THE PRESIDENT'S BUDGET FOR FISCAL YEAR 2003

HEARING

BEFORE THE

COMMITTEE ON THE BUDGET
HOUSE OF REPRESENTATIVES

ONE HUNDRED SEVENTH CONGRESS

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TUESDAY, FEBRUARY 5, 2002

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

The committee met, pursuant to call, at 2:38 p.m. in room 210, Cannon House Office Building, Hon. Jim Nussle (chairman of the committee) presiding.

Members present: Representatives Nussle, Bass, Thornberry, Ryun, Collins, Toomey, Watkins, Hastings, Doolittle, LaHood, Schrock, Brown, Putnam, Spratt, McDermott, Bentsen, Davis, Clayton, Price, Kleczka, Moran, Baldwin, McCarthy, Moore, Capuano, Holt, and Matheson.

Chairman NUSSLE. The committee will come to order.

Let me first announce, if it isn't obvious, that we have made some renovations with the committee room over the recess. As some of you remember from last year's markup of the budget, we could barely hear ourselves in the room when we were having the debate.

We put in a new sound system, a renovation that has been in the works for actually a few years. That was finally done—new microphones and sound system. I want to thank the staff and Architect of the Capitol, and a couple of private contractors that did the work for getting it done for our opening hearing today.

As members know, we had a few hearings in other rooms, and we want to thank those committees as well for letting us use their rooms while we were going through our renovations.

Just one piece of technical business. If you would like to speak, hold down this green button next to the microphone for a second. It will light up. That is your cue to start speaking. If you speak too long, I have been given a red button up here, and evidently I can cut all of you off if I need to.

I know that is the order. See, I am about to do it now. We will, of course observe the First Amendment here in the committee room.

Also, I would like to acknowledge the return of our friend Mr. Spratt, who was out. I wrote him a note just before his surgery. I told him that I know over the last year I was a pain in the neck, but I didn't realize that you had to have surgery over that. But we welcome you back. We are glad that you are back with us and feeling better.

Mr. SPRATT. Thank you, Mr. Chairman. I appreciate that.

As I lay there in my hospital bed with lots of time to think, I asked myself how in the heck did I come back with this tumor in my back? The only reason was it must have been all of these years of repression in the minority.

Chairman NUSSLE. Think of the size of the tumor that we had over 40 years.

The hearing today is of course the kickoff. Maybe I should turn to Mr. Capuano for a quick 30 seconds. At least put your hat on if you are going to be here.

Mr. CAPUANO. No, in deference of the decorum of the committee.

Mr. SPRATT. I move we allow Mr. Capuano to wear his hat.

Chairman NUSSLE. This is the opening kickoff of course for the budget season, and unfortunately I think maybe some of the laughter may leave after about the next 10 minutes. Who knows. We will see.

But this is a serious time for our country. Obviously today our country is at war. Today we cannot claim that our homeland is totally secure against future terrorist attacks. Today people throughout Iowa and throughout our country need jobs. And when it comes right down to it, when you need a job, that is the mother of all budget deficits. When you are sitting around your kitchen table and you don't have a place to go to in the morning to punch a time clock, to get a paycheck, that is the budget that really matters.

In part that is why we are here today, to talk a little bit about that budget. Our President, in accordance with the 1974 Budget Act, submitted his budget yesterday in the context of these three great American challenges. Our world did change on September 11. The question is whether we will allow those changes or those challenges to manage us or whether we will manage those challenges and those changes.

Let me be crystal clear. We will meet those challenges that confront our Nation and we will begin today to craft a budget that funds America's priorities first and secures America's future.

The President has submitted a wartime budget. He makes resources available for those three very important endeavors: To win the war, to secure the homeland, and to create jobs.

The President's budget is an appropriate blueprint to craft our response to these challenges, but it also holds accountable and measures all government spending to that balancing test of those new priorities.

The President's budget relies on reasonable sets of economic assumptions, within of course the mysterious world of economic presumptions. The budget that President Bush has sent to Congress I believe is a responsible budget, and I believe the budget is alive and well on Capitol Hill. Thank God that America's fiscal house was in good order back on September 10, so that we could address the challenges with the full power of America's Treasury today.

Today we are honored to have before our committee again the President's Director of the Office of Management and Budget, Mitch Daniels.

Let's take a quick look at what has been presented by the President. The President has prepared a wartime budget, and if it were not for the national emergency of September 11, today's budget would be a balanced budget. But you have to add it to homeland security and the emergency of September 11. You have to add to it the war against terrorism, and of course you have to add it to addressing the economy.

So what does that equal? It does equal in fact a temporary budget deficit. What do we do about that? Well, there are basically five areas that we could use to address these temporary deficits that have been suggested. There are those who have suggested that we could raises taxes or somehow gimmick the tax cut. I think that is a non-starter. We could fail to fund some of the security priorities that the President has put forward. I also believe that is a non-starter. We could use smoke and mirrors, like forgetting to put in minus signs, or other smoke and mirrors that have been tried and true in the past. The guy who forgets two pages can make fun of somebody else for a change about a little mistake within the budget.

I think the last two are really the place where we have to focus our attention in order to deal with the temporary budget deficits. We have got to grow the economy and create jobs, because I believe that is truly how we are going to get our economic house back in order, and we have to eliminate, where we can, wasteful Washington spending. Those are the solutions I believe that we need to look at.

Republicans just had a retreat, and let me report to my colleagues on the Democrat side what we have decided are important priorities. Let me just announce them to you by way of what we came up with. Those are our budget priorities.

No. 1 is obviously to win the war and fund the defense priority similar to what the President has presented today. Double homeland security funding. Stimulate the economy and create jobs. Fund America's priorities first. Hold down government spending anywhere we can. Modernize Medicare and provide a prescription drug benefit and get back to balance as soon as possible. These are the priorities and principles by which we believe we can begin to formulate a budget.

Now, I have heard over the last couple of days that there is still the rolling out of those who suggest that the tax cut somehow has gotten us to this point, and let me just comment on that briefly.

In 2002, as can you see from this chart, 72 percent of the reason why we lost the surplus is accountable to the economic downturn, 58 percent in 2003. As the next chart shows, over the 10-year period of that $5.6 trillion surplus that we saw last year, while 1.7 of it was from the tax cut, as everyone remembers, 1.6 was because of the economic downturn, and almost a trillion of it was from our spending.

Now, I say our spending, because I heard some suggestion somehow that this was Republican spending, and I went back and I reviewed the appropriation votes, and I would be glad to share those with anyone who wants to continue to call those Republican spending bills. They were some of the most bipartisan votes to pass appropriation bills that we have had in the history of the Congress. In fact for those who are wringing their hands saying where are we going to find areas in the budget to hold the line on spending, or maybe even to suggest some reduction in spending, let me also refer you to the chart that you may remember from last year.

The green bars demonstrate where we were supposed to be within the caps. The red line with the numbers shooting up $150 billion over the last 5 years alone show where we actually are. So for those who say 2 percent in nondefense discretionary spending outside of homeland security may not be enough cushion in order for us to fund our priorities, please remember that this is on top of huge increases of spending over the last 5 years.

Let me also suggest that I have heard those who have begun to use Medicare and Social Security as somehow a—I don't know—some type of a tactic within this debate. Let me read to you a quote, and then I am going to ask you to tell me who said this. "The terrorist attack against the United States on September 11 has changed the focus of Congress and the Nation. Our first priority must now be to defend against further attack. Care for the victims. Rebuild what we have lost and track down the perpetrators of those acts on terror. The world must know that our country stands united and determined to provide whatever resources are necessary to accomplish these goals. Our concern for protecting the integrity of Social Security and Medicare Trust Funds remains, but must be achieved by returning to a policy of fiscal discipline over the long-term."

Now, you might think either I said that or the President said that, but interestingly enough, that is right from the Senate Budget web site, from Senator Conrad. I join Senator Conrad in suggesting that we should not be scaring our seniors. We should not be using scare tactics. We should be honest about the fact that in order for us to get back to some level of fiscal discipline and still fund these priorities some tough choices remain. We can do so in a spirit of bipartisanship and I believe that we can still accomplish that together with the Senate.

Now, as we move forward I believe that we can craft a budget together with the Senate. Senator Conrad, I believe, has a very strong set of credentials as a budgeter. I know that if he is willing to write a budget, his first budget, that is willing to win the war, defend our homeland, and deal with the economic recession that he will find a very willing partner in the House.

So as we move forward we have to—we will win the war and secure the homeland. We will get our economy moving again. We will hold down the costs of government. We will protect Medicare and Social Security, and we will get back to balance as soon as possible, and we will secure America's future.

We need to work together in order to accomplish that. The President's blueprint is a good first step that we will be glad to work with him in order to craft. I am happy to welcome back and to turn to John Spratt for any opening remarks that he would like to make at this time.

Mr. SPRATT. Thank you, Mr. Chairman. Director Daniels, welcome to our committee once again. We are glad to have you. Mr. Chairman, let me commend you for what you have done to the committee room. I think you are going to make it a much more effective room for us to conduct business and for the public to understand our business. I am glad you got it in last year's budget because I don't think we would be able to afford it in this year's budget. But nevertheless, it is a decided improvement.

Let me begin by echoing what the chairman just said in one major respect. When it comes to waging war on terrorism, we stand foursquare with you and with the President. We are committed to paying whatever it takes to win this war, period. But we do believe that national security and homeland security don't have to come at the expense of Social Security. We can pursue terrorists. We can also pursue other priorities at the same time.

We have before us a budget that has been badly mangled by the economy over the last 12 months. We could argue all day as to whether or not we should have foreseen these conditions, which I think we were trying to suggest at the time, the storm clouds gathering across the economy, but that is neither here nor there at this point in time. It has taken a hit on the budget.

Nobody saw the war on terrorism. Nobody saw September 11 coming. It has taken a hit. But if you will look, Mr. Chairman, on page 415 of Director Daniel's budget, you will see that he ascribes 43 percent of the deterioration in the surplus to the tax cut last year and 17 percent to other legislated action.

If you add to that the repealer, the provision of the enacted tax cut last year which repeals everything in 2010, then the cost of these budget actions goes well over 60 percent in contributing to the deterioration of the budget.

If I can have the first chart, because it shows in very simple tabular form the 10-year unified budget surplus. We see what has happened in 12 months. This is the most radical fiscal reversal in American history. Just last April, as we began the budget process, we were told the surplus would be cumulatively over this 10-year period of time $5.6 trillion.

Last August, after taking account of the palpable decline in the economy over that period of time, that estimate was reduced by that amount, down to $3.1 trillion. This February, if you implement, according to our understanding of this budget, if you implement what the President is seeking here, we will take the surplus down to $661 billion. That is the unified surplus over this 10-year period of time, this same period of time. The unified surplus will drop from 5.6 trillion to $600 billion over this period of time.

Now, this is the unified surplus. Until very recently we had agreed that we would no longer look at this, but on the on-budget surplus, excluding Social Security. The on-budget surplus last April was computed to be just a tad over $3 trillion—$3 trillion, 46 billion. By August, the economy had taken that down to $575 billion.

By our estimation the on-budget surplus will be an on-budget deficit cumulatively over the next 10 years, 2002 through 2011, and each year we are taking a budget that had an on-budget surplus in it every year and converting that on-budget surplus into an on-budget deficit, the total of which will equal 60 percent at least of the accumulating surplus in the Social Security Trust Fund.

That is the extent to which we will be invading, borrowing from once again and spending the trust fund for Social Security on the eve of the biggest demographic change in fiscal history. In 2008, 77 million baby boomers will start to retire. That is what we are doing to get ready for their retirement.

We understand the need for temporary deficits to fight a war. We understand the need for temporary deficits as a kind of cyclical step against the declining and downturning economy. But we also understand the need to in the long run save, pay off debt, and provide for the commitments we have made, keep our promises to American citizens and some of the most fundamental programs that we have got, Medicare and Social Security. We just don't see those promises being upheld in this budget.

Indeed, as I read through the budget, and I haven't read that much of it, but I really don't see where in the long run there is any effort to restore to that path that we were on so recently when we were all saying we won't spend another dime of the Social Security Trust Fund, where we were all saying, vying to see who could pay off the national debt the fastest. There is no sense that that is an objective worthy of reinstating, deferring sure, for the short term at least, past this recession, past the hump in this war, but at least having some kind of strategy built into the budget where we recover and return to that as an important policy objective.

If it is in there, if the implementation is in there, I would like to know about it, because I cannot find it in there myself, Mr. Chairman.

We have got other presentations to make, and I don't want to encroach on the Director's time. So I am going to end basically at that point, but also by emphasizing once again that there are going to be parts of this budget that we support, no question about it. We are going to support the parts that have to do with fighting the war on terrorism and protecting the American homeland. We are going to ask for justification. We are not going to be stinting. We are not going to nickel and dime you, but we have got a job to do.

We are going to raise a debate, too, as to whether or not it is right, proper, and fair to use the surpluses in the Social Security Trust Fund to pay for the war, to pay for homeland security, is this the proper means of financing it. We can raise that argument, which I think is a debate we should have, and at the same time support what you are seeking, but question whether or not the means by which we would finance much of this is the way we should go.

Thank you very much, Mr. Chairman, for the opportunity, and, Mr. Daniels, we look forward to your testimony.

Chairman NUSSLE. Thank you, Mr. Spratt. Without objection, all members will have 7 days to submit written statements for the record at this point.

[The prepared statement of Mr. Bentsen follows:]

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

I am pleased that the House Budget Committee will have the opportunity to question Office of Management and Budget (OMB) Director Mitch Daniels, as well as Congressional Budget Office (CBO) Director Dan Crippen about their new economic forecasts released during the August District Work Period.

Today is not about assessing blame. It is about the Congress and the White House coming together to evaluate these new forecasts and begin appreciating their ramifications with respect to the President's domestic and foreign spending priorities. I am stunned at how much the Nation's fiscal picture has changed in four short months. Recall that in April, the OMB surplus projections were $281 billion for this fiscal year and $3.4 trillion for the next 10 years, which they portrayed to be more than enough to fund Bush's tax cut and new spending initiatives, while staying the course on debt reduction.

Today, our Nation must come to terms with a new fiscal reality. By OMB's own admission, $123 billion of this year's surplus had somehow vanished, leaving a $158 billion surplus, almost entirely made up of Social Security tax receipts. We now expect that in fiscal year 2001 alone, all of the Medicare Trust Fund ($29 billion) and $9 billion of the Social Security surplus will be consumed to fund government operations, according to the CBO, the Congress' official budget analysts. Moreover, looking ahead, the CBO estimates that all $170 billion of the Medicare surpluses and $30 billion of the Social Security surpluses will need to be diverted to meet our current obligations over the next 5 years.

At this critical juncture, with much of the appropriations process still ahead, it is vital that President Bush identify where spending will be cut in order to make room for his initiatives, including a $18.4 billion boost to defense an enhanced Federal role in education as well as Medicare reform. Will farm subsidies have to be slashed? What about tax credits for the working poor or housing programs? What about prescription drugs? What about the missile defense shield?

Additionally, I am growing increasingly concerned about recent statements from Congressional Republicans that signify an about-face regarding Congress' commitment to protecting the Medicare Trust Funds. On four separate occasions over the past 2 years, the Republican leadership has shepherded legislation to the floor that not only dedicates the Social Security surplus but also the Medicare surplus to debt reduction. At this time of weakened economic performance, I am deeply concerned by the apparent willingness of Congressional Republicans' to retreat from their commitment to paying down the national debt. This departure from the path of debt reduction, in addition to the "incredible shrinking surplus," perpetuates economic uncertainty within the financial markets, potentially doing real damage to today's sluggish economy.

Finally, it clearly appears that the President and his allies overcommitted and cut the budget and fashioned the tax cut too close to the margin on the basis of overly optimistic economic assumptions. Now, the President's budget has us borrowing against Social Security and Medicare, increasing our long term public debt and leaving not a penny for fixing those programs.

I am eager to hear where the administration plans to make the budgetary adjustments to meet our current obligations and their own spending priorities while adhering to the Congressional mandate for debt reduction and protection of the Social Security and Medicare trust funds.

[The prepared statement of Mr. Holt follows:]

PREPARED STATEMENT OF HON. RUSH D. HOLT, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW JERSEY

Mr. Chairman, yesterday, the President submitted his budget to Congress. While we are all still trying to put our arms around more than twenty-five hundred pages in four separately bound volumes, I was happy with many of the President's proposals and disappointed with others.

As OMB Director Daniels stated, the President's $2.13 trillion budget proposal will run a $106 billion deficit—the first deficit since 1997—and will continue to spend Social Security and Medicare dollars until 2005.

What does that mean for this committee and for Congress? We are going to have to make some difficult choices this year, and we are going to have to work together to question the return on every dollar the Federal Government takes in and spends.

Obviously, the war against terrorism, our homeland defense, and our economy should be our first priorities. These priorities are not in dispute-I think it is fair to say that every Member of Congress shares in these concerns.

I would, however, challenge my colleagues to make investment a priority in the 2003 fiscal year as well. The best way to stimulate is to invest, and I believe we have an opportunity to enjoy high returns by prioritizing the education of our children and research and development.

I was pleased to support the bipartisan "Leave No Child Behind" Act. And, in many ways this budget represents the President's commitment to education. However, this budget comes seriously short in other respects. While the budget calls for a 2.8 percent increase in education spending, this is below the rate of inflation. Moreover, hidden within this small increase is over $84 million in cuts to the bipartisan education reform the President signed into law just a month ago. I understand that Congress must restrain spending, but every dollar we invest in our children will certainly return many more dollars in the future.

I was also happy to see the President's commitment to the National Institutes of Health, which enjoyed more than $3.9 billion in proposed spending increases. While overall investment in research and development is up by 14 percent, this statistic largely represents defense development. Civilian, non-health research and development would increase by only one-half of 1 percent, far below the level of inflation. Moreover, even though the National Science Foundation was identified by Director Daniels as a model agency only 3 months ago-described as one of the "true centers of excellence in this government" for its low cost and efficient use of tax dollars-the National Science Foundation received only a one and one-half percent increase.

We have many difficult choices to make this year. However, I hope in our effort to question priorities and eliminate waste that we do not eliminate investment in our future-our children, technologies and medical breakthroughs that will enhance every American's way of life.

QUESTION SUBMITTED FOR THE RECORD BY CONGRESSMAN HOLT FOR DIRECTOR DANIELS

I was pleased to see that the President proposed more than $27 billion in funding for NIH, including $1.75 billion to combat bioterrorism. NIH funding has improved America's overall quality of life and led to new and innovative cures and treatments for some of humanity's most devastating ailments. Yet, I was disappointed to see that civilian, non-health research and development would increase by only one-half of 1 percent, far below the level of inflation. Moreover, even though-in an appearance at the National Press Club only 3 months ago-you identified the National Science Foundation as a model agency, describing it as one of the "true centers of excellence in this government" for its low cost and efficient use of tax dollars, the National Science Foundation received only a one and one-half percent increase.

Can you explain why the President has proposed funding well below the rate of inflation for this agency, particularly considering the many practical research and development programs in NSF's jurisdiction? And have we formally rejected any plan to double the funding for NSF?

No response was received from OMB at time of publication.

Chairman NUSSLE. Director Daniels, welcome back to the House Budget Committee. Last year, when you testified here, one of the things you mentioned, and I was pleased to see within your budget blueprint, is that you wanted to put the "M" word back into OMB—management—and I see that throughout the document, and I want to commend you on that, we welcome you back to the committee, and you may proceed as you wish, and we look forward to your testimony.

STATEMENT OF MITCHELL E. DANIELS, JR., DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

Mr. DANIELS. Thanks, Mr. Chairman, and Congressman Spratt in particular, glad to see you back.

Mr. SPRATT. Thank you, sir.

Mr. DANIELS. I have been doing it a little differently. Instead of doing these hearings on consecutive days, I took batting practice in the lower body this morning. So with your permission I would like to follow my usual practice and abbreviate as succinctly as I can the testimony which I have submitted for your inspection. Let me just highlight a few things from it, which will in part respond to comments each of you just made.

The President submitted to the Congress this week a budget to win a two-front war. It asks for spending quite honestly in excess of what we would have under normal conditions, larger than what we requested last year and agreed upon with the Congress. It includes a request that in the aggregate would lead to a temporary deficit, something else we would vastly prefer not to do, but the President has been pretty forthright about his priorities and his belief that there are certain specified circumstances, war, recession or emergency, all of which exist today, which can justify temporary deficits.

I wanted to associate very strongly with the comments of Congressman Spratt that returning to a path of surplus and further reductions of our national debt is a very appropriate and important goal. We did attempt to speak to it in the budget and if it is not manifest, we will make it more so. But it is our belief that if the economy comes back, and the sooner the better, that we can get back on a path where we not only can fund the needs of warfighting and defense, but also begin to balance and further reduce our national debt, and you are right to keep that objective in front of us. There are very few things more important to this President than balanced budgets and debt reduction, but we have a couple of tasks at hand that are more important.

I would simply say beyond this that we got to keep our heads about the situation we are in. The chairman's statement, I thought, was right on target. Thanks to the efforts of members of this committee and many of your other colleagues, we arrived at this recession and then at this conflict in very, very strong fiscal position. The result is a deficit, yes, but the smallest one we have seen in any recession in the post-war period, a deficit that is far, far smaller than that being experienced right now by all of the other developed countries of the world. And this deficit is small in dimension despite the fact that we have a war and the costs of that war overlaid on top of it. So we ought to count our blessings in some respects for the kind of situation that we do find ourselves in.

I want to say one other thing. Congressman Spratt spoke of a radical reversal, and so forth. But here too we need to keep a level head. We really don't know, and can't know what the next 10 years hold. We have made a brave attempt over the last 7 years in what I would characterize as a failed experience to tell us ourselves with any kind of confidence what our surplus or deficit will be over that stretch of time. As the last year just reminded us, we can't even do that over a 1-year period, let alone 10, and there is every possibility that we can be meeting here next year with even higher surplus forecasts than the ones we looked at last year.

I will simply point out to you that even with all of the changes that we have experienced, the $2.9 trillion, 10-year baseline surplus that we now see is the biggest we ever had except for last year's. Was last year right? This year wrong? Was last year wrong and the year before that right? We just aren't going to know for years. What we need to do is make the best decisions for the benefit of the Republic on a year by year basis, always with an eye to the future.

But I appreciate the Chair's pointing out that this submission deals in a different way, possibly a little more serious way, with the issues of how the Federal Government is managed. We assert that that was something that needed doing in any event, but is essentially urgent now that the priorities of national defense, defending Americans in their homeland and restoring the economy to strength through an economic growth package have first, second and third claim on our resources.

I appreciate as always the opportunity to be here, and I am eager to answer your questions.

[The prepared statement of Mitchell E. Daniels, Jr. follows:]

PREPARED STATEMENT OF HON. MITCHELL E. DANIELS, JR., DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

Mr. Chairman, my colleagues at OMB and throughout the executive branch have worked hard to present this committee and our fellow citizens with a very different budget for the fiscal year 2003. Before turning to the traditional subjects of totals, balances, and specific policies, let me recommend to the committee's attention some new features which I hope will now become part of your annual expectations and deliberations.

This budget takes seriously the assessment of government performance, and its relationship to future spending. Activities where effectiveness can be proven are maintained and often reinforced; those that demonstrably fail, or can make no showing of effectiveness, in many cases are looked to as sources of funding. The days when programs float along year after year, spending taxpayer dollars with never a showing of reasonable results or return, must give way to an era of accountable government. This and all future budgets must no longer be permitted to answer only, "How much?" They must also address the question, "How well?"

This innovation responds to decades of calls by good government advocates. While long overdue, it is especially necessary at a time when the physical safety of Americans requires that the Federal Government take on many additional, expensive tasks.

In the interest of both accuracy and sound management, this budget takes a major step toward full cost accounting of programs and departments by assigning the costs of health and retirement benefits to the places where those costs are created. At long last, the true cost of these programs will be visible, and managers will have full incentive to control the costs of additional personnel. Other disguised costs, such as the future liability associated with hazardous waste, remain and should be the object of further reforms.

THE UNEXPECTED COST OF THE RECESSION

It has been clear for months—since September 11 to be precise—that our fiscal picture had changed in a fundamental way. The weaker economy erased $177 billion of revenues previously expected for 2002, and $120 billion for 2003. Additional spending to respond to the terrorist attacks in these years subtracted another $31 billion from the surpluses we all had anticipated. Over a 10-year period, for those still professing to find use in such numbers, changed economic and technical factors reduced the surplus by $1.345 trillion.

The recession that began in the first quarter of 2001 was the largest but not the only economic factor reducing estimated surpluses. The revised outlook for near-term productivity growth reduced the level of GDP—and hence the receipts base—throughout the budget window. Both the recession and the impact it has had on budget surpluses took us all by surprise.

As the Washington Post has noted, "2001 was a nightmare for economists," pointing out that, almost without exception, forecasters failed to see recession or its effects coming. In our misjudgments, our economists were in large and renowned company. The good people at the CBO, and 51 of the 54 private forecasters in the Wall Street Journal survey, all missed the recession even as it was well underway. The fact that our assumptions were toward the conservative end of the forecasting spectrum did not protect us from a very large misestimate. May I add that when the nation's economists are having nightmares, budget directors lose sleep, too. We ultimately must choose assumptions that we believe will be accurate, and it is no comfort later that the rest of the world was in error, too.

The administration stated from the outset that it would leave room for error, particularly when it came to longer-term projections. In mapping out long-term policy proposals, our Blueprint expressly marked off over $800 billion (15% of the total expected) as a contingency reserve in the event that the hoped-for surpluses did not materialize. At least as far as one can tell from the latest 10-year estimate, even this generous hedge was not enough.

The 2001 experience casts further doubt on the entire idea of 10-year budget forecasts. The attempt to see 10 years out began only 6 years ago—prior to that time 5-year forecasts were the longest ever attempted—but already enough evidence is in hand to convict. The experiment with 10-year forecasts demonstrates that no one can reliably predict budget levels this far into the future. In fact, despite all the lamentations, this year's 10-year baseline surplus forecast is just as big as that of 2 years ago; even after tax relief, it is the largest ever except for last year's. If we had taken a 1-year timeout from 10-year guesswork, no one would say that anything was "missing."

Our budget extends 10-year forecasts at the top-line level, for those still determined to find them credible, but it drops them from the rest of the document. There we return to the wisdom of our predecessors by using 5-year numbers, which are plenty uncertain in their own right.

A TWO-FRONT WAR AGAINST TERRORISM

Mr. Chairman, we present this week a budget for a two-front war. It proposes substantial increases, those the President believes necessary to deliver on the paramount duty of the Federal Government, to secure the safety of the American people.

Last year's budget began the reconstruction of a neglected national defense base, and that project continues now with new urgency. The President asks Congress to support a 12% growth in base defense funding, part of this reflecting the new threats presented by a long-term terrorist foe. He also requests an additional $10 billion, if needed, for the costs of continued hostilities at today's levels.

Funding for the category of activities we now term "Homeland Security" will double under the President's plan: airline security, first responders, bioterrorism, border security and preventive law enforcement, are all scheduled for major increases as recommended to the President by Governor Tom Ridge.

We have worked closely with the Office of Homeland Security to define and budget for these activities; an explanation of the definition of the Homeland Security budget is attached at the end of my testimony. We will guard against and oppose efforts to divert funds from Homeland Security requirements or to misclassify unrelated funding under Homeland Security's priority status.

Winning our two-front war is not optional, and will be expensive. As in other times of national conflict, tradeoffs will be required. Other priorities will have to stand aside for a time, lest we commit the "guns and butter" mistake of the Vietnam era. We propose a very reasonable level that allows spending not related to the war or homeland defense to grow by around 2%.

Within this "Rest of Government" category, the President proposes $355 billion of spending. It must be noted that the activities it encompasses have enjoyed rapid funding increases during recent years, growing by an average annual rate of more than 8% since 1998.

Within this enormous sum, it is both possible and desirable to increase high priority programs of proven effectiveness, and this budget recommends many such increases. Dozens of programs across the government are scheduled for growth based on demonstrated results.

MEASURING PERFORMANCE AND DELIVERING RESULTS

For decades, good government advocates have called for systematic measurement of government's performance, and its reflection in the allocation of resources. In 1993, Congress passed the Government Performance and Results Act (GPRA), which was intended to implement this reform, but this mandate has been virtually ignored. The President's budget for 2003 responds to Congress' instruction, differentiating where the facts are available between programs that work and those that do not.

Many programs of proven effectiveness are strengthened, by shifting funds from those which can make no proof of performance. NSF, WIC, Community Health Centers, and the National Weather Service are among the best performers, based on clear targets they have set and hard data that says these goals have been met or surpassed.

A serious attitude toward performance is long overdue, but takes on special urgency at a time when the demands of national security assert a heavy claim on our resources. We hope the findings of this budget will trigger interest in performance assessment, and bring forth much new information about that large majority of programs for which we have no useful data at all.

RESTORING ECONOMIC GROWTH

This budget funds a two-front war, but takes aim at a third priority as well, the struggling American economy. The President urges the Congress to act, and act quickly, on a jobs and growth package like that which passed the House but was blocked in the Senate just before Christmas.

There are some encouraging signs of recovery, but the President is not satisfied to leave matters to chance. Government cannot "manage" the economy, but it should do what it can, and the President wants to act on a stimulus measure that might accelerate and strengthen recovery. While adding this action to his other budget proposals would likely make 2003 a year of a small deficit rather than a year of small surplus, the President favors the tradeoff in favor of jobs and growth. Past the short term, it is only rigorous economic growth that can restore surpluses in any event.

CONCLUSION

In sum, we should count our national blessings. Despite simultaneous war, recession, and emergency, we are in a position to fund the requirements for victory, plus a stimulus package, and still be near balance. The deficit we project will be the nation's smallest in times of recession since the early 1950's.

Interest costs to the Federal Government will continue to decline; interest payments will fall below 9 cents of each budget dollar for the first time in 22 years. Despite everything, the outlook is promising for balance in the year after next, and for a return to large surpluses thereafter.

The President's proposals thus do what must be done, while protecting our fiscal future. It is a privilege to submit them for the committee's review.

Chairman NUSSLE. Thank you, Director Daniels, for your testimony and for the budget submission.

Let me direct your attention to the one area in particular that has caused some question as we try and deal with the next 2 years in particular. The Congressional Budget Office has submitted their economic factors and their projections as to what may or may not bode for the economy in the near future: Revenue projections, technical assessments about that.

There is about a $65 billion difference between OMB and CBO in this regard. This is a pretty big difference. There are some that suggest that while your economic factors are a little bit more pessimistic than CBO's, your revenue projections are a little bit more optimistic and that has contributed to these big differences. Obviously, as we are trying to get back to some form of balance, as quickly as possible, meeting those priorities, that big difference is going to be—is going to loom out there as we are trying to land that 747 on the runway, as small as it may be.

Would you comment on the differences between the economic factors within your proposal and what you know CBO to have been proposing?

Mr. DANIELS. Sure, I will. The $65 billion difference was a little bit of a surprise to me. We have worked closely with CBO. We see no advantage to the Congress in having to wrestle with starting points that are materially different.

About a third or more of the difference is explained by the fact that they included in their baseline the emergency spending you voted for last fall and we did not. So that alone narrows the gap to something closer to maybe $40 billion.

Much of that emergency spending is part of the new request that we have asked for. We have asked for it where Governor Ridge, for example, believes it is necessary, not where in the rush and the haste of last fall that $20 billion was placed. So that is a starting point differential that does leave a gap on the revenue side. It surprised me because, as you pointed out, we have what some people feel are perhaps unduly pessimistic economic assumptions here. I confess that I am trying to get to safe numbers, and I think probably we have accomplished that. We have growth this year of 0.87 percent. Some people think that that looks like pretty low growth over the 2-year period. That is right consistent with the private Blue Clip Index and a little bit below CBO.

That notwithstanding, their revenue expectations came in a little bit lower than ours. We will have to see which is right. I think the biggest factor, as far as I can tell, is they assume almost no snapback in terms of corporate profits and therefore the tax receipts from that.

But when you factor for their inclusion of emergency spending in their baseline, you are down to about a 2-percent difference, and I hope that this is something the Congress will not find confusing.

Chairman NUSSLE. Would you give us your thoughts and the President's thoughts on the issue of Social Security and Medicare? I mean my sense from talking to my constituents who are seniors—these are seniors, by the way, who fought and won—I even have a few of them left from World War I—fought and won World War II, fought in Korea, and there is even a few that are looking at retiring here shortly who had some experience in Vietnam. And what they tell me is that now is not a time to worry about putting green eye shades on. Now is the time to win the war and secure the Nation.

Having said that, Mr. Spratt has brought up, and others have brought up the question of Social Security and Medicare. How are those issues addressed by the President in this budget? How can we get back to some form of balance in the near future so that we can again begin to pay off the national debt and prepare for that time when Social Security will be a much bigger challenge within this budget, probably in about the next 5 to 7 years?

Mr. DANIELS. I think the commitment to Social Security and its promises is the most solemn one and the most bipartisan one I know of, and there need be no doubt on where the President is on these issues. Again, this year every penny of benefits will be paid, and the trust funds will grow by every penny that they are entitled to. And you know, the issue that perhaps we will debate has to do with what is to be done with the extra revenue that temporarily, for the next several years at least, will come into the Social Security system. And one option of course is to use it to pay down debt.

That is what we have done when we have had the opportunity. That is what we look forward to doing again. Temporarily there are higher claims on that money, and it will be used not to pay down debt but to pay the cost of the war, the cost of homeland defense and the cost of reinvigorating the economy. We can run a surplus this year. I have got a chart to show you on that. This choice, certainly on the OMB baseline—this goes to your previous question—but we clearly have this choice.

We can have a $51 billion surplus this year, use those dollars to further reduce our national debt. But to do that we would not be able to strengthen our national defense as the President has proposed. We would not be able to strengthen our homeland security as the President has proposed. It gets you to the second bar from the left. You would still have a surplus.

The rest of government that we have growing at 3 percent—or, I am sorry, 2 percent, could do that and still leave you at a rough balance. The largest contributor to this segment, by the way, is the farm bill that we believe Congress will finally enact.

Then you have one last choice, whether to pass an economic growth or stimulus package or not. The President's view is that

that should occur, we should not take a chance on the basis of a few encouraging signs that the economy is coming back strong enough and quickly enough, and therefore he continues to hope that the Congress will pass a bill like the one that the House passed and the Senate almost passed in December. I happen to think that would not only be the right thing for America's workers, those who are out of jobs now or whose jobs may be in jeopardy, but also the right thing in terms of the long-term fiscal strength of the country.

To go back to those long-term projections and the wild fluctuations that they go through, the decisive dominant variable is always economic growth, and the sooner we return to a path of strong economic growth, in the 3 and 4 percent range, year on year, the sooner we will be back here debating how much debt we can pay down, as we would like to do.

Chairman NUSSLE. And that is the X factor that was reported to us by the CBO Director as well. That economic growth is X factor in the long-term solvency of Social Security. If we have economic growth and it is vibrant and growing, the solvency lasts much longer in the Social Security system, is achieved for a much longer period of time than if we don't have a growing economy. So the choice for Social Security is not only a strong country and a safe country and winning the war on terrorism, but it is a growing economy.

Mr. Spratt.

Mr. SPRATT. Mr. Chairman, let me share a couple of quotes. You are sort of asking is this still the doctrine of this administration? George W. Bush said, "every dollar of Social Security and Medicare tax revenue will be reserved for Social Security and Medicare." I don't think you can say that now. I understand why not now. But the question I am asking is, where do we go from here? Is there some time in the foreseeable future when this doctrine, this value, this policy can be said to have primacy again? If so, where is it? How do we get back to this path in the budget you are presenting us?

Mr. DANIELS. Well, sir, it could be as early as the next couple of years. The estimates that allowed us all to think in terms of sustained on-budget surpluses, we had never seen anything like it before last year. What we see now, as I pointed out, is as good as anything we saw before. I can't tell you what course the war will take, whether the levels of spending we now need to undergo will continue for a long time or not, but they might. I have to tell you that we do believe the new costs of homeland security are probably a permanent fact of life, that the two oceans are no longer enough to protect Americans and that, sadly, these new dollars are likely to be a part of our budgets on a long time basis.

Again the thing that matters most and really the thing that dwarfs everything else as a factor here is how fast the economy comes back and therefore how fast revenue growth comes back.

You know, as those statements were being made the economy itself was taking us well below the Social Security or on-budget line. If we had not increased spending at all last year, if there had never been any tax relief, we would still have been well below the Social Security line last—or this year and next. So it is the economy that matters most, and let's hope that the signs we are seeing now are real.

Mr. SPRATT. Well, once again the concern we have is not where we are. We can't do much about that now, but where are we headed and where are we going, and can we expect to get back on this path that we thought was a noble pursuit for us; that is, to pay down the national debt, to prepare for the retirement of the baby boomers, and to increase national savings. We seem to have lost the path, and I just can't find the route back to it in the budget you have got.

In addition to the fact that these substantial increases in defense and homeland security are likely to be recurring, they are not going to be one-time increases, they will be pretty well institutionalized, built into the budget in the future, they will add to a lot compounded out to the future, particularly if you adjust them for inflation.

In addition to that, you are seeking over $600 billion in additional tax reduction in this budget this year. When you put those two things together, an enormous increase in defense spending, a huge increase in homeland security, and a sizeable additional tax reduction, $600 billion worth, what happens? How do we get back without some kind of really rocket comeback in the economy to the halcyon days of the mid-1990's?

Mr. DANIELS. Well, sir, the spending increases you are talking about do occur this year. When you talk about tax reductions, you are talking about something 10 years or 9 years in the future. Perhaps it would help the committee to be reminded of that.

Even after tax relief, the tax relief passed last year, revenues will be growing up very substantially over this time period. I hope, frankly, that economic growth comes back sooner and stronger and that even this is understated.

The second point made here is that the amount of tax relief provided by the Congress last year is relatively modest, and much of it will not happen for a long time. Only about 24 percent of the tax relief will occur in the first 3 years, only about 40 percent in the first 5 years. So for those who believe that this is an undertaxed society and an undertaxed economy, there will be multiple chances long before this tax relief takes effect, lots of chances to make changes.

Mr. KLECZKA. Could I ask a quick question? Are FICA taxes part of the blue line, Mr. Director?

Mr. DANIELS. These are total revenues.

Mr. KLECZKA. So what percentage of those lines would be the FICA tax? We saw a similar chart this morning at the Ways and Means Committee, and interestingly enough a big chunk of that is FICA. So you can't say that all of that is for general purpose spending.

Mr. DANIELS. Well, it would be around a third, but let me just pursue the point a little bit. Even after tax relief we are taxing the American economy and the American taxpayer at some of the highest levels in history, well above the post-war average, which was right around 18 percent. This is after tax relief. The tax relief was necessary to keep this from skyrocketing even further.

Now we can have an honest debate about whether more should be exacted from Americans, but it is important to keep things in perspective. Ours I would assert is not an undertaxed economy and we have got to be very, very careful letting taxes get to a point where they might choke off growth. Without that growth we don't have a prayer of getting back into surplus. And to your point, which is an important one, we need to bear in mind that different sources of our revenue, we are taxing Americans after tax relief at record levels, and this is individual income taxes.

So quite apart from the payroll taxes, we are continuing to raise now between 9 and 10 percent in income taxes, individual income taxes, out of every dollar this economy generates.

Mr. SPRATT. Mr. Daniels, if I can get back to the line of questioning we were following. I don't have your numbers for projected deficits every year over 10 years. But we do have the numbers that CBO gave us, and I don't know how much you deviate. There is before any of the policies you implement, spending or tax reducing according to this chart, which is the CBO summary, table No. 2, every year under current services, every year from 2002 until 2009 there is an on-budget deficit. Every year. Last year it was an on-budget surplus. This year, every year is an on-budget deficit. The question I am asking is if you add to that $600 billion in tax reduction and the substantial spending increases for defense, national defense and homeland defense, how in the world in this 10-year time frame do we ever get the budget back into on-budget surplus?

Mr. DANIELS. Sir, we get there if and only if the economy is very strong. When we met here in August, tax relief was already a reality. It was part of the numbers. And we saw long-term surpluses over 3 trillion, and we saw on-budget surpluses. It is the economy, and the recession, which we were only then beginning to discover, was already on top of us, as well as some other economic factors. One of them that is in many models is what might be viewed as a terror attack; that is to say, the assumption that there will be somewhat higher nonproductive costs in the American economy to protect us from the threats that are now so evident.

A lot of debate about whether we had overestimated productivity in that one very large estimate of last year and whether it was already running at a slightly lower rate, and whether it will run at a little bit lower rate still. So it is the economic factors that will dictate the outcome. That is another reason that we hope the Senate will join the House in passing the set of measures that would get this economy roaring again soon.

Mr. SPRATT. Two more quick questions, and I will turn you over, because I am taking a lot of time. But quickly, when do you expect to ask for an increase in the statutory limitation on the national debt, and what do you expect the national debt to be under your policies if your policies are implemented in this budget at the end for year 2011?

Mr. DANIELS. I would expect to request for the increase in the debt limit to happen in the next 2 months, probably be necessary to have that task taken care of by March some time. That is the advice that we have from Treasury. And we would see a debt—did you say at the end of the time period?

Mr. SPRATT. 2011.

Mr. DANIELS. And were you asking about public debt, sir? Debt held by the public? It is a little lower than I thought—2.6 trillion.

Mr. SPRATT. By that point in time. I referred earlier to a chart on page 415 of your budget, I think it is table No. S16. If you have that handy, I just want to clarify.

Mr. DANIELS. Yes.

Mr. SPRATT. In any event, by my arithmetic, using your numbers, looking at the April pre-policy baseline of $5.6 trillion cumulative surplus over 10 years, declining to $665 billion, now, including the economic security plan, you attribute 1 trillion, 478 to tax reduction, and almost $600 billion to other legislative action, which is other budget action, mainly spending action.

I think my arithmetic is that is 43 percent, 17 percent due to other budget action so that 60 percent of the deterioration in the $5.6 trillion surplus over the 10-year time frame is due to legislated action to date, including the tax cut?

Mr. DANIELS. That would be correct. I guess I would point out, as we did last year, that when you are anticipating running gigantic surpluses of that kind we thought it was only just, as well as economically smart to share a significant portion of that with the American taxpayer who is producing the revenue.

Mr. SPRATT. Thank you very much.

Chairman NUSSLE. Mr. Bass.

Mr. BASS. I have got a few things to work out with the sound system here. Thank you, Mr. Chairman. Thank you for coming, Director Daniels. I am sure that you agree, as will everybody on this committee, that statements made almost a year ago, that were basically agreed to by everybody, are subject to some review, understanding what happened to this country in September, and that we all agree that national security and homeland defense has to be the top priority of this budget. I suspect that you would also agree, having now been around for a year or two, and some of us having been around for 6 or 7 years now, that trying to pin a debate on a budget estimate that is 7, 8, 9 or 10 years out is about as accurate as trying to forecast the weather 7, 8, 9 or 10 days from now. What really matters is what we do in the next 12 months or 24 months.

Clearly the money that we are proposing to spend on defense and homeland security is important. Some of the other priorities that you have outlined in your budget are equally as important. One of the biggest issues that will be debated, and I think perhaps my friend on the other side of the aisle alluded to this, is whether or not in a time of potentially recovering economy whether or not the administration will be willing to continue to consider the need and/or the scope of the economic stimulus package as we try to debate the issue of whether or not we have a deficit in fiscal year 2003, wanting to have strong economy, versus getting closer to balance, if the economy appears by most people's judgment to be headed to recovery anyway.

Do you have any comment on that?

Mr. DANIELS. Well, Congressman, I think it is not an open and shut call, because balanced budget, surpluses, debt reduction are goals that we I think all share, and we are eager to get back there as fast as we can. The President, weighing this against the opportunity to try to do something to ensure swift and vigorous recovery, opts for the latter. And as I pointed out, although it would add to a little temporary red ink, over the long haul it may prove to be the best money we can spend, certainly if you are out of work today I think a trade-off that you would prefer the President and the Congress make. I would also submit that if you want to see those large surpluses return soon, as we do, that it is pretty good policy in that regard, too.

But I acknowledge it is a close call, and as the chart I put up a little while ago shows, frankly, I think to an astonishing extent in a recession and a war we are very, very close to balance anyway, and no other country I think would find itself so well positioned. In fact, it is a better position than this country has been in in previous recessions.

Mr. BASS. I agree with you, Director Daniels. I yield back.

Chairman NUSSLE. Mr. McDermott.

Mr. MCDERMOTT. Thank you, Mr. Chairman. I always look forward to reading the newspaper in the morning. I learn interesting things. I have been reading some of your editorials. I am glad to see you here today producing a no-pain, no-gain budget. In the athletics I participated in it was always the feeling that if you didn't have some pain, you weren't getting anywhere. I look at the way you keep blowing smoke like you did the last time when you told us that the estimates were probably too low, that they would be up higher when it was all over. Now, I picked up the two papers this morning, if you put that slide up, No. 10.

The Wall Street Journal says, "Bush offers trillion dollar budget, launching era of deficit spending," and on page 8 in the Los Angeles Times it says, "Budget sells Social Security down red ink river." Included in that is the graph which is on the board, and I would like to make a point.

This business of being able to fight a two-front war. Right there is where Mr. Reagan cut taxes. That was the last time we had someone trying to fight a war and cutting taxes. You can see the direction of the line. You don't have to be an economist or anybody fancy to see what happens when you cut taxes. You don't provide the money, and then you have a military buildup.

Now this is the Clinton years as we worked our way out of the problem. And hardly Mr. Bush gets in again and he says, let's build up for a two-front war and we can cut taxes another $600 billion.

Now, this morning, I had the pleasure at the Ways and Means Committee, with Mr. Kleczka, of hearing the Treasury Secretary, who told us, No. 1, that we were passing this $600 billion tax cut now so that we could kind of sneak the estate tax repeal out. So we don't have to ever worry about that. He said there would be a lot of financial planning that would change, because people would have their money and would keep it forever. Then he told us that we were going to borrow from Social Security.

I would like to put the next slide up, No. 8. This is what the Los Angeles Times is talking about when they say Social Security is down the river of red ink. If you look at that first blue line there, if you had not made the tax cut, this is where we would be at the end of 10 years.

But you insisted, no, no, no, we have to do this. We have to make this tax cut to make this economy run. In 10 years we will just barely be up a little bit. And now you come in to us with a budget that says we are going to be in Social Security for as long as the eye can see. I don't know where you put that, how far out on the wall before you get out of using Social Security.

The reason that is important to us is that there are thousands of people in Houston, Texas and around this country who have been working for a company called Enron. Today they have nothing, nothing but their Social Security check in the future.

United Airlines, Sunday, they are talking about the fact that they are going to perhaps go into Chapter 11. The reason that is going to be real difficult is because it is an ESOP and all of the pilots' retirement money and all of the mechanics' money is in the corporation. If they go into a Chapter 11, they will have nothing but their Social Security money.

And everybody in this country knows that right there, 2008, 80 million people are coming onto Social Security, and you are deep in the surplus because you want to put a tax cut on the budget.

Now all of this nonsense we hear about we want to raise taxes. If you call taking the repealer off and taking $600 billion more out of the budget a tax cut, you have not heard the country saying that when you are in a deep hole the best way out of it is to stop digging. This budget is simply digging the hole deeper, and you simply are being irresponsible in planning for those people coming on Social Security.

Now I am drawing mine, thank you, but all the rest of you who aren't, you better be wondering about what is going to be going on in 2010, because my kids are going to have to pay for it. They are going to have to dig us out of this hole, and so is everybody else in this room.

So I think this budget is really fraudulent. I want to know when you are going to stop. What is your plan to get that line to come up out of the red? Where is it?

Mr. DANIELS. Thank you, Congressman, for those gracious comments.

Mr. MCDERMOTT. Thank you. You are welcome. I will have more for you.

Mr. DANIELS. Well, in the first place I would ask you to please share your impressions with us in the future. If you can tell, as you assert you can, what will be going on in terms of Social Security, in terms of Social Security 7, 8, 9 years from now, I wish you would have told us that September 11 was coming.

Mr. MCDERMOTT. We told you in April that you were skating on very thin ice.

Mr. DANIELS. You know the simple fact is that one of the reasons that much of the spending that has to occur now is required is because the peace dividends of the 1980's was cashed in two or three times over in the 1990's. So almost all the Congress succeeded in cutting in those years, and therefore there is an awful lot of rebuilding to do. This was the case even prior to the onset of the terrorist war and wherever that may lead us.

The idea that we need higher taxes, that somehow this is the best way forward, either for a strong economy or to protect the Social Security, the future of Social Security, I think is pretty fallacious. But, again, if you believe that the central goal of policy should be to raise taxes or to have higher taxes than those we have today, you will have many, many chances to do it. Very, very little tax relief has been delivered to the American people, 40 billion last year, 38 billion this year. So if the prospect of giving parents a child care tax deduction, dependent tax deduction, you have many, many chances to correct what you see as mistakes.

Mr. MCDERMOTT. Mr. Chairman, this is the chart that I was referring to. When you ask us did we show it to you, you wish we would have been prescient last year, that line right there showed that you left no margin for error. I admit that you had a downturn in the economy. We said it was coming. And big chunks of it had happened by August when they made the estimate. 9/11 did not cause the problems that we have right now. That overestimation of what money was there was the real problem.

Chairman NUSSLE. The gentleman's time has expired.

Mr. Thornberry.

Mr. THORNBERRY. Thank you, Mr. Chairman.

Mr. Daniels, all of us certainly find deficits distasteful. I think when you get past the demagoguery the question is, what are the alternatives for fiscal year 2003? That is what is in front of us, that is what we can deal with. The rest of it is assumptions and projections. The question is what can we do about this?

Now, you had a chart a while ago that showed us some alternatives. If you want to take away the increase in defense and take away the stimulus, you showed us one way that we could get back to a balanced budget. But what we have heard from Mr. Spratt and others is they agreed generally, as I understand it, with the defense and homeland security emphasis. So what are the alternatives then if you assume that you are going to have this increase in defense, assume that you are going to have the homeland security? You don't like the fact you are going into deficit, you want to set all of the Social Security and Medicare money aside in a lock box to pay down debt. What are you left with for the fiscal year 2003 budget?

Mr. DANIELS. You described the choices we face very completely, Congressman, and the President's choices are obvious, obviously the ones encompassed in this budget. The defense of the American people is the first responsibility of the central government, above and beyond all else. That is where the new investments go.

The Congressman sees this as a no-pain budget, but I don't think everyone is going to agree with that, because we have constrained the rest of government to the lowest growth rates we have had in a long time after years of big run-ups, and I think we can already hear the first complaints about that from folks who have been used to much bigger increases, and we will have to respectfully disagree.

So there was another choice, as I illustrated. We could have left the fence where it was. We could not move forward with the war, we could not add to our homeland security and all the rest of that, and we could have a surplus. And instead of using Social Security funds to pay for those purposes, we could use Social Security funds to pay bondholders. That is the choice. We will get back to that one day, I believe, but not at a time of war.

Mr. THORNBERRY. Well, let me follow up. We had Director Crippen before our committee January 23 talking about their changes and assumptions and so forth. Frankly, I was most interested in the point he tried to make at the end, and this is paraphrasing a little bit. He says it doesn't really matter what you are talking about the deficits, whether you use this year's numbers or last year's surplus numbers, it is not going to solve your Social Security problem. This is a long-term demographic problem. Unless you face that head on, you are not being straight with the American people about what it is going to take to solve it.

Do you make those similar kind of—do you have a similar sort of outlook on what really matters in Social Security and what doesn't?

Mr. DANIELS. Yes, sir, absolutely. As much as I hope that we can regain our footing, once again begin paying down debt, all that accomplishes is to marginally increase your borrowing capacity when the crunch arrives, and you will not be able to borrow your way out of the Social Security problems if we don't reform the system. It depends entirely on reform of the system that we have today and strong economic growth so that we have revenues coming in when that time arrives.

Mr. THORNBERRY. Which was also the point that he made, the economic growth—encouraging economic growth is the key factor to solving Social Security down the road.

Let me ask you about one other issue. I share the chairman's view that putting more emphasis on management is a good and appreciated thing. I have been particularly interested in some homeland security issues. I notice in this budget, for example, that you have grants going to local police, local firefighters, to help them get the equipment that they need administered through FEMA, which are the people who are used to working with the local folks, and I think that is a terrific addition.

You also have a lot more money going to border security, but what you have not done yet is consolidate or rearrange or change some of the border security agencies, which is something that I think is a good idea.

We all want the money to be spent well, even in homeland security and defense. Can you tell me if maybe some other management reforms are coming, particularly our border security, to make sure that money is spent well, and that agencies actually talk to one another.

Mr. DANIELS. Quite possibly, Congressman. Governor Ridge is looking at this. I think he has openly expressed his view that we might be able to do better than we do today. We do have some parallel and sometimes overlapping activities going on at our border and he has got that under study right now.

The administration did move even prior to the 11th on reform of the INS itself, and that is pretty well under way. But that may prove not to be enough, and I will report to the Governor your view that maybe further consolidation here would be a good idea.

Mr. THORNBERRY. Thank you.

Chairman NUSSLE. Mr. Bentsen.

Mr. BENTSEN. Thank you, Mr. Chairman.

Mr. Daniels, I do want to go back. I have tried to avoid this, and I don't like this, where people say you are Enronizing and all of this other stuff. But I sat through two days of hearings saying it was the other guy's fault or whoever. I look at your testimony and you have a quote for those still professing to find use in such numbers, talking about a 10-year period and the fact that you were in good company of people who missed the recession, and people who missed the fact that the assumptions would be wrong, you have a word "misestimate," which I am not sure that that exists. Then in your testimony from last year you go into some detail about people being skeptical about $5 trillion expected surpluses.

Then you say, "But the data suggests strongly that it is at least as likely that total surpluses before policy change will come to more and not less than today's projection." Quite frankly, you know, I am not going to accept this from anybody, that last year people were saying, oh, well, we are really not looking out 10 years because we were sold on 10 years. And my friends on the other side can try and sell it and say, no, nobody looks out 10 years, we only look out one. But I think the record is pretty clear on that.

Now, let my say with respect to your overall budget package. I understand the need for the homeland security aspect. I was one of the ones who joined in calling for that last year. I understand the need for a great deal of the defense ramp-up money, both to pay for the cost of the war in Afghanistan as well as transformation as well as other needs on security that we now realize that we need.

What I don't understand, quite frankly, is—and you said it just a few minutes ago—that these were additional costs, and costs in some cases without tremendous productive value, but they are necessary costs for security.

But on the one hand while we agree on those costs, at the same time you have a budget that has a 9-percent increase in spending, and then you want to go and cut taxes by three-quarters of a trillion dollars over the 10-year period. To me, quite frankly, that doesn't make a lot of business sense or business logic. When you have already locked in the one tax cut, now you want to add on to it an additional—I don't know what—35 percent on top of that, at the same time that you are admitting that you got additional costs that were unforeseen by anybody that you have to plug into the budget. Now, you are going to come back and say, well, we think tax rates are too high, we need to lock these in and we need economic stimulus.

I would raise two points. No. 1 is that if it is the same economic stimulus bill that was brought up last year by the administration, if I understand correctly, that a vast majority of that occurs in the second, third and fourth and fifth years, well, all of us, including your own numbers, project that we will be out of recession by that time. So what type of stimulus is that?

Second of all, the fact is that what is the point of borrowing money to pay for tax cuts? There is clearly a drag that is associated with that, whether you are borrowing at 4.9 percent over a 10-year period or a lesser percent over a 7-year period.

Finally, with all due respect to my colleague from north and west Texas, that I do think in the long term, this is not a Democratic or a Republican idea, but I do think in the long term, and what Dr. Crippen is saying, that you do grow the economy in part by lowering your debt ratios, and in fact we are going in the wrong direction here. Last year everybody was bragging about how much debt they can pay down, and now we are going to be adding a little debt for a while, then we are going to end up with considerable more on the books than any of us had projected. I don't think that does us any good positioning the economy for the long-term liabilities of Social Security and Medicare, and I think that is a real shame.

I think that you know you have sent us two budgets. You have sent us the necessary budget on the defense and homeland security, and then have you sent us a political budget that has this additional tax cut that defies business logic, in my opinion.

Mr. DANIELS. Let me respond to a couple of the points that you made. First of all, I think the President would agree with you that any stimulus we do needs to be near term in its impact. The problem is here and now. We would want the effect a true stimulus bill would have to have effect here and now. It should be temporary.

Now, the one that got so close to passage last year was reasonably well suited to that. It would have included, as I recall, rebates to people at the very low end of the income scale.

Mr. BENTSEN. But the bulk of it, sir, was in the corporate side, was out multiple years, $200 billion.

Mr. DANIELS. I disagree. The accelerated depreciation provisions, which had a lot of support on both sides of the aisle, would have lasted 3 years, but they would have started right away, and the rate reductions for the people in the 30,000, 40,000 sort of bracket would also have had near term effects. So that was not a bad stimulus measure, certainly was acceptable to the President, and I think it is responsive to your point when you have a recession on now you want to take measures that have effects right now.

A couple of other things. Among the reasons we ought to keep our heads in the current situation is that our debt and interest picture remains pretty darn strong. Actually our debt ratio will continue to come down even under the conditions that we think we see now in this particular budget. Interest costs as a percentage of Federal spending are continuing to come down. They are passing through 9 cents this year. Just a few years ago they were twice as high. They were 16 cents on the dollar just to service the debt.

Mr. BENTSEN. But a trillion dollars in additional P&I cost over what was projected in the last year does not appear to me to be a productive use of taxpayers' money, and I think both sides would agree on that fact. So, we seem to be moving in the wrong direction here.

Mr. DANIELS. It is hard to tell. These are the 10-year projections for the 7 years we have tried to do this, and you can see what an outlier at this time last year's is. When I said last year, and you quoted it accurately, was simply a literal translation of a matter of probability, that is to say that the 5.6 trillion, based on the situation as it was understood then, the assumptions in that budget, which are no different than CBO's essentially, were 50 percent probability assumptions. That meant there was as much chance that the number could go up as the number could go down. We could be back next year looking at the same projections. It can change as fast going up as it did going down.

I point out to you if we had taken a 1-year time out from this 10-year experiment, we would be looking at a surplus projection that is the biggest one we had ever seen, actually slightly larger than the one that the previous administration made 2 years ago today.

So the point is we don't know. We have to deal with the situation in front of us, which at the present moment I don't hear much disagreement here. We have to deal with it very vigorously in terms of the priorities that we face.

Mr. BENTSEN. Thank you.

Chairman NUSSLE. Mr. Toomey.

Mr. TOOMEY. Thank you, Mr. Chairman.

Mr. Director, thank you for being with us today. Some of my colleagues on the other side of the aisle appear to be quite exercised obviously over the fact that we currently are projecting lower surpluses than we did last year.

I find this baffling, frankly, especially when I look at the chart that you have. S6 on your supplement, which demonstrates, to my analysis, that from 1998 to 2002—at least if you look at those years—average annual discretionary spending grew at about 7 percent on an annual average basis, which is growth that is at least three times the rate of inflation. With all of that spending going on, it seems to me that most of my colleagues on the other side who are complaining so much about the size of deficits nevertheless voted against Republican budgets in the House-passed budgets that would have had less spending, voted against appropriation bills when they first came through the House at lower levels of spending, and consistently advocate even more spending.

So I don't understand how people can be quite so upset about deficits when they advocate ever more spending, but let me shift to the tax question. You pointed out on a chart that when we passed tax reduction last year, we were passing it from a level that was at a post-war record high and that even after this tax reduction we will be well above the historical high.

Are you aware of any time in American history, or any other developed nation that you might care to cite, when a modest reduction of marginal tax rates from a record high level has had negative impact on economic growth?

Mr. DANIELS. No, sir, not offhand.

Mr. TOOMEY. There is a significant consensus amongst private sector economists that one of the contributing factors in the current economic downturn may have been the fact that peoples' incomes were rising consistently in the 1990's and it was pushing them into ever higher tax rates. During the 1990's we increased tax levels. Do you share the view that that effective bracket creep, that ever higher taxes that people might have been facing may have contributed to this current economic downturn?

Mr. DANIELS. Well, I am not certain. I do know that economic theory, but more importantly your common sense tells you at times of economic weakness, like right now, taking more out of the hands of private citizens and businesses is probably not a smart idea.

Mr. TOOMEY. Thank you. I also wanted to refer to the budget where you have rated the effectiveness or the performance of various measures of the various executive branches. Now, when you look at the chart that you have put together, it is hard not to notice the dominant color on that chart. The dominant color is red, which indicates an unsatisfactory performance, if I understand it correctly. Do you intend and do you think we ought to systematically begin to reduce funding for those areas that are performing at an unsatisfactory level? Is that not an indication that there is waste of taxpayer money?

Mr. DANIELS. Let's be careful about how we interpret. There are two things going on, both of which we think are very important in the area of better management here. We have on the one hand attempted to begin, and this responds to a mandate of Congress in some statutes, such as the Government Performance and Results Act, passed in the 1990's, responds to the mandate of Congress by trying to become serious about separating programs that work from programs that don't. We do give a number of examples. I think we have 41 effective programs, somewhat more than that, we can point out or point to as ineffective, and frankly the vast majority in the middle about which we just don't have good enough data. I absolutely believe that we must come to the point where, as any business would, as any family would, we rigorously weed out those things that are not working and strengthen those things that are.

So on that point I would very much agree with you. I would be careful not to mix too much the concept with the scorecards, which are a little bit different.

This administration is committed to trying to do a better job of managing the day-to-day business of the Federal Government, and the five areas on those scorecards were selected because we think they are some of the biggest problem areas. Those are sort of by definition, therefore, you would expect a lot of red. As we told some of the departments, if you are all green we picked the wrong problem. We picked the problem that you solved already.

So the thing to watch there is our ability or not to improve, and this is certainly the President's view. He has said to each Cabinet Secretary, of course the starting point is bad, that is why we picked these areas of systems, financial accountability, human capital, and so forth.

Now, the real problem will be if they come back to him in a year or two and they are still red. But as he has pointed out, measurement is not about punishment, it is about creating the conditions for improvement.

Mr. TOOMEY. Very quickly. I notice if you exclude the assumed economic stimulus package in your budget we would be within $3 billion of a balanced budget. I frankly think if you exclude the economic stimulus package—I hope we get one, I am not sure we will—absent that, I think we could and should get to a balanced budget for fiscal year 2003.

My question is, if we can't get the economic stimulus package that we want, do you oppose spending that money on other purposes?

Mr. DANIELS. Yes, I do.

Mr. TOOMEY. Thank you.

Chairman NUSSLE. Mr. Davis.

Mr. DAVIS. Thank you, Mr. Chairman.

I would like to go back to chart No. 3 that Mr. McDermott was referring to, put that back up if we can, Mr. Daniels.

I will stipulate to what the chairman said. Many of us who were Democrats voted for the spending proposals, so we can refer to those as Democratic and Republican spending proposals for the most part. If you could briefly take the opportunity to point out what you think is incorrect about this chart, if anything, Mr. Daniels?

Mr. DANIELS. Not having prepared it, let me study it for a moment. Well, one thing to bear in mind is that this excludes, of course, trust fund revenues in the calculation, which to me is a distortion, and the better calculations were those I heard earlier which measure the change in the surplus on the basis of the total revenues of government. This you know is designed, I guess, to measure the tax cut against only a partial revenue base. So I think a fairer comparison would be the one that the chairman, I think, started us with earlier.

Mr. DAVIS. But, Mr. Daniels, we are not going to use any of those other trust funds to fund Social Security or Medicare. So I think we can agree to that. So this is really a representation about what availability there is in the surplus to deal with those needs in the future, right?

Mr. DANIELS. I am not sure I understand your question, sir.

Mr. DAVIS. Let me move on in the limited time I have. The assumed rate of growth in the GDP in the tax cut you advocated to us last year was about 3.2 percent. Obviously that was a gross miscalculation. Apparently in your testimony you are advocating an additional tax cut that you calculated about $591 billion. The Democratic staff calculates that as $675 billion. So, splitting the difference, let's call it about $630 billion. Aren't you concerned about equally miscalculating again the rate of growth, and shouldn't we be conservative this time as far as whether we are willing to plunge into a further major set of tax cuts given the uncertainty in the economy?

Mr. DANIELS. I am very conscious of the need to be careful about our estimates and we have in fact the most cautious, the lowest estimates in the field. They are lower than CBO's, they are lower than the blue chip. At this point, our estimate of this year of 0.7 many people think is far too conservative. I would rather, frankly, be safe. I would rather be on the safe side. I don't like it in business and I don't like it here to have to miss revenue estimate.

Mr. DAVIS. But, Mr. Daniels, with all due respect, isn't that the same thing you told us last year about the assumptions you brought to the committee?

Mr. DANIELS. It was true we were in the bottom half of all predictors last year. Everybody was wrong. All the private sector people who make their money doing this all missed it, too, as well as CBO, as well as the administration. I am not asking for forgiveness here. I am angry that we missed. But I would—what I told you was true at the time; we believed that looking—everyone else thought that we had a reasonable projection.

Mr. DAVIS. Perhaps you and I can agree that you are being as cautious this year as you were last year in your assumptions. My grandfather used to always say, there is no education in the second kick of the mule. Shouldn't we simply focus on our security needs, trying to minimize the deficit, before we launch into another major set of tax cuts and risk repeating the same mistake from last year?

Mr. DANIELS. Well, sir, the tax relief that is already in place, let alone making it permanent which is 10 years away, 9 years away, you will have many, many chances to prevent that happening.

Mr. DAVIS. So you are suggesting we might repeal some of the tax cuts.

Mr. DANIELS. I am just saying that if you believe that they are such a bad idea, you haven't lost anything. Only 80 billion, $78 billion of relief has been given so far. Last year plus this year. All the rest, as my one chart showed, is out—most of it, way out in front of you.

Mr. DAVIS. But, Mr. Daniels, my time is up. What I hear you saying, correct me if I am wrong, is if our estimate is wrong again. We can go back and repeal some of these tax cuts, right?

Mr. DANIELS. If you think it is a good idea, for any reason.

Mr. DAVIS. But under your definition, that is a tax increase.

Mr. DANIELS. I didn't call it that.

Mr. DAVIS. I know you didn't. Not in this context. But if we miscalculate again, the only recourse we have, unless we want to go further into deficit—and you are advocating—is to go back and repeal some of these tax cuts.

Mr. DANIELS. There is a lot of spending you could cut, too. We could have gone further than we did, I suppose, in the proposals we made for this year. But you will have in any given year $2 trillion of spending you can look at.

Mr. DAVIS. If I could, briefly, I just had one other question.

Chairman NUSSLE. One more.

Mr. DAVIS. Mr. Daniels, do you have any concern about the level of deficit that you are proposing to us which—actually let me restate that. The level of increase in the debt held by the public that you are advocating to us, a $157 billion increase in 2002, for example, do you have any concern about the impact that may have on the interest rates that we are currently enjoying and what that would do to our economy?

Mr. DANIELS. Not much. I have a lot of concern about any increase in the debt. I would like to be paying it down. But if you are interested, we have the lowest interest rates in 40 years, lowest home mortgage rates, lowest long-term bond rates. We have looked and looked and looked. It is an interesting theory that what drives this is surpluses and deficits.

But, in fact, there is absolutely no correlation. You can't find it. We have had interest rates go down when deficits were high. We have had interest rates relatively high when deficits were low. So you know, the good news here is we are—we have very, very low rates, historically low rates right now. If that was enough to ensure a strong economy, we would have a boom on, point one. And, No. 2, they are not connected in any way that one can find.

Mr. DAVIS. If Chairman Greenspan were to testify before this committee that he sees there is a relationship between us reducing the level of debt held by the public and interest rates levels, you would not agree with that?

Mr. DANIELS. I read very carefully what the chairman has said. I think he would agree with me. Look, we agree that we ought to try to bring down deficits. You are certainly not interrogating someone today who enjoys red ink. I probably have as big an aversion to it as anybody in the room. I do believe it is far better to reduce our debt levels as far and as fast as we can. We do face a current situation, which means we have to interrupt the very healthy debt reduction we have undertaken. I hope that interruption is very short.

Chairman NUSSLE. Mr. Hastings.

Mr. HASTINGS. Thank you, Mr. Chairman, and welcome, Director Daniels. I give you some credit for doing a two-fer today, to go to the Senate and here. I don't know what you heard in the Senate but sometimes the discussion here today is rather pointed.

Mr. DANIELS. I guess I called it batting practice. It is a doubleheader.

Mr. HASTINGS. There is, however, a silver lining out of all of this, believe it or not, coming from both sides of the aisle; because there is a common thread of what everybody has said, there is a concern of having and running deficits.

There was a time when there was never any agreement on running deficits. One side would say that was not a problem. In fact, it was pointed out in one of the earlier charts that the Reagan tax cut exacerbated by implication the deficits. But what was not pointed out, the agreement that was not kept, and that agreement is for every dollar of tax cut there should have been a corresponding cut of spending. In fact, just the opposite happened. Spending increased by a dollar and a half for every dollar tax cut, so that exacerbated the problem. That is the fact.

Mr. Nussle pointed out in his opening chart, and Mr. Toomey corroborated, that if we stayed with the baseline we would probably be in a very good situation coming into this year. But that was broken earlier. We are probably all to blame for that. The President was pretty specific in his State of the Union speech when he suggested that if you want to eliminate these deficits in the future—and apparently we all agree that deficits are not good—we ought to watch the spending part.

You have talked about that it seems the only argument that we can talk about here is what revenue projections are. You stated over and over—I will give you one more chance to say it either short or long—to anticipate what revenues are coming in over a long period of time is an inexact science.

I would just go back; probably only one person sitting around here thought that the football game would turn out differently last Sunday, and that is Mr. Capuano. Even the experts in the very short term were wrong in that case. But you are the only one. At any rate, you have your—it is an inexact science of estimating revenues over a long period of time. Just—if you don't want to answer it, that is fine.

I have one more question to ask you. If you want to respond to that, I would appreciate that.

Mr. DANIELS. No. Well said. I mean, we have learned in the last year how big a miss can be just in a 1-year period, let alone 10.

Mr. HASTINGS. I would just say the good news is when things start turning around, we anticipate that will happen hopefully sooner than later. You will have a lot of support on this committee. If it appears we won't get into a deficit situation, you certainly have my support.

Mr. DANIELS. I should probably kind of confirm what you say by pointing out that the misses, the revenue misses, were just about as big on the happy side for a couple, 3 years, when the economy grew at rates that hadn't been foreseen. That could happen again. We have to do all that we can to see that it happens again. And that was the point, really, of showing earlier how when you run those out over 10 years how wildly varied the answers can be.

Mr. HASTINGS. The point is that even as much as a miss still anticipates more revenue over the next 10 years.

Let me focus just on one area. I represent the Hanford area in Washington State. It is one of the nuclear sites that needs to be cleaned up. I might add, since we are talking about a war budget, Hanford came into being because of the Second World War, as did the other sites, and we are still cleaning those sites up.

DOE has come up with a way of trying to incentivize, if you will, accelerate the cleanup. Would it be accurate to—with respect to the nuclear cleanup at those sites, that the administration's goal is to ensure that these DOE sites, the ones that are getting the job done, will continue to receive the funding that in fact they need?

Mr. DANIELS. Yes, absolutely, Congressman. The administration's real goal is to speed up the cleanup of these sites. It has been dragging. Some of them, if you can believe it, you know, are not scheduled to be cleaned up for 70 years. That is just unacceptable. In the meantime, we are experiencing incredible cost overruns in the aggregate that are well over $70 billion.

So this budget does seek a reformed program and makes available new money for sites that get on a faster, surer track to cleanup. And we hope Hanford will be one of these to have more money to get the job done quicker.

Mr. HASTINGS. Let me just follow up on that. You have within the budget a $800 million pot of money for that. I mean, when you total that with your baseline, it is exactly the same baseline as we had last year. This is the way to try to incentivize that. But you also said that if in fact there is progress that is being made at that $800 million, that can be increased in outyears. Can you give me an idea somewhere, how much that could go?

The whole idea of this, of course, as you mentioned, is that it is like the Fram oil filter: Pay now or pay later. If we can pay now and save money in the outyears and accelerate the cleanup, that is what we ought to do. With that $800 million, can you give me some idea of perhaps what the ceiling would be in the future?

Mr. DANIELS. I am sorry, I can't give you a good guess, Congressman, except to say that we do believe this is the way to go. It would be money well spent and increases would be in order.

There is a pretty good model for this, I have learned. Probably it is the Rocky Flats Colorado example and spending more early, spending it smarter. In some cases, this will involve redoing contracts that are there now. But to get these projects on a lot faster track to cleanup, that has got to be in everybody's interest.

We appreciate your leadership for a long time and your staying in touch with us to make sure we don't take our eye off this ball.

Mr. HASTINGS. I appreciate that very much. I would just say that I mentioned a lot of these sites came into being in the Second World War. We take care of our veterans. Yet the outyears on this, I agree with you, is way out of line. So I appreciate your comments on that. Thank you, Mr. Chairman.

Mr. SCHROCK [presiding]. Mrs. Clayton.

Mrs. CLAYTON. Thank you, Mr. Chairman, and welcome back, Mr. Daniels. You know that the discussion of the budget is probably one of the most important issues we can talk about. It is indeed not necessarily a difference in principles or big pictures, it is a discussion about priorities, priorities of what we think is important for the American people. We can really agree that indeed, our defense should be a priority.

The question, though, comes—at least from this member—as to what extent it needs to be raised. So I think one should understand that there are areas that we can agree on, but don't agree on the exact number. You shouldn't be surprised if Democrats or others may be saying, "I told you so," because I remember when we had these discussions before, when we had a 10-year budget, and we wanted to find out. Then there was the discussion about defense, then, was the big missing piece. Can we afford it? Has there been a plan for it?

Now, September 11 has come and has clearly made all of us keenly aware, as we must be about the security of our Nation. We can't take anything for granted. We must be prepared for terrorism. But I gather this is also an opportunity to revisit last year's proposal for our defense without having September 11. So when we think about that, we put that priority at the expense of everything else. One is constrained not to talk about it because they think we are not patriotic. Well, we are patriotic to the American people. Those budget items you want to cut, will affect people who are going to need heat or air. Those people are Americans. Their need to protect their quality of life is also important. Yet, those types of cuts are proposed, and also proposed are cuts in training.

We are now in a recession. There are proposed to be cuts in Medicaid to hospitals. Our hospitals are struggling. I mean, the priorities in a budget identifies where we think things are very important. Homeland security, is very important. In fact, where you propose to make those allocations makes a lot of sense. The question is, how much and where does it come from?

So the discussion about whether it should be $48 billion at the expense of cutting something else, those are questions we ought to have a debate about if you are serious about the budget. Do we take from the current law enforcement programs that they have enjoyed in bringing home, now to give to one's homeland security opportunity to give to another? I mean that we are shuffling the same money around. The same police department, who now wants those dollars to protect us, and to make sure that we are free from drugs. Now we call it homeland security, and we shuffle some more money over there.

So, part of this needs to be revisited in terms of having the right balance and the right set of figures.

Finally, the whole area of our commitment to our senior citizens. You know, all of us can be quoted, including myself, that we were not using this money. I have always said, where is the box and where is the lock? Apparently there is no box if there is no money in the box, right?

As for the President—I agree with the President. The President said there are times when we should have deficits. Everybody knows that. There are times with the situation of our families, that we have to go borrowing because the issue is so important. So it is with the American people. But the rate that we are borrowing while we have to borrow and the double hit that Social Security is going to get, we are taking money now, and guess what, the debt we have to pay later is going to hit them again.

So there is chart 8 which makes this abundantly clear. Social Security surplus. Without the new tax or last year's tax, that line on top would be showing where we would be. Now, if you include your new tax cut, you begin to see where the red ink is. You begin to see the impact that it is going to have on Social Security. In fact, the new tax cut, an additional $665 billion on top of that—well, we are really going to have a train wreck. I am like Mr. McDermott, I have already started receiving my Social Security, so I don't want you to cut it off. I need my money; I want you to know that. But anyhow those who are coming behind me, like you and some others, you may not need it, but a lot of folks do need it.

Mr. DANIELS. I brought yours with me today, Mrs. Clayton.

Mrs. CLAYTON. Did you? You are a scholar and a gentlemen.

That $675 billion new tax cut is going to make it even more devastating. So I hope this debate as we go forward will allow room for us to discuss the priorities that ought to be equally as important.

You put in there that we are going to have a prescription drug, but the amount of money you put in there is less than the amount of money you proposed the last time. And guess what? It is going to provide less assistance to a number of seniors.

So this debate, I hope, is just beginning. Thank you, Mr. Chairman.

Mr. DANIELS. I will just respond by thanking you very much for those comments. I strongly agree that it is not only not unpatriotic, it is the patriotic thing to do to debate these proposals. I know that the Congress will and should take a close look at the President's defense request. I think you will find that Secretary Rumsfeld has put it together carefully, and he can justify what's asked for both in terms of rebuilding things that had deteriorated before and meeting the new threats that are there.

But those are very, very legitimate questions. And I am happy to tell you that on a couple of the matters you mentioned, job training for instance, when one reads the whole budget, the President is asking for a substantial increase.

Mrs. CLAYTON. Is the Job Corps going to increase?

Mr. DANIELS. There is the Job Corps. But in total, we were asking for an increase from 6.3 to 9.3 billion. He wants the national emergency grants which almost made it in as a part of the stimulus package in December—we certainly want those back. And that will give us a huge new amount of money that States can use to respond to the job training needs and other dislocated worker needs of the people that they are serving.

Mrs. CLAYTON. How about the low-income energy to help seniors who need it?

Mr. DANIELS. We are asking for 1 billion 7. We have got a good bit left. This has been a kind winter, extraordinarily kind both in terms of mild temperatures and lower costs for energy costs, and therefore we have a lot of money, 770 million the last I looked, still in reserve for this year. But we are asking, of course, for 1 billion 7, moving forward, to continue that program.

Let me say, lastly, that you say money will be shuffled around. Well, true; but you know that is exactly what we must do. In other words, for instance, you mentioned law enforcement. There are some new needs. We really may be saying the same police departments or fire departments, but there are some new needs. We do need the money to be moved from one purpose to another. We now know that we need emergency response teams, very well trained, to come into action if we are attacked again. So we do need to move the money from yesterday's top need to today's. And that is what we hope the Congress will work with us in doing.

Mr. SCHROCK. Mr. Daniels, thank you for being here. I am pretty much pleased with the budget, I can assure you. I am especially pleased with the defense part of it. I think you were dead right when you said that the military establishment was decimated during the 1990's. Some of us have been screaming about that for a long time, whether we were up here or other places. I am glad to see the money in there.

I have always been a voice of the military. I am a retired Navy captain, so I am very pleased to see that we are doing for the men and women in uniform what we need to do, and giving them the assets they need to fight this war on terrorism.

There is one area that I am a little concerned about and I would like your comments on it. I noticed there were only funding for five ships in this next year. If we are going to maintain the fleet of 315 like everybody thinks we need to—frankly, I think that is entirely too low, but that is the number they are talking about. I am not sure five a year will do it.

I also understand that they are trying to delay—they want to delay the construction of Carrier 77 by a year or so. I am really baffled by that.

Before you answer that, I was out of here for a few minutes on the triangle. I know Mr. Thornberry was talking about what if there is no economic stimulus package. Someone announced out there that Mr. Daschle said out there it is dead, kaput. So that might change things dramatically. I wonder if you could comment on the ship thing, and what the $80 billion in the stimulus package that looks like it is not going to happen will mean for this whole budget process on the coverage we have had here today.

Mr. DANIELS. You are correct about the five ships and also that most models suggest that is not a sufficient replacement rate to maintain today's 315. Beyond that, I will direct you to Secretary Rumsfeld and his people. Obviously, even in the context of a budget request that grows by 12 percent, they have had to make a lot of choices. There is a lot of—one would might say—transformation in this budget. There are a lot of requests for the kind of weapons that have just proven so effective in Afghanistan. We have to replace them. And now the people see we will need them to occupy a bigger place in our overall military readiness. So much of the new money goes in that direction.

But I am well aware that among the areas that some people think have been—have been left behind a little bit is shipbuilding. That is a question that the folks at DOD will address for you.

I am saddened to hear the news—I hope maybe it will prove inaccurate—about the stimulus package, because I think it is way too early to declare a victory over this recession, even as promising as some of the recent news has been. And once again, just from the fiscal standpoint, it makes a lot of difference whether we get to a 3 or 4 percent growth rate early this year, late this year, or not till early next year. You put those into our 10-year models and you will find very big changes for better or for worse, if you actually knew for sure that they were going to carry out over that whole time period.

Mr. SCHROCK. Right. I agree. The carrier debate that they have had over the years I think is a moot point now, based on the mission they have carried out over in Afghanistan. To delay construction over another one is not a good thing.

Mr. Price.

Mr. PRICE. Thank you, Mr. Chairman.

Mr. Daniels, welcome back to the committee. We appreciate your testimony. I would like to concentrate on the levels of publicly held debt that we are anticipating in this budget and the relation of that to the future of Social Security. To lay the groundwork for my question, I want to put two slides up. The first has to do with the amount of publicly held debt that we are now projecting for the end of the 10-year period compared to what we were projecting 10 months ago. Ten months ago, we were projecting no debt at the end of the 10-year period. Now we are projecting a debt of approximately $2.8 trillion.

The next slide shows the implications of this debt on the cast of debt service. If there is any money in the Federal budget that represents money down a rat hole it surely must be interest on the publicly held debt. We were anticipating debt service of approximately $700 billion over this next 10-year period. Now that projection is almost $1.8 trillion, over a trillion dollar increase in the projected interest payments.

Now, I would like to ask you a couple of questions about this. First I would like to clarify your views on the Social Security Trust Fund. On September 6 before the Senate Budget Committee, you said you would appeal for caution and precision in the words we use. Then you went on to say that the assets of the Social Security fund were only bonds, and that, quote, “there are no assets other than the future promises that future taxpayers will pay off the bonds in those trust funds.”

A month earlier you had said to the Senate Budget Committee that the bonds in the trust funds were, quote, “nothing but a pile of IOUs.”

Now, this leads to three questions. First, do you believe that the Treasury bonds held by the Social Security Trust Fund are or are not real assets backed by the full faith and credit of the United States?

Secondly, assuming they are real assets, does the United States have an obligation to redeem these bonds when the Social Security cash flow reverses around 2015 to make good on promises to beneficiaries?

And third, does this projected debt, which is 3 trillion more than what was anticipated 10 months ago, and this projected debt service, which is 1 trillion more than what was anticipated, does this make it more difficult to redeem these bonds and meet these obligations?

As you know, until recently both parties have assumed that it is important to use the Social Security surplus to pay down the debt, and this is related in a positive way to meeting our future Social Security obligations. Do you still agree with that proposition?

Mr. DANIELS. Thank you Congressman. I do agree with that. I would say that paying down debt does make a positive but, I would say, partial—very partial contribution to addressing our long-term Social Security problems.

Let me answer your other questions by way of illustration along the way. Are the instruments in the trust funds real? Yes, they are real. And, yes, they represent an obligation backed by the full faith and credit of the United States. And they will be honored; I don't doubt that for a second.

When I said they are only bonds, I was really addressing a question much like the one that Congresswoman Clayton mentioned a minute ago. Some people have imagined or confused themselves that there is some cash somewhere in the box or that there is some other kind of asset, when in fact what is there is exactly what I said: simply a bond, a promise to pay on behalf of the taxpayers of the U.S., a very solemn promise, but one that will only be redeemed by the ability of the economy in the future to generate the resources necessary.

Will it be more difficult to redeem that promise when the day gets here that Social Security is costing more than the payroll taxes that are scheduled to come in? It will be more difficult only in the sense that for a limited period of time we can borrow the money back, the money we have paid down in the interim. You know, it will not solve the problem. That's why I say positive but partial.

Let me just make one or two other points about the charts. No. 1, we do very earnestly hope that in addition to defending our country and meeting the high priority issues of homeland defense and so forth, that we will be back quickly into surpluses and once again moving down in terms of outstanding public debt.

Your chart shows a balance of less than zero dollars. Let me just point out, we always said that we thought there was a minimum beyond which it would be difficult to go, a few hundred dollars at least. If we get to that point as we all, I suppose, hope to do, to reach the numbers on your chart, you have to begin buying assets in the private marketplace. And this, I think, would be a very serious mistake and one that we will want to debate very vigorously if it is ever seriously advocated.

Mr. PRICE. But the caution you expressed a year ago before this committee, that there is a danger of trying to buy down too much debt too quickly, I assume that we have solved that problem.

Mr. DANIELS. I don't know. You know, Chairman Greenspan and many others made the very same point. I hope it is something that we are seriously discussing again before too very long. But I do want to link your various excellent questions together by pointing out that if we can get back to that point, someone may suggest—a few already have—that it would be a good idea for the government to acquire not bonds, but equities or other assets, and put those in the Social Security or other trust funds. That, I think, would be a very, very dangerous mistake.

Mr. PRICE. Can you say at what point we would in fact start again buying down debt under the budget projection you have submitted today?

Mr. DANIELS. Under this projection, it would be many years ago. But a strong economic recovery could bring that prospect a lot closer, just as the shift from 12 months ago pushed it out several years.

Mr. PRICE. Thank you. Thank you, Mr. Chairman.

Chairman NUSSLE. Mr. Moran.

Mr. MORAN. Thank you, Mr. Chairman. A lot of us try to be as nonpartisan as we can, including the ranking member of the committee. But, boy, on budgets like this it really makes it kind of hard.

Let me share three quotes. I think the first is from Casey Stengle where he suggested this was "deja vu all over again." I really think that is an apropos quote to this budget course.

I think it was Santyanna that said, if we don't learn from our mistakes we are doomed to repeat them.

And then one that I had occasion to read over the weekend: "free lunch economics is the worst kind of intellectual sophistry." That is a quote from your predecessor, Mr. Daniels—Mr. Stockman in his book, The Triumph of Politics. When you read that book, it just seems so eerily familiar, what is happening 20 years hence. Today we have a popular President again who is promising deep tax cuts, dramatic increases in defense spending, and yet he said that it is going to be OK, we are going to balance our budget. Of course, the fact is that for 8 years, President Reagan never submitted a balanced budget. I am afraid that is the situation we are going to have again in the first decade of the 21st century. And we are going in, I am afraid, with our eyes wide open. That is why, you know, it may seem like we are giving you a hard time, but it is really—I trust you don't take it personally—it is really this budget that you are forced to defend.

You know, we entered the decade of the nineties, and I remember the grief that President Clinton had when he increased, actually increased income tax rates on the highest level of the wealthiest people. On the other side of the aisle, every single one of whom voted against that tax increase—I see the Chairman smiling, and I remember some of his histrionics, although they were effective at the time, and they caused us concern; but, you know, it passed by one vote.

Despite all these claims that we were going to have high unemployment, that we were going to have a depression, that, you know, the worst kinds of scenarios were pictured, and yet for that decade the people at the highest income tax brackets actually took home more after-tax income than at any time in history. We had the lowest inflation, the lowest interest rates, the highest economic growth.

In fact, one of the most important things was that long-term interest rates came so low because the financial markets realized that the government was serious about balancing its budgets, about paying off its long-term debt. That is why we increased the rate of home ownership higher than it has ever been, and we had the highest standard of living. Those long-term interest rates are terribly important, and I am glad that Mr. Davis brought that issue up.

But today we see long-term interest rates not budging. Even though the Federal Reserve has cut rates historically, what, 11 times over the last year, down to 1.75 percent, and still long-term rates are over 7 percent. That is what affects people's standard of living. That is why we are so concerned about the direction in which we are going.

The other thing that troubles me most is what this generation—the generation of which I am a part, the baby boom generation, I was born in 1945—we were the principal beneficiaries in the 1980's of those low income tax rates and high spending. But we have we had one chance given to us before we all retired en masse, to pay off our debt and to provide for our own retirement.

That is basically what this issue is all about. Are we going to seize that opportunity to make right with the next generation, with our kids' generation, or are we going to give ourselves a tax cut because we are the principal beneficiaries that need these tax cuts, the baby boom generation? Yet last year, we made the decision to reward ourselves and to stick our kids with the cost of our retirement and public debt.

Now we see in this new budget that of the debt, the vast majority, almost all of it, you know, $1.7 trillion tax cut plus another approximately $800 billion that is recommended now over the next 10 years, so that is about $2-1/2 billion of tax cuts, and yet our debt is going to be $2.8 trillion, so it is the vast majority of our debt; and we are going to go into hock to the Social Security Trust Fund for that amount of money.

That is the problem. That is the issue before us. What does this generation do for the next generation? Do we reward ourselves with tax cuts or do we pay off our debts and provide for our own retirement? I don't hear a good answer from you or your colleagues in the administration, other than to say, well, we are going to—look at the economic growth rates we are projecting 5, 6, 7, 8, 9, 10 years out. Yet, on the other side of your mouth, you are saying, how can you predict anything longer than 5 years?

The Treasury Secretary, on Meet the Press, said, well, if you want to project more than 5 years, nobody knows what's going to happen more than 5 years out. It is an inconsistency. I think it is an irresponsibility. But I would love to hear how you respond to that, Mr. Daniels. Thank you.

Mr. DANIELS. I certainly think that we are speaking the same out of all sides of our mouth; that is, to be very skeptical. I didn't say anything different last year. I said it over and over again, we have to be very, very mindful how inaccurate these long-term numbers could be. That is still the case. I very much hope that our long-term numbers are inaccurate. I think they might be. That is to say, things could be much better than we have 3 or 4 years down the trail.

Mr. MORAN. But, Mr. Daniels, couldn't they be much worse, too? If that is the case, why, 60 percent of the tax cuts don't take place more than 5 years out.

Mr. DANIELS. Precisely. It took into account how uncertain all this is. As I have said before, if one believes that the best way to strengthen Social Security and to deal with our long-term problems is to have higher levels of taxation, even higher levels of taxation on the American public than we have now, there will be lots of chances. Nothing has been lost, you know, the tax cut in the main hasn't happened yet. That tax relief has not happened yet.

It is the point of view of the administration that the two things that must happen for Social Security's long-term health are, one, strong economic performance on a sustained basis, which we don't think is made more likely by higher taxes; and, two, reform of the program, without which everything else we attempt is kind of playing around the fringes.

Yes, the nineties were a good decade, the eighties were too, by the way. But they obviously ended on a weak note. No good time lasts forever, I guess.

We now know that the economy was grinding down from the second quarter of the year 2000 on and a full-blown recession arrived early last year. To our way of thinking, exactly the right time to—you say reward taxpayers; I would say punish them a little less and lift our foot off their throats a little bit as the tax relief bill of last year did.

Chairman NUSSLE. The Chair recognizes a true patriot, Mr. Capuano.

Mr. CAPUANO. Thank you, Mr. Chairman. Mr. Daniels, thank you. Before I comment on the budget in particular, there are few minor points that I would like to ask. I would appreciate in the future when you talk about unemployment rates—I said the same from the CBO—that you also talk about the numbers of people. I mean, based and just using your number of 5.9 rate, that is 8,395,000 people out of work. That is greater than the population of all but eight States. It is greater than the work force in all about three States. Only California, Texas, and New York have a larger work force than that entire number. It is greater than the combined work force of 15 States. It is a number, it is not a percentage. I understand you have to talk in percentages, I respect that. I would also like to see at some point a reference to individuals.

Relative to Social Security, I just want to make it clear that I understand about the lockbox, I understand about the trust fund, I understand about borrowing from it. But nonetheless, when my brother pays his FICA taxes each and every week, that money is now being used not for Social Security, but to balance the budget, and will be so used, as I understand it—CBO had it for 8 years, you have it for 10 years, it doesn't matter. So I don't want to make any mistake about it. I don't want anybody listening to think that there is not real money here. There is.

That real money, those dollars actually being paid by employers and employees, is being used not to fund Social Security, as people think it is, but to fund the budget. So I don't want to make any difference between trust funds and lockboxes. It is taxes. It is being used as such. People don't necessarily think that.

I guess I also have to say relative to 10-year budgeting, I agree with you, 10-year budgeting is not a good thing. But neither is phasing in or out significant tax policy over a 10-year period. When you do that, and you do it in such a manner that the weight is in the last several years of the 10-year period, if you really want to be seeing the impact of that action—again, tax increases, tax cuts, whatever it is going to be—the only way to compare apples and apples is to take a look at the full impact of that action.

Therefore, if you are going to do one over 10 years, then you should—you must do the other over 10 years. Other than that, in a purest sense, I wouldn't do either over 10 years. Do your tax cuts, do your tax increases; bang, do them, get them over with. So I would agree with you that 10-year budgeting is not good, but you can't have one and not the other.

As for the budget itself, I guess I have come to the conclusion—I mean, I did Financial Services all morning and I have come to the conclusion that basically Enron has decided our energy policy for this country. I am now starting to come to the conclusion that Arthur Andersen is doing our budgeting. I look at it, all I can think of, it is the exact same thing. I haven't had time to go through the entire budget, obviously. We have only had it for a day and a half. I look at it and I see Enron had hidden losses. They would borrow money from themselves and shift it off their budget into other places.

We are borrowing money from ourselves in Social Security and shifting it to someplace else. I look at tricky accounting schemes. Enron would do things like use employee pensions, they would do all kinds of things. We are doing the same thing. We are using tax gimmicks, we are using accounting changes. We are using proposed stimuluses that aren't there. We are using revenue from ANWR that hasn't been approved. We are doing all those same things. Not as bad, and I certainly don't think it is as evil as potentially the Enron thing might be, but it is the same bottom line.

We are weakening the SEC. Enron did it by lobbying, keeping us away from dealing with the SEC. We are doing it by not increasing pay parity. We are doing it by proposing people on the SEC, who are the very people that have caused the problems in Enron. Enron had a disregard for the workers and their children. They did it by ruining their pensions. We are doing it by dipping into the unemployment trust fund, by cutting that when the State of Texas is going to be the first one here at the door to ask for a loan.

We are doing it by cutting job training. We are doing it by gutting GME for pediatricians. What is the next generation of pediatricians—where are they going to come from? My grandchildren won't have pediatricians.

We are doing it by cutting LIHEAP. Enron did all of this while taking care of the fat cats. All the big guys walked away with only tens of millions, and they are crying that it wasn't hundreds of millions. We are doing it while doing corporate AMT tax cuts. We are doing it while accelerating the income tax cuts for the upper class. We are doing it with no benefits to the economy, according to CBO. This is CBO's statement, not mine.

For me, I am very concerned. I understand there are different ways to do it, but we need to talk straight about it. We haven't done it in this budget. I understand the needs you have. I understand the pressures you have. I respect what you have done so far. But I will tell you there is going to have to be a lot of discussion relative to the way we get from point A to point B, and I don't necessarily think we are starting off on a great foot.

Thank you.

Mr. DANIELS. Let me just comment favorably in several cases on things you have just said, Congressman. First of all, it is a good idea to think about people and not unemployment rates. The President certainly thinks that way. We have said the stimulus package, we think, would put 300,000 people back to work. It is the way we ought to think about testimony. It is a very good reminder and we will take that advice.

Secondly, when time permits and you are able to read the budget, I think you will feel better about some of the things you singled out there. First of all, in unemployment insurance, this is a reform which is dollar neutral to the States; and yes, the Federal rate would go down, but we'd like to see the States able to deal with unemployment more quickly and flexibly.

Part of the same proposal is to shift $9 billion that has been piling up in Federal hands to the States quickly as part of the reform. This is meant to be dollar neutral. It is really aimed at creating an unemployment system that works better than the one we have today, which is sort of crazily designed.

Job training, when you are able to read all the way through the budget, you will see we would like to see it go up substantially. We are tying to do two things with job training. One is to raise the amount of money, all things counted, especially these national employment grants that I talked about, or national emergency grants. Secondly, to concentrate the money on the programs that seem to work well.

We have got four programs in ten different departments, all trying to train Americans for jobs. We have tried to zoom in on 28 that seem to be working pretty well. We would like to get more people working, more people into lasting jobs. So we agree with you on that. We are asking for as much LIHEAP money as last year, and we have a substantial carryover. We think we will be in really good shape on that. It is a very important program.

The GME thing, I would like for you to feel a little better. It is a subsidy to hospitals. Fifty-eight hospitals in America get all this money. Three out of four are doing very well. That is $51,000 for pediatricians. We don't think we get any more pediatricians out of it, we just simply fund a few fortunate hospitals a little bit better. We think there are better ways to do this.

And the training of medical personnel. We continue to train primary care physicians through other subsidies, while we have too few nurses and too few minority doctors. So we are trying to direct the funds from these, I would say less effective programs, to health professions' support that meets the needs of today.

But those are all very important questions. We would be glad to follow up with to you make sure you understand how we are trying to address it. We are trying to make forward progress on those fronts.

Mr. CAPUANO. Thank you.

Chairman NUSSLE. Mrs. McCarthy.

Mrs. MCCARTHY. Thank you. Thank you, Mr. Daniels, for the patience of staying here with us.

Mr. DANIELS. I always admire the patience of the people at the far end of these tables more.

Mrs. MCCARTHY. No. 1, before I forget, I would like to ask you to follow up with me also on what you were talking about. I would like to understand the section a little bit better on what you are talking about, nursing and the health care issues, because that is extremely important.

Mr. DANIELS. Yes, ma'am.

Mrs. MCCARTHY. And I am going to be gentle with you on this one. Going way back right, after September 11, we met and we talked about certainly—and this is going off the subject a little bit but it is still going to be in the budget, so it is important. I am a New Yorker. I did read what you said. I have to say I was extremely hurt by it, because we are not that way. We are just trying to protect certainly our victims and our citizens and make sure New York comes back to be the great State that it is.

Now, with that being said, going back to the meeting that we had in the White House with you being there and talking about certainly the monies that would come to New York that was promised. And a promise is, from what I understand when I first got down here, your word is the only thing you have. If you do not have your word, nothing else matters. So I will fight for that. I am going to make sure I keep you to your word on that. You are Irish, right?

Mr. DANIELS. On my mom's side.

Mrs. MCCARTHY. That means you are Irish, by the way, which means you are cursed because you do the same thing I do. I open up my mouth sometimes when I shouldn't. But this is what it comes down to.

Mr. SPRATT. Let the record show he nodded his head.

Mrs. MCCARTHY. I always get censored. See what I mean? What I am saying is that we cannot take the money that was promised to the victims out of that money. I was one of those New Yorkers Congresspeople, that believed the President would end up giving us the money, and more so because we are going to need it. It was very difficult in my delegation because they want to make sure they had the money. I take people at their word. So I want to make sure that you follow that through. Because I will be very honest with you, if we can't keep these promises, then I have to say that

I probably would not trust a lot of the things that were said here today. I mean that, because we are trying all to do the right thing.

We have to win the war. We have to certainly make sure our men and women in the service are getting the services they need and are prepared for it. So I don't think you will find anyone here on this side of the aisle that will disagree with that.

I don't even mind short-term debt, and I don't—if I was going to buy a house, that is short-term debt. Well, in my stage of life, it would be long-term debt. But it is an investment for the future. So I think we all understand that.

But since I have been here, we actually have been trying to bring down the debt.

So with that, I am asking you, are we going to make sure that New York State gets the money that it needs? Are we going to make sure that that $5 billion is not coming out of the September 11 victims' fund? Because I know what those victims are going through. I have gone to too many wakes, too many funerals. They should not even have to go through this stuff, they shouldn't.

If what the President said is true—and I hope it is not—if we have another attack in this country, we have to make sure that we take care of those that have already gone through it. We will have to make sure that we take care of those that might have to go through it. So, with that, I am going to put you on the line.

Mr. DANIELS. I am glad to affirm, again, that the President's commitment from somewhere back in mid-September of $20 billion of aid to New York City is going to be delivered. That is quite apart from the victims' compensation, which, whatever it becomes—and it will be several billion dollars—ought to be viewed separately and apart from that.

I had a chance to apologize to Senator Clinton this morning on the same subject.

Mrs. MCCARTHY. That must have been interesting.

Mr. DANIELS. It was a good exchange. I started by reminiscing that Churchill said he had frequently been called upon to eat his own words and generally found it a wholesome diet.

Mrs. MCCARTHY. Well, you could gain a little weight.

Mr. DANIELS. I tried to make clear yesterday, today, and every day, that the $20 billion is an inviolate number. We are going to go beyond that, it seems pretty clear to me, in terms of total aid to New York. We will go beyond that before the first penny of victim's compensation is counted.

All that I meant to say is that I thought it was fair to the taxpayers of America that someday, when history totals up the final score, that we be given some recognition for this completely unprecedented arrangement to compensate the victims' families. We didn't do it in Oklahoma City. We didn't do it in other disasters. It is a new project. I think it is fair that somewhere along the line it be counted. But it won't be out of the $20 billion, I can assure you that.

The other thing I mentioned this morning, it is especially relevant if Senator Daschle in fact has decided there will not be a stimulus bill, one piece of that bill that the President was looking forward to signing in December was the so-called "liberty zone" concept that I think all New Yorkers are pretty much in agreement on. That is $15 billion of economic activity, subsidized by 5 to $6 billion of taxpayer likely lost revenue. We need a vehicle for that. That is the biggest missing piece of the $20 billion. Particularly if the growth package is now in real doubt, we need to be talking about how to get that done.

Mrs. MCCARTHY. Obviously we were here together and we both heard it at the same time. I don't know what happened over there, but certainly, hopefully, we will find a vehicle to help New York get back on its feet.

Thank you.

Chairman NUSSLE. Mr. Moore.

Mr. MOORE. Thank you. Welcome, Mr. Daniels, to the committee. I think we are about finished here. I want to be gentle with you as well, just as Congresswoman McCarthy was.

Mr. DANIELS. A very healthy trend. I like this.

Mr. MOORE. I do have some questions and comments maybe mostly comments. I would like to find areas of agreement. It is important to recognize where we have differences. But I think it is also very important to recognize that we have a lot of areas of agreement and we should build on those.

I heard you mention early on the difficulty in long-term projections and budgets, things of that nature. I had a proposal last year for a 5-year budget. I would sure like to see us move to something like that. It makes so much more sense than these crazy 10-year projections that we have, because we have all seen what has happened there. We don't need to go through all that again.

I was at the White House last February or March, you were there, when the President had several members over talking about his proposed tax cut which is $1.6 trillion. I was frankly a lot more comfortable with about a trillion over 10 years. But when the Senate worked its magic and the President was willing to compromise, I thought I should as well, and I supported that tax cut to the consternation of some of my friends on this side of the aisle.

I really try to call things like I see them and not go party line all the time. I hope we will do more of that in Congress. I tell my chamber groups and other groups back home what is happening here. And the President, when I talked to him at the White House, I was commenting on the fact that Kansas had three or four tax cuts over the past 4 or 5 years, and all of a sudden the legislature is grappling to find appropriate funding for education because of a revenue shortfall. I said, I don't want that to happen in our country. The President gave me that little smile that he has and he said, Congressman, when we have these surpluses, that is not going to happen. I don't hold him responsible for that. The surpluses are gone. I was wrong and he was wrong, and that is fine. We can get on with this.

I did vote for the tax cut. But what I do want to say is this, I don't have a problem with him on that. I don't have a problem with him on the recession. That is certainly not his fault in my view. And certainly nobody can point the finger at President Bush and say he is responsible for 9-11. Nobody.

But I guess what I want to talk about is, having supported one tax cut in the past is one thing. But I am very concerned with—

the surplus is all gone, that we are talking about a $600 billion additional tax cut.

I appreciated your very candid remarks. You said there is room for some good-faith, honest differences here. Well, if the information here is correct, that what Senator Daschle said is maybe that is not going to happen this year.

But could I have that 2003 deficit chart, please, that Mr. Daniels had here? Chairman Greenspan and other economists with whom I trust have indicated that they think they see the light at the end of the tunnel here, that we are on the way to recovery. If that is the case, as you have indicated, that is a possibility. What I don't want to do is add another $600 billion of debt to my kids and grandkids.

We have fought so hard. I have only been in Congress 3 years, but we have fought so hard to get our financial house in order and be fiscally responsible. I understand and I accept the President's word—I agree with this. There are times when it is appropriate for deficit spending, just as Mrs. McCarthy said: recession, war and national emergency. That is fine. We are there. That is fine if we have to do it. I am willing to support the President on the war, as is every Member of Congress I believe, virtually every Member of Congress.

But I think and I hope and believe that, whatever we do here, we need to keep our eye on the ball and understand that in the future, if we pass these massive new tax cuts or massive new spending programs, we are going to have to live with the consequences or our kids and grandkids are going to have to live with those, No. 1.

No. 2, and I will finish and hear your comments, I was back at the White House I think in early December. At that time I talked to the President about the stimulus package. That is why we were there, and for the trade promotion authority.

But the other thing I talked to the President about was assistance for displaced workers. I asked him if he would support a freestanding bill if it got locked up and the stimulus package wasn't going anyplace, and he told me that he would. I would like to see that happen. That needs to happen.

I have 3,000 Sprint employees in my district who were laid off, lost their jobs. There are people around this country who aren't asking for a handout. They only want a helping hand until they can find a new job. They were taxpayers before. They lost their jobs through no fault of their own. They just need assistance until they can become taxpayers again by finding a new job.

I think the President—I hope and I believe—I know he is going to do the right thing there and push the leadership in Congress to bring up an assistance package. I am talking about unemployment benefits as well as medical benefits for displaced workers. That should happen, in all equity and fairness. We were promised that back at the time—all of us on a bipartisan basis voted for this airport security bill. The leadership and Congress said, take that out, we will pass this bill, and we will come back and pick that up.

Well, the promise was made, and it has not been kept. The President made a promise. As Mrs. McCarthy said, promises and words are important; and I hope and believe the President will keep that promise to—not just to me but to the people in this country, the displaced workers. Because, again, they don't want a handout. They just need a helping hand right now.

Thank you.

Mr. DANIELS. The President has been trying now for quite sometime to get a package that includes exactly the elements you talked about, extended unemployment and help for workers to maintain insurance, medical insurance until they can get back into productive employment; and he is going to be for that in whatever situation we find ourselves.

Mr. MOORE. But if the stimulus package doesn't fly, if it is dead or whatever, I hope that we will move forward on this package.

Mr. DANIELS. I think you are going to find him in favor of that. I think there is a need for caution, because a very bad mistake I think from a budget standpoint and from an economic standpoint would be to have a bill that gets bigger, bigger, bigger with all kinds of spending, all—probably in the name loosely of dislocated workers, doesn't put a single person back to work, only digs us a little deeper temporary hole.

So, if in fact Senator Daschle has performed the last rights over stimulus today, then I think that is the next step, we have got to be careful about that.

Chairman NUSSLE. Mr. Matheson.

Mr. MATHESON. Well, it is the end of a long day for you. I appreciate you taking the time for the committee. I just had a couple of issue areas I wanted to run past you quickly.

Last year, I remember the administration gave Secretary Rumsfeld a very difficult challenge. They asked him to take a look at modernizing and reforming our military to address the challenges of the 21st century.

Obviously, we have had remarkable events take place since that challenge was first given to him, and he has got a very full plate with the war on terrorism. Do you have a sense of where that effort is now in the review process, relative to the large increase in defense spending that is in this budget?

Mr. DANIELS. Yes. It is a very important question. I think as you look at Defense's proposal in the tail end you may get a chance to ask questions of the Secretary and his people. I think you will be encouraged that transformation is moving ahead, may have been propelled ahead by the events of September 11. I think if you talk to folks at the Pentagon that you will hear them saying that that situation and fighting that war has been generating a changed thinking and certainly is reflected in the budget requests that are made for the kind of new weaponry that performs so well there, precision guided munitions and unmanned vehicles and the like.

Secretary Rumsfeld, you may have read in the last week or two, has been in his usual direct and blunt way talking to his department and to the uniformed services about how he is not satisfied that the mentality shift has been clear enough, and he is still hearing too much pre-9-11 thinking, comments like that. So I think you can look for him to be just as aggressive about this as he has been about the conflict in Afghanistan. The administration certainly owes Congress a good accounting on this score.

Mr. MATHESON. I appreciate that. I noticed on Defense it had the red lights across your scorecard.

Mr. DANIELS. Well, you will be shocked to hear that the Department of Defense is not the best-managed enterprise in America. But it is under awful good management now. I think you can be optimistic, as I said earlier, that although we picked problem areas here and, therefore, it is not surprising you see some red lights there, I think you can look for some of those to improve.

Mr. MATHESON. Let me ask you one other—shift to a different issue. That is relative to how Medicare has been treated under the Balanced Budget Act amendment from a few years ago. The notion that here in Congress our Medicare Advisory Commission, we have taken a look at this and feel like the current formula for physician reimbursement is flawed, and I think there is general consensus in both parties that is the case.

There is also a suggested 15-percent cut in home health care agencies. I am wondering if this budget—it seems that it incorporates—it does incorporate that 15-percent cut in home health care. It also incorporates the physician reimbursement cuts that are going to be put in place by the flawed formula. Am I reading that correct when I say that?

Mr. DANIELS. You are. For now it does not contemplate a change, that Congress hasn't flawed in those formulas. I would say that we are certainly open—I think you will find Secretary Thompson also very open to working with the Congress to see if there are ways to look across the whole realm of reimbursement. There may be some areas which are overly generous now that could be used to help level up areas that may be headed for real restrictions due to those formulas.

Mr. MATHESON. Do you think that the current formula for physician reimbursement for physicians is a flawed formula?

Mr. DANIELS. I don't know. It has led, of course, to some healthy increases. Now continuing to apply it literally would lead to some decrease, and that has got people understandably concerned.

I would have to say I take an open mind toward it.

Mr. MATHESON. I would close with your comment earlier about funding for increased nursing. I am interested in that as well and finding ways to maintain the stability of our medical training hospitals.

My spouse is a pediatrician, as a matter of fact; and I am real anxious to enter into that dialogue and learn about what thoughts are to reform the way that we provide a good environment for medical training in this country and medical research.

Mr. DANIELS. We would like to talk to you, to any interested Member about this. We spend a lot of money in this area. A lot of it for a long time has had as its central purpose getting new medical personnel into underserved areas, and yet we have a pretty poor record of that. We have subsidized an awful lot of medical education that did not lead to people serving the underserved communities, and we can do better. That is what some of our changes are aimed at.

Mr. MATHESON. Thank you.

Chairman NUSSLE. Thank you.

Ms. Baldwin.

Ms. BALDWIN. Thank you, Mr. Chairman; and thank you for your testimony and endurance, Mr. Daniels.

The majority of members of this committee in their questions and comments have reiterated that we have no more important role than protecting the lives and the health of the American people, and I agree, and certainly many areas of this budget are relevant to those two topics. I wanted to explore two of them, interestingly two of the ones that the previous questioner delved into, Medicare and defense.

Certainly under the 5-minutes rule you won't have nearly enough time to answer and explore fully the questions in either area, but at least I would like a sneak preview of the administration's thinking, and I know that we can trust you will follow up later with further detail.

First, in the area of Medicare, for the second year in a row those of us who have worked long and toiled hard on the issue of prescription drugs are told that this administration will, if you will, hold that matter hostage to broader modernizations and reforms in the Medicare program. While there are a couple of short-term modernization or reform details that are spelled out, I think we have yet to see a broader sense of what the administration's vision is for Medicare modernization.

As we are very anxious to be able to move forward with assisting—and, of course, every Member hears those painful stories of what our senior citizen constituents go through in terms of struggling with prescription drugs. I, for one, am very eager to hear details about that.

On the defense side, a completely different direction. The data that I have been provided with, background materials from both DOD and OMB, suggests that, of the $48-billion increase proposed for defense, that $16.7 billion of that increase is attributable to the war on terrorism and three on the DOD budgets portion of homeland security.

I presume that another significant chunk of this is the pay increase. I don't know how much that adds up to, the 4.1 percent, if that is what is being proposed, but I would like an outline of what the rest of some $28 billion is being proposed for. What is DOD proposing if it is not for the war on terrorism or pay increase or homeland defense?

Mr. DANIELS. OK. Let me answer briefly, and particularly on the last question I would be happy to, by nightfall, to give you a little something on paper that breaks this out.

But, first of all, on Medicare, the administration, the President is proposing yet again—this is second or third iteration—an immediate help for people who are most in need of prescription drug coverage right now. Reforming Medicare is not going to be an overnight thing. It has proven difficult to get started. The President is not prepared to do nothing on the prescription drug front, certainly for those who are the most exposed to the unacceptable choice between medication and other necessities.

So we have a different approach. Our block grant to States approach of last year didn't seem to generate much traction here. So we have a different approach using the Medicaid program and one we have some hopes for. So we hope that Congress will take a look at that.

Through more flexibility in Medicare over the last year, Secretary Thompson has approved well over a hundred waivers, many of which had been sitting around. When you gave States flexibility, he has gotten a million and a half uninsured people covered in the last 12 months; and we have a new standard waiver that we think will add a lot to that number.

So it takes a little bit the same approach, and we would like to get that done.

Ms. BALDWIN. I do want to steer you back to—we are quite familiar with some of the immediate proposals. But that longer range—I am waiting to hear what the administration's vision is in terms of modernizing Medicare with a prescription drug benefit.

Mr. DANIELS. Sorry for dwelling too long on the near term. But yet I heard you say "held hostage." but that wouldn't be our vocabulary for it, you might imagine. We just think it would be a terrible mistake to have, as some have said, desert before dinner, to put a complete prescription drug program on top of what we believe is a badly flawed and in need of reform Medicare program. We think it ought to be comprehensive reform.

Now the President has laid out some principles for that. I would like to share those with you, and we will.

Let me say that near their heart is the concept of greater choice for people and the opportunity to try to pick insurance coverage that fits their own needs, as opposed to the one-size-fits-all system of today.

On defense, just very quick. Most of the $38-billion defense increase—and you are quite right. There are 10 in addition that are in a contingent request, very much for war fighting that may be required by Presidential decision. But of the 38 you named, most of the big categories, I believe the homeland defense, when you see it all, is bigger than three. It is closer to eight or nine. There are some very substantial costs. For example, for force protection around bases here in the continental United States that contribute to that.

But, most of the 38 I think Secretary Rumsfeld would say is restoration of the base of defense and repair of portions of our readiness and our procurement, our equipment that had been allowed to erode over the years when we didn't pay too much attention to this.

So we will give you a full accounting, but I think you will find that, in addition to the areas you mentioned, personnel and replenishment of munitions, things that are directly attributable to the war, basic readiness and procurement are the two biggest categories.

Chairman NUSSLE. Mr. Daniels, thank you so much for your testimony today. It has been a long day for you.

Mr. DANIELS. We can't keep going? Kidding.

Chairman NUSSLE. We probably could.

We appreciate your testimony. Your budget was on time. Last year, there was quite a folderol about the timeliness of the budget. The budget was on time. And let me report to you in return that our process will be timely as well. We will keep a very steady course in the House. We anticipate that we will have a similar track to what we had last year. By April 15 we will have a budget completed. So we appreciate the work you have been doing with us and will continue to do with us as we try and meet those deadlines.

For my colleagues, 10 a.m., Secretary O'Neil is the next hearing.

If there isn't any further business to come before the committee, we are in recess.

[Whereupon, at 5:15 p.m., the committee was adjourned.]

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