. HERGER. A piece of paper written up in West Virginia will be there. OK, thank you. I think the point's made.

Mr. CHAMBLISS. I want to recognize my friend from Massachusetts for his questioning. And let me just say that we've still got a number of members here. We've got three votes. So it's probably going to take us 25 minutes for these votes. If you all want to come back and ask questions of Mr. Lew, if you're available, we'd like to have that option if members want to come back. Or, we can submit written questions. What's the preference of the committee?

OK, we got some that would like to come back. Can you stick around?

Mr. LEW. I would be delighted to stay if members would like to come back.

Mr. CHAMBLISS. OK. Great. I recognize the gentleman from Massachusetts, Mr. Markey.

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

Mr. Lew, as we look at your pie chart over here, 62 percent of the pie chart is dedicated to Social Security?

Mr. LEW. That's correct.

Mr. MARKEY. Now the way that I understand it is that the Republican 10 percent across the board tax cut would consume an additional 38 percent, is that correct?

Mr. LEW. That's my understanding.

Mr. MARKEY. Now, the way I've heard it on television in the last couple of days, Mr. Archer and Mr. Domenici have both said that the 62 percent now up for Social Security makes some sense to them. I think that I've heard that. If that's the case, that means that the Republican 10 percent across the board tax cut consumes all of the money that would be expended for Medicare, all of the money for the universal savings accounts, all of the money for defense, all of the money for education, all of the money that's left on that pie chart. So the 10 percent tax cut, obviously, is something that threatens every other program, except to the extent to which I guess I would say that I am not worried that the money will be found by the majority for the defense budget. I think they are finding that one. But that puts even more pressure on Medicare, even more pressure on education, even more pressure on the universal savings account.

And here's the problem that I have. In 1997, as part of the last budget deal, there was a $115 billion cut in Medicare, which almost exactly matched the huge tax cut—huge, however, only in 1997 terms, not huge when compared to a 10 percent or a 9 percent or an 8 percent across the board tax cut in perpetuity.

So here's my problem: there was a $17 billion cut out of Medicare for home health services in 1997. We have 4,000,000 people with Alzheimer's in America. We have millions more with Parkinson's and other neurological diseases, cancer, diabetes. They are at home. And husbands are caring for wives, and wives are caring for husbands. Then we cut that program by $17 billion. All they got was a daily visit from a visiting nurse to give them a break. This just gave them a couple of hours where they could take a nap.

Now, these people are the biggest heroes in our society. Twenty-four hours a day with their wife or their husband in a condition that is almost impossible for anyone in our age group to even consider. But they do it. And they are the real heroes. But heroes need help. And the way this debate is now structured, following on what happened in 1997, is that we're guaranteeing that that generation of people who built this country are going to be left with a smaller and smaller and smaller share of the help which they need to be heroes. And I think that if this tax cut debate continues as it has, that we're going to wind up with a tremendous confrontation in this country—between the legitimate needs of this older generation that can only be served if the revenues are there. And they are there. And by the way, I think when we did that tax cut in 1997, if that has produced this surplus, we cut home health care in order to do the tax cut. Now, we've got the surplus, let's give back the money to the program.

Now, Mr. Lew, can you help me with this. I know you've made an effort to increase somewhat the program for home health care in your legislation, but it still is far short of the money that was cut out in 1997, or of this growing need which has been identified in our society.

Mr. LEW. Congressman, the choice that you've put forward is a very real one. If 38 percent of the surplus is dedicated to a tax cut, I believe that that will mean cuts in Medicare in the future, and I believe that those are going to be very, very difficult and painful decisions. We have to deal with Medicare. We have to go beyond this 15 percent and make the kinds of long-term reforms that require tough choices. The President, in the State of the Union, said that that would give us the opportunity to make some tough changes and also perhaps expand some benefits like the prescription drug benefit so that the program meets more of the needs of people. But if we don't start by putting 15 percent of the surplus aside, we are setting the bar very high. And we are probably going to have difficulty reaching bipartisan consensus. And we're going to be faced in a very short period of time with very difficult choices. We think the most prudent thing to do is to take the good fortune we have, that we've gotten because we made tough decisions on Medicare, we made tough decisions to reduce the deficit. We now have a surplus. We should put some of it back. That 15 percent would really be putting money where we should put it, to keep the promise we've made to pay benefits.

Mr. MARKEY. Thank you, Mr. Lew. Thank you, Mr. Chairman.

Mr. CHAMBLISS. We will stand in recess until 12:45 p.m.

Mr. LEW. Thank you.

[Whereupon, at 11:57 a.m., the committee recessed, to reconvene at 12:45 p.m., the same day.]

Mr. CHAMBLISS [presiding]. All right, why don't we resume, and we will take members as they come back in the order that they are on the list, and if we have to skip somebody, we will try to get back to them. But the gentleman from Pennsylvania, Mr. Toomey, is recognized for 5 minutes.

Mr. TOOMEY. Thank you, Mr. Chairman, and thank you, Mr. Lew.

Just a couple of questions for clarification purposes. The courts have clearly stated, I believe, that workers have no ownership per se, no property rights to the payroll taxes that they pay into the Social Security system, and that implies and really means that all future benefits are, therefore, entirely subject to the whims of politicians. Is it true, is it fair to say that the President's proposal does nothing to substantively change that feature?

Mr. LEW. I think that it is true that individuals don't have a right to their contributions. But I think that it is not correct to say that they don't have a right to the benefits. It would require a change of law to take the benefits away from them.

Mr. TOOMEY. Exactly, which could happen by a majority vote of Congress——

Mr. LEW [continuing]. Yes, it could.

Mr. TOOMEY [continuing]. And passage by the President at any time.

Mr. LEW. It has not been an easy thing to do in the past, but, yes, theoretically it could happen.

Mr. TOOMEY. Right.

In your opening comments, I believe, if I understood you correctly, you suggested that one of the important features that the President feels must be retained in Social Security is that the benefits are guaranteed, there be a guaranteed defined-benefit program. But, in light of the previous question, isn't it really impossible under the current structure to guarantee them because the political process could always reverse that guarantee?

Mr. LEW. Well, I would say that the history since 1935 has been expanding, not contracting, benefits. In 1983, there was a bipartisan effort to deal with the Social Security financing problem. Tough decisions were made. It was very, very difficult to get agreement on any benefit reductions. And I would suggest that benefit reductions will be very hard to make for good reason. People work their lives and plan on receiving the benefits, and they do have a right to them.

Mr. TOOMEY. Right, but we also are in a situation now as the system has matured and there are no longer ever-increasing numbers of workers paying for an increasing number of retirees, it is going to be much harder to make those payments. So, I would suggest that the ability to honor those payments under the current system is increasingly in jeopardy.

Mr. LEW. And we agree that we need to work together to get 75-year actuarial solvency, which would require some of those tough decisions. We think that this is a good first step.

Mr. TOOMEY. OK.

Second question is, in a system in which workers were free to direct and actually own, actually have property rights to a portion of their payroll tax, invested as they see fit, perhaps with restrictions and guidelines, if such a system included an explicit government-minimum guarantee in it, would that not fulfill that objective, and would the President, therefore, be willing to consider such a system?

Mr. LEW. We have said for the last year that we would look at alternatives, specific alternatives, as they are proposed. I am a little reluctant to respond to a hypothetical. The principles that the President laid out through the past year of discussion about Social Security reform have been very clear about guaranteeing the benefits, about making sure that there is progressivity in the system, making sure that we don't somehow do something that undermines the benefits available for someone when they become disabled, for a survivor.

In order to answer a question about a specific plan, one really has to look at it in its entirety. We think that preserving the core benefit as we have it today is the safest way. But we will look at alternatives. We have said in recent weeks, and I have said this morning, that our view is that the entire payroll tax should remain dedicated to the traditional Social Security benefit.

Mr. TOOMEY. OK. Let me try to ask it a different way.

Would it be fair for me to conclude, then, that if the design of the system met certain conditions that you feel are important, then there would be a possibility that the President would agree to a system in which workers would own and control a portion of that payroll tax?

Mr. LEW. I think that I have indicated very clearly what our view is. You are asking me to draw hard lines about it, not even having a discussion. We have tried very hard, on an issue where it is difficult to keep lines of communication open, to keep lines of communications open. So, I am trying not to draw the kinds of arbitrary hard lines. But at the same time, I am trying to be very clear about what our view is and what our position is. And we are not wavering from that. I am not wavering from that today.

If there is a specific plan that you would like us to look at, I would be delighted to look at it. I would be delighted to have our Social Security team look at it. And I think that the five principles that the President outlined over the past year speak for themselves, and that is what will guide our view of any proposal. Our view is that the Social Security payroll tax should remain dedicated to the traditional benefits.

Mr. TOOMEY. OK. Thank you Mr. Lew.

I will yield the balance of my time, Mr. Chairman.

Mr. CHAMBLISS. Thank you.

Mr. Minge.

Mr. MINGE. Thank you, Mr. Chairman.

Mr. Lew, as I understand it, in fiscal year 1999, to talk about a surplus requires that we focus everything on the unified budget, and if we were to simply look at the Federal budget without Social Security—as I believe the budget legislation requires us to do on the congressional side—we would have a deficit of $38 billion. Does that square roughly with the numbers that you have been working with?

Mr. LEW. Yes, it does.

Mr. MINGE. And, as I understand it, that would mean that if we were to have a tax cut this year, we would be borrowing money, essentially, from the Social Security Trust Fund in order to fund that tax deduction, and similarly, if we were to expand programs this year, we would be expanding them by borrowing that money from the Social Security Trust Fund.

Mr. LEW. Technically, we are leaving the assets to the Social Security Trust Fund, but the entire surplus this year is attributable to the contribution of Social Security through the off-budget calculation to the surplus.

Mr. MINGE. Now, I would like to take this one step further and look at the 15-year proposal which you have outlined, which I think is admirable because it really challenges Congress and the country to plan in the long term.

If we were to simply insist that as long as we must rely on the Social Security Trust Fund to balance the budget that we would devote all of the surplus, so to speak, which is really all of the Social Security Trust Fund money, to the Trust Fund and not have any program expansion or tax reduction that was not otherwise offset within the budget, wouldn't we be doing better by the Social Security Program by such an insistence, at least during the next couple of years until we have a surplus in the nonunified budget?

Mr. LEW. Well, I think that we would have to look at the Social Security Trust Fund, and the question of the unified budget a little bit more broadly, looking at a longer term. The Social Security Trust Fund will build up assets from now until 2012. Until 2012, Social Security revenues will be equal to or greater than the benefits paid. After 2012, the Social Security Trust Fund will start getting drawn down, and under current law it will expire in 2032, and we have proposed to extend it until 2055.

The question of the unified budget, as much as what do we do today, is what condition will we be in in 2012 through 2055? And at that point we will need a non-Social Security surplus of substantial magnitude to pay back these bills to Social Security.

So, the discussion of "on budget-off budget" becomes a very different one once those lines cross and Social Security starts needing to have its bonds paid back as opposed to paying them in. And we——

Mr. MINGE. But for the next couple of years the lines haven't crossed——

Mr. LEW [continuing]. Correct.

Mr. MINGE [continuing]. And we are dealing with truly a deficit in the nonunified budget, and what we are trying to do, as I understand the President's proposal, is to look at this 15-year period of time and saying, "If we can maintain the course for 15 years and devote 62 percent of the unified surplus to Social Security, we are going to be ahead." Do you have any estimate as to how much we would be ahead by doing that as compared to simply insisting that all of the Social Security Trust Fund cash flow surplus be reserved for Social Security purposes?

Mr. LEW. Well, roughly speaking, if you looked over the next 15 years, the 62 percent that we are putting in over 15 years is roughly equal to the off-budget Social Security surplus. If you look at the Medicare component, that is all additional debt reduction. That is all additional savings for the future. And it is a rough proxy. It is really when you get beyond the 62 percent that the question starts to come in.

On a year-to-year basis, our proposal would not be exactly as what you have described, but over 15 years, it would be a little bit more.

Mr. MINGE. It would be a little more, but it would be roughly the same. It is when you look at Medicare that you are really making a dramatic improvement in savings.

Mr. LEW. That is right.

Mr. MINGE. Now, to take this one step further, it troubles me that here, at least for the next 2 years, we would be only using 62 percent of that Social Security Trust Fund surplus that is being generated each of these 2 years for the Social Security Program and we would be counting on future Congresses and future administrations that show the self-restraint and the discipline to stay the course on that 62 percent thereafter, when, of course, it will be a future Congress and a future administration.

Is there anything that you see that we can do during this year and next year that would truly commit future Congresses and the future administrations to this course, or is it somewhat like what we faced back in 1994 or 1993 when we adopted a 5-year budget plan, but when the next year rolled around and the next Congress rolled around, that budget plan was just gathering dust? That was history. And people again wanted to plan and look to the future.

Mr. LEW. I think that there is a very big difference between a budget plan and a promise to make certain contributions to the Social Security Trust Fund. I would hazard the political guess that, if we put into law scheduled contributions into the Social Security Trust Fund, that we will keep those promises and that it will be very difficult for future Congresses to change that. It is not impossible. Our constitutional system does give future Congresses the right to change the law, but I think that it is highly probative how difficult it has been to cut Social Security, and I think correctly so. I think that it is very unlikely that we would see a substantial backing off of commitments that we make this year to put money into the Trust Fund.

Mr. MINGE. Thank you.

Mr. CHAMBLISS. My good friend and colleague from Georgia, Mr. Collins, is recognized for 5 minutes.

Mr. COLLINS. Thank you, Mr. Chairman.

Mr. Lew, I want to go back to a comment by Mr. Minge, when he referred to tax relief as having an effect on Social Security.

Under current budget law, tax relief would not affect Social Security unless the benefit structure of Social Security was changed. Is that not true?

Mr. LEW. I am not sure that I understand the question.

Mr. COLLINS. You do nothing to Social Security, and you give tax relief, it has no effect on Social Security.

Mr. LEW. Well, it wouldn't reduce the benefit that we owe.

Mr. COLLINS. It would not even affect it.

Mr. LEW. But, it would reduce our ability to pay the benefit.

Mr. COLLINS. The question, though, it would not affect—tax relief would not affect Social Security unless you change the benefit structure to match the tax relief also?

Mr. LEW. But we have no way now to show how——

Mr. COLLINS. Yes or no to that?

Mr. LEW [continuing]. I don't think that it is a simple yes-or-no question.

Mr. COLLINS. Sir?

Mr. LEW. I don't think that it is a simple yes-or-no answer, Congressman.

Mr. COLLINS. Yes, it is.

Mr. LEW. Then the answer is, yes, it would affect Social Security.

Mr. COLLINS. It would not affect Social Security at all.

Mr. LEW. Yes, it would.

Mr. COLLINS. I only have limited time. You seem to want to skate around the answer there. Let's don't do that on some of the others.

Lots has been said about Mr. Greenspan and some of his comments. When he testified before the Ways and Means Committee the other day, he had several recommendations. One, he said, run the surpluses. I am very reluctant to use the word "surplus"; I like to use the words "positive cash flow" because it is all over in the Trust Funds today, the positive cash flow. And I understand, too, by running those positive cash flows into the Trust Funds and having public debt offset by government bonds will help in the area of interest rates.

Second thing, though, he said, is if you do look at tax reduction, look at marginal rates, and also look at capital gains tax relief. We know that some of the changes that have taken place in the last 4 years have been through the cooperation of the Congress and the administration in a year of taxation, and one of those was capital gains tax relief.

But what he did caution about was no new spending, no increase in spending. Now, he did not say no new programs, and no one else will say no new programs. But if you are going to look at new programs, you look at them within the structure of your existing budget where you make your move around your budget caps.

Another thing that he cautioned us about, and it is in an area of Social Security, and that is in the pay-as-you-go system—in other words, current workers are paying current beneficiaries' checks—but what I see that the President has offered is not an end to the pay-as-you-go system but an extension of it from some 30 to possibly 50 or 75 years. Is that not true?

Mr. LEW. Well, it is a change in the sense that it is committing resources in a different form. Pay-as-you-go refers to the payroll tax, and this is a bit different.

Mr. COLLINS. But it doesn't change the pay-as-you-go system from that of social income insurance to that as vested interest retirement.

Mr. LEW. That's correct.

Mr. COLLINS. And a debt is a debt. And as you have said, each year the national debt increases. Now I understand your difference between the public sector portion of it versus the government portion of it, but it does increase. And at some point in the future—I don't see the chart there now—you estimated that the interest portion of the budget would be 2 to 3 percent?

Mr. LEW. That was 2014, that projection.

Mr. COLLINS. Now, using that 2 percent or 3 percent—and I believe that you answered this when Mr. Price was questioning you—that does not include the interest accrued of interest owed that particular year to the Trust Fund. Is that not true?

Mr. LEW. That was net interest, correct.

Mr. COLLINS. That's right. So, that is true; it does not include it. If you use the word "debt interest," that means that you have excluded that portion.

Mr. LEW. That's correct.

Mr. COLLINS. OK.

Once we get to the point of having to redeem those government-held securities, how do you plan to do that? You said that you have to have discipline in the budget and have resources beyond the unified budget.

Mr. LEW. Our current forecast shows surpluses—I forget if it is through 2045 or 2046; it is way, way out into the next century. If we are running surpluses in the non-Social Security budget, we will be able to pay those bills back, and that is exactly the point in terms of fiscal discipline. If we are not running those kinds of surpluses in the non-Social Security budget—we already have the debt. The Social Security benefit is a promise. If I were to promise you that I was going to give you $100, that is a promise. If I then write up a note, that doesn't make it more or less of a promise. That records it. When you record it, it shows up as increasing the debt subject to limit. But the promise is every bit as much there today without that note.

Mr. COLLINS. But it you are increasing the debt year after year based on new spending, that is not very good fiscal discipline, is it not?

Mr. LEW. I actually think that it is very good fiscal discipline, and most of the comments that Alan Greenspan——

Mr. COLLINS. An increased spending and increased debt year after year?

Mr. LEW [continuing]. Alan Greenspan, when he testified before the Congress, made a number of points. He said that the President's approach to Social Security reform is a major step in the right direction and that it would ensure that the current rise in government's positive contribution to the national savings is sustained. The reason that he said that is that we reduce the debt held by the public.

Mr. COLLINS. That's right.

Mr. LEW. And that is the reason that we have the virtuous cycle which reduces the net interest cost. I would argue that there is a very big difference between a dollar of interest that is being used to pay a current commitment for Social Security benefits and a dollar of interest used to pay a privately held bond. A dollar is not a dollar in this case. One dollar is keeping a promise to Social Security; the other is not.

Mr. COLLINS. In the area of accounting you use the same dollar twice the way you are using it. And that——

Mr. LEW. No, we actually haven't used the same dollar twice.

Mr. COLLINS [continuing]. Yes, you are. And also—I am going to close with this because my time is up—I think that the greatest threat to this Nation is the national debt. At one point in time—at some point in time in the future it will bankrupt this country if we don't get this thing under control and keep it under control.

Thank you, Mr. Chairman.

Mr. CHAMBLISS. The gentleman from Minnesota, Mr. Gutknecht.

Mr. GUTKNECHT. Thank you, Mr. Chairman, and I appreciate this opportunity to visit with you, Mr. Lew, and I appreciate a lot of the things that you have said today. In fact, I probably, at least on this side, am going to be more congratulatory perhaps than some of my colleagues, because it seems to me that there are three questions that this committee and ultimately the Congress has to answer. The first question is, how much do we want to spend? The second question is, how much surplus will that create? And the third, and perhaps the biggest, question that we are going to have to resolve is, what is the highest, best use of that surplus?

Now we can argue—and I have found, and I will let my colleague pass here—I have found in my townhall meetings, and when I meet with my constituents, one of the most difficult questions to really respond to and to define is this whole Social Security system because it seems to me that it is a hybrid between a defined-benefit plan with a Trust Fund and a pay-as-you-go system. And that is how we sort of wind up speaking out of both sides of our mouths about the unified budget, and it does get very difficult. And I don't have a perfect answer for it either.

But let me come back to the central question: how much do we want to spend? And that is where I really want to give the administration a tremendous amount of credit because, as I read through the budget, as my staff looked at it and as I looked at the numbers, and so forth, the first thing that really did strike me is that you are talking about a total spending increase for the next fiscal year of only $39 billion. Now am I correct in that?

Mr. LEW. I don't remember the exact number, but it is very close, if that is not right.

Mr. GUTKNECHT. And if I remember correctly, and I have been one who has felt very strongly that it is important for this Congress, for a whole variety of reasons, to keep faith with the spending caps which have been set in the past, and with at least the spirit of the balanced budget agreement that the President signed a couple of years ago, and many of us went down to the Rose Garden to join in the signing. And as I read your budget request, you are actually talking about exceeding those spending caps by only $17 billion.

Now, I think that within that framework there is at least an opportunity for us to agree—the Senate, the House, Republicans, Democrats, Independents, and people in the administration—to agree to some kind of a spending cap that is somewhere at least within the spirit. And starting with your budget document, I must say that the average family, to the best of my knowledge, the average family budget today in America will probably increase about 2.5 percent. So, to your credit, for the first time in my memory, we are talking about increasing the Federal budget at a slower rate than the family budget, and you deserve a tremendous amount of credit for that.

That is the good news. The bad news, it seems to me, is that we look through the document and begin to sift through it—Mr. Chambliss has raised the issue of the agriculture budget and crop insurance. Others have talked about veterans' benefits. Mr. Bass talked about special education. I am extremely concerned about what ultimately this means for Medicare reimbursements, particularly in rural America. The NIH budget, it seems to me that there is a good deal of shifting, or however we want to describe it. And then there is the big issue of the defense budget. Where it strikes me that in some respects the administration is saying, OK, we're going to hold the limit at a lid at 2.3 percent, but in a way we're going to do a little jostling so we can fund our new programs.

Let me just ask you this question: Does the President's budget reflect the requirements that the administration and the Defense Department and others are going to need in terms of our commitment to Bosnia, to Iraq, and perhaps even to Kosovo? Are those reflected at all? Are those within the budget? In other words, the real question is this: Do you anticipate coming back to this Congress sometime before we adjourn or go home this fall with some kind of an emergency supplemental to fund those requirements?

Mr. LEW. Congressman, the answer is in some cases different, so let me go through the items.

In the case of Bosnia, we did include funding in our budget, in the body of our budget——

Mr. GUTKNECHT. So, you will not be coming back to Congress for more money for Bosnia?

Mr. LEW [continuing]. That is certainly my expectation. I would just caution that we are talking about situations that are inherently fluid. But this budget is for the full year, correct.

Mr. GUTKNECHT. Assuming that nothing changes, you will not be back for more money?

Mr. LEW. Right.

Mr. GUTKNECHT. OK.

Mr. LEW. With regard to Iraq, we are working with the Defense Department on whether or not there is a need for a supplemental, and we haven't reached that determination yet. The one supplemental that we do know that we are going to be presenting is for Central America, and we hope to do that very shortly. With regard to Kosovo, I can't answer that question until policy decisions are made.

The budget includes an allowance of $3.25 billion in anticipation of, at a minimum, the Central America supplemental and the possibility that there may be others. We put in a number that was consistent with last year's budget. It was not consistent with last year's final action. And I think that we share the concern that many here share that it got a little too large last year. We think that the emergency authority remains an important one. If things happen between budgets, as a country, we have to be able to respond, but a real emergency is different than other circumstances that may test the definition.

We hope to work with the Congress to make sure that the emergency authority remains available, but we don't currently have any immediate expectations except for the Central America supplemental.

Mr. GUTKNECHT. Well, the fear of this Member is that there is the temptation already to say, well, you know, Congress is probably going to plus-up the crop insurance program. Congress is probably going to do something with veterans' benefits. We certainly need to do something to change the special education formula and live up to our commitments there. Medicare, you know, I don't know what is going to happen with Medicare. NIH, Defense, all of that—the danger I see happening is that we start off with this number 2.3 percent, but by the time it is over, the deal at the end of the day could be significantly larger than that.

Mr. LEW. Congressman——

Mr. GUTKNECHT. And it seems to me that it is the responsibility of this committee to set the overall spending limits and to do what we can to make certain that we enforce them, and that is where we need your help.

Mr. LEW [continuing]. Well, we certainly hope that we reach agreement on a broad basis, so that we move beyond the discussion of 2000 to the multi-year context.

In the case of 2000, we have a number of offsets in there, and if they are not adopted, we understand that it is going to be a difficult process working through the year.

Last year, when we got to the end, the President's class size initiative, which was a very important priority, was included in the final Omnibus with an offset. It was an offset that we worked through with the two Budget Committees to make sure that it scored. And we hope that we can work together both on a multiyear basis to have a resolution to the question of the surplus, because we do believe that there is a need for more discretionary resources going into the out years, but after we do Social Security first. Hopefully we will get to the point where we do Social Security and this gets a little bit easier.

But I agree with you, there is a need for discipline. There is a need for caps. There is a need for pay-as-you-go rules. We know where we go when we don't have any rules. We know that it is a lot easier to spend money and to give tax cuts and then afterwards see the result. We need to use the opportunity of the surplus to make some very wise decisions now and then have discipline going forward.

Mr. GUTKNECHT. Thank you, Mr. Chairman. My time has expired.

Mr. CHAMBLISS. That was a very good question, Mr. Gutknecht, and being a little bit more definitive, Mr. Lew.

And now with respect to Bosnia, the administration has Bosnia funded in the fiscal year 2000 budget, fully funded there. You have only got 6 months budgeted in the fiscal year 2001, so I am assuming that you are planning that we are out of there in 2001; otherwise we have got no money in there for Bosnia; we've got no money in there for Kosovo. So, we need to be—everybody needs to thoroughly understand that as we move into this.

Mr. Wamp.

Mr. WAMP. Thank you, Mr. Chairman, and thank you, Mr. Lew, for the relationship that you have with our chairman, and just carrying forward in a positive way. I want to say that I think Congressman Clement is onto something that this budget, from our side of the aisle, should represent a good starting point. I think that it raises the right questions, and I think that it does include some good ideas, and I would think that my friend from Minnesota is correct there.

A couple of points that I would like to make because I have learned—this is my fifth year—that you have to clear things up. You talked about the NIH funding being ahead of schedule, and let's be candid, the Republican Congress has really carried a lot of that weight over the last 4 years to increase NIH funding. As a member of the Appropriations Committee, I just want to point that out.

Also, earlier, when Chairman Kasich questioned you on the 2 percent payroll tax, I have also found that out there are across the country regular people who think that that means somehow that money would be turned back over to the beneficiary. But it needs to be pointed out every time that we talk about it, so they will understand, that the government will still control that money. The beneficiary will just direct that money. And I hope that somehow we can come to an agreement much like Chairman Kasich said, like the Thrift Savings Account for Federal employees, where you can direct where it is invested, but the government keeps the money. The government controls the money. That money doesn't go back to the beneficiary. It stays in a fund, but it can continue to grow.

There is another thing that I am a little dismayed about. I am one of the Republicans that for the last 4 years has said let's be more broad-based in our approach to tax relief, so that they can't say that we're trying to help the wealthier Americans. I am a little frustrated that, after carrying that mantra for the last 4 years and for us to propose more broad-based tax relief and then you still say that it benefits more wealthy Americans. The only way that you can really take that position is that you think everybody with a job, or everybody that is working, or everybody that is doing OK out there represents wealthier Americans. At some point we need to come together on broad-based tax relief. And I concur that the more broad it can be, the more it can affect every working American, the better off it is.

But my one question is this: On education funding, will there—and this kind of presses you, like Chairman Kasich pressed you about ever agreeing to a 2-percent payroll tax that is self-directed by beneficiaries—is there any way that the President can agree to block grant the education dollars? Because, during the Great Society the intent was to eliminate poverty. It didn't work. We created Federal program after Federal program after Federal program, and ultimately the Governors have cried long enough and loud enough for us to start block granting those same dollars, and that is working. And I just wonder if we've got to go back throughout this entire exercise over a generation of creating programs—in terms of trying to improve education, that motive and intent is all the same. We all agree that we need to improve education. But do we have to go through this same cycle again, or can't we just go ahead and block grant the money right back to State and local governments and let them spend it in a more efficient way. And is there any way that you will agree with us on that approach over the next few months?

Mr. LEW. I think that over the last several years we have made very clear how strongly we, the administration, the President oppose block granting all of the education funds. We have worked with the Congress to provide greater flexibility in many areas.

When it comes right down to it, the argument comes down to what do you want the Federal education policy to be? Do we want to be promoting the kinds of standards that the President has spoken to? Do we want to be promoting policies that are aimed at specific objectives like reducing the social promotions? This is an important part of our policy.

The question to block grant or not to block grant sounds like it is an accounting issue, but it is not. It is really a policy issue, and the President has very strong convictions in a lot of these areas. So, I think that you can expect that our opposition will be consistent with our past position.

Mr. WAMP. Let me just say one thing: If you go to a PTA meeting, you get on talk radio, you go out there where parents are involved today, they will say, please, no more mandates; please, don't create any more education programs that tie our hands—we've got people doing paperwork instead of delivering education because of the Federal programs we have created in education.

I would just submit to you, please try to work with us on this, so we can have fewer programs but more money flowing back to the schools to let them spend it as they see fit without all these mandates that seem to flow every time we come up with a new education bureaucracy in Washington.

Mr. LEW. Hopefully, we will be able to work through the Elementary and Secondary Education Act amendments to achieve some of our common goals and to reduce the paperwork. Our goal is not to be paying for administrators and paperwork. Our goal is to improve the quality of education. And on that, I think that we can agree.

Mr. WAMP. I think, Director Lew, the glass is half full and not half empty. So we have got a good starting point.

Thank you, Mr. Chairman.

Mr. CHAMBLISS. Jack, let me thank you again for being here, and I particularly thank you for having patience with us and hanging around to give everybody an opportunity to ask questions.

I hope that everybody that wanted to ask questions has come back to do so. But let me just say that if there are any members who have additional questions, we would like to submit them to you in writing, and I assume you will answer them within about 30 days or so.

Mr. LEW. It would be my pleasure.

Mr. CHAMBLISS. And we, obviously, have a lot of things that we agree on. There are a lot of things that we have a disagreement about with respect to particular issues and philosophically, but we look forward to working with you and my friend John will be in touch and dialoguing, and, hopefully, we will come up with something that is beneficial to the American people here in short order.

Mr. LEW. Thank you.

Mr. CHAMBLISS. Thank you very much.

[Whereupon, at 2:50 p.m., the committee was adjourned.]

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