

Center for Strategic and International Studies (CSIS)

Panel One

National Security Implications of America's Debt:

Introduction:

**John Hamre,
President and CEO,
CSIS**

Speakers:

**Robert Gates,
Former U.S. Secretary of Defense (via Satellite);
Admiral Michael Mullen,
Former Chairman of the Joint Chiefs of Staff**

Panel Two

The Bipartisan Plans to Address the Situation

Speakers:

**Erskine Bowles,
Former White House Chief of Staff (via Satellite);
Former Senator Pete Domenici (R-NM);
Former Senator Alan Simpson (R-WY);
Alice Rivlin,
Former Director of the White House Office of Management and Budget;
Former Senator Sam Nunn (D-GA);
Former Senator Warren Rudman (R-NH);
Former Senator Evan Bayh (D-IN)**

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JOHN J. HAMRE: (In progress) – waited for them, I get to start. You know, and we're just going to get this going.

Thank you all very much for coming. My name is John Hamre; I'm the president here at CSIS and very honored that we are given the chance to partner with these other very, very important institutions to bring to the public debate a debate we should be having as a country. You know, I hate to say it, but the news right now is Congress is heading out of town. And I don't know if you saw the poll ratings; it was 12 percent popularity. That's because, for a combination of reasons, they're not doing their job. And we need – we need politicians to help us find solutions for America, more now than ever. And that's the reason that we're offering this with our colleagues, to try to provide a debate that we should be having in America.

I have said on other occasions, we're facing the most perilous time, from a national security standpoint, in my memory. But the threat is not outside the United States; it's inside. It's our inability to get our act together, is in my view the greatest risk we face from a national security standpoint. We want to – we want to drill in on this today. And I want to say a special thank-you to these remarkable leaders who have decided, as – I was talking with Chairman Gray (sp), and he said that he's been spending too much time on the outside avoiding trouble, and now he realizes the country needs him to get in the middle of it to make trouble. And I – I'm very grateful that he's willing to do something like that.

So let me turn it to Sam Nunn, chairman – my chairman. You know, the one thing I will say: When you – when you work for a senator, you work – you work your whole life for them. I mean, and the advantage of coming to CSIS was I get paid working for him. So he's the chairman of the board. So Senator, I turn to you. Thank you very –

SAM NUNN: Thank you, John. Thank you very much. At least I never did to you what David Boren, my former Senate colleague and now president of the University of Oklahoma, did to George Tenet when he was head of the CIA. He used to call him up and get him to make his hotel reservations around the world. (Laughter.) So I – I'm not that bad, John. (Laughter.)

Thanks, John, for your outstanding leadership and for hosting these forums. I also want to thank, again, Warren Rudman, my co-chair at Concord Coalition; Evan Bayh, who is a full partner here and helped plan these forums; and of course Pete Domenici, who will be both a co-chair and a presenter today with Alice Rivlin, Alan Simpson, Erskine Bowles during our second panel. And Pete, it's going to be a great pleasure to have you as a witness today. I have served with you, and we've done a lot of things together, but I've never been able to ask you hard questions. But – so –

PETE DOMENICI: My questions are all going to be deferred, and they're going to be answered by Dr. Alice Rivlin. (Laughter.)

MR. NUNN: (Chuckles.) OK.

In our first forum last week, Jim Baker and Bob Rubin made it very clear that America's present fiscal trajectory and debt are very dangerous to our nation and that a U.S. debt crisis with

little or no warning is a real possibility. In a few minutes we will hear from former Secretary of Defense Bob Gates and former Chairman of the Joint Chiefs Admiral Mike Mullen on their views of the security and foreign policy implications of our current fiscal outlook. So we look forward to that testimony in just a few minutes.

In our second panel today, we will hear from former U.S. Senator Alan Simpson, former White House chief of staff Erskine Bowles, former Senate Budget Committee chairman and our forum co-chairman Pete Domenici, and former Office of Management and Budget director Alice Rivlin. These four individuals will present their findings and recommendations of their bipartisan panels, which were separate undertakings but which came to broadly similar conclusions as to the steps that must be taken in response to our fiscal challenges.

I'm confident that both our panels will address the subject of sequestration or going over the cliff or whatever the title is these days, which by law will occur at the beginning of next year. But I'm hopeful that our discussion will not just include these sequester matters and concerns – very legitimate – but will also engage in the much broader and long-term but essential structural problems and challenges that must be addressed and solved.

Most analysts believe that our lawmakers and the White House will find a way before January 1st to delay the worst effects of sequestration, particularly in the defense arena. Even if this is a correct guess, the threat alone is creating a climate of uncertainty that is harmful to the defense industry, to defense employees and harmful to defense planning and harmful to confidence in America's leadership abroad. Even if we avoid an acute crisis in the short term, interest on escalating debt will increasingly dominate the budget, and interest rates will inevitably increase, putting more and more pressure on all other parts of the budget and certainly on national security and the defense budget.

Trade-offs will become necessary between the size of the active military force and the health of the defense industrial base. This problem is exacerbated by the dynamics within the defense budget itself. The same broad trends affecting U.S. economy are affecting the Pentagon's budget: the rising cost of health care and retirement costs. Other countries, including both our allies and our adversaries, pay close attention to America's fiscal problems. The debt problems makes diplomacy, development and preventive defense less feasible. So shaping the environment, as our military leaders like to say, to prevent war becomes much more difficult. According to the Congressional Budget Office's latest projection, defense spending this year will be just under 20 percent of the entire federal budget, totaling \$670 billion. This accounts for roughly one half of what is called discretionary spending, the portion of the budget not on automatic pilot that is determined through the annual appropriation process. The United States spent more on defense in 2011 than the 13 countries with the next highest defense budgets combined, but of course we do far more, including trying to complete two wars while fighting another war on terrorism every day and maintaining a global presence to protect trade routes and economic lifelines around the globe.

Given the size of the defense budget, it is clear that any credible approach to deficit reduction must include defense, as well as other parts of the federal budget. We must not, however, bang away with a mindless sledgehammer. We must manage effectively and cut

wisely over time, over time, with the security of our nation as the top priority. Both federal revenues and expenditures are shaped by our national economy, and in a democracy, they are shaped by the public need.

We cannot divorce the debate over national security from the fact that since 1960, our national spending, both public and private, on medical care has gone from 5.7 percent of our gross domestic product to over 17 percent, and is rapidly heading toward 20 percent. Neither can we ignore the reality that our population is steadily aging. We live far beyond the age of 65 that marked life expectancy when Social Security was created. Not sure of the last numbers on life expectancy, but it's in the mid-80s. That makes a huge difference. Social programs that were created with the expectation people would live to the age of 65, and we're now, thank God and great medical developments, technology, we're living much, much beyond that. But the social programs and the funding of those programs have not been fundamentally redressed to reflect that reality. These trends profoundly affect our economy and our well-being, and certainly affect our nation's security in the broader context.

Finally, since we here at CSIS – we're here at CSIS and we're holding three of our four forums here – since CSIS is one of the world's premier defense policy institutes, and since one of the founders of CSIS was Admiral Arleigh Burke, and since Tony Cordesman holds the Burke Chair, let me quote from Tony's recent report on the defense budget and our fiscal crisis. (Inaudible) – quotes from Tony – and they're not necessarily in the order he made them, so I'm summarizing – number one: The United States still dominates world military spending, but we must recognize that maintaining the U.S. economy is a vital national security interest.

Number two: The U.S. military and national security spending already places a lower burden on the U.S. economy than during the peaceful periods of the Cold War, and existing spending plans will lower that burden further in the future.

Number three: The Department of Defense needs to make a major new effort to deal with its own self-inflicted threats, lack of cost control and realistic planning of future budgets, plus the massive rises in the cost per soldier on active duty.

Continuing, quote, from Tony, number four: The real pressures on federal spending are driven by entitlements, which are driven by the fact that most Americans do not save adequately for retirement and massive rises in the burden of all medical care costs, government and private, and the pressures they put on the economy, end quote.

So I commend Tony and the CSIS national security team's report for all of those who are interested in national security as well as economic security and who would like some relief from the current campaigns' flawed addition and subtraction; at least, that's my view.

Again, I thank our steering committee members who are with us today: Bill Brock, I believe Bill Frenzel – did Bill get here? – here, Bill Gray and Jane Harman have joined us. They were members of the steering committee, and they've joined us today. We're very delighted to have them and Tim Roemer, former United States congressman from Indiana and former ambassador to India, who was with us in our first forum.

I'd also like to again thank the organizations that have made these forums possible: CSIS, the Concord Coalition, the Bipartisan Policy Center, as well as the American Business Conference, the James A. Baker II Institute of Public Policy at Rice University, the Belfer Center at Harvard University and the Hoover Institute at Stanford University.

Pete, let me turn to you, and then we'll hear from other committee members, and then we'll get to our witnesses.

PETE DOMENICI: Thank you – thank you very much, Sam, Mr. Chairman. And let me say what a pleasure it is to serve with you. And please, if there's – if you have a shortage of time, just let me know. I need not really make these opening remarks if you have them reserved for someone else, but I'll try to be very brief.

First of all, it's an honor to have these two participants, patriots, with us today. The nation owes them both a very, very large debt of gratitude. Admiral Mullen, though you are far away fiscally from us, we have used some of your quotes extensively the past several days so that your words are right here with us today.

Secretary Gates, you will come to us from your – from where you are in Texas. And many of the reforms that you have advocated in defense spending have guided the work of the Bipartisan Policy Center Debt Reduction Task Force, which I co-chaired with Dr. Alice Rivlin – that is, your reforms permitted and justified us making some substantial reductions in defense, but nothing like the bludgeon that will occur under the sequester order that is already law.

You've also guided us and work of our analysts of the impact of the defense sequester on our national security and the nation's economy. We face these mindless, across-the-board cuts, called "fiscal cliff" by some, because policymakers have failed in their fundamental responsibilities developing fiscal paths that give the nation both long-term debt reduction and short-term boosts to economic growth.

The failures of the past several years and especially the past 18 months have led the nation to a – to the edge of this cliff. I cannot imagine a worse way to reform defense spending and procurement of defense needs than using the instrument we call "sequester." Our Chairman Nunn has said this is almost a suicide pact. That is true. If you don't do fiscal change just the way we want, both poles in the debates say, then we are going to shoot ourselves by using the sequester. I don't know where we will shoot ourself, but it will be lethal for certain.

We will be refreshing to hear from both of you today your recommendations and thoughts. There are no more qualified individuals to let us know the relationship between fiscal policy and the – and American security. It is my pleasure to be able to participate, and today I get to share a – with the committee a proposal that we put together as an alternative to that one that was put together by the president's commission. And we will then look at the overall picture, including defense and all the other things, and see how we can get out of the mess we're in.

One last remark: I was thinking to myself, how many meetings have I attended where we have addressed this issue? How long has it been front and center in the minds and hearts of those that know and love America and those in positions to know and do something about it? For many, many months, if not few years, we know we must fix this. But somehow there's – it doesn't get across, and those who say it to the people of our country, who some way or another don't quite feel it and don't quite believe it. We don't want to wait until it happens and then say, you see? We said it would happen. America's gone over the cliff. Our dollars have gone. Our U.S. dollar is no longer the value of the world, and we're in one mess as a nation. We don't want that to happen. We want to fix it first. That's what this is all about.

Thank you.

MR. NUNN: Thank you very much, Pete, and I see John Tanner joined us. John was at our first forum, and we're glad to have you again, John, former congressman from Tennessee. And Jane Harman, we're delighted to have you here today. And since you didn't make the first forum, we will give you a few minutes for whatever comments you'd like to make. And Bill Gray, we're delighted to have you join us today. Bill, former congressman from Pennsylvania and former chairman of the House Budget Committee.

Jane.

JANE HARMAN: Thank you, Sam. Sitting here with former colleagues and dear friends, I can't help but observe that security is also a woman's issue. I served in – from – I served in Congress for nine terms from the heart of California's aerospace industry and was on all the major security committees, Armed Services, Intelligence, where Tim and I served together in Homeland Security. I left last year to succeed Lee Hamilton at the Wilson Center. Today is the Jewish New Year, and at Temple this morning, I prayed for peace and prosperity both at home and abroad. My Sunday school teachers taught me that you pray not to be given something, but for the will to do something. So I've decided to come here this afternoon to do something about our budget and national security.

Last Friday, the White House released a report detailing the chilling potential effects of sequestration on every aspect of military procurement and operations. Particularly alarming given last week's attacks on U.S. and other embassies and consulates abroad is that diplomatic programs and embassy security would lose \$1.2 billion. I know, and many of us up here know, that with political will, we can avoid this because we've done it before. I was in Congress – most of us were – in the '90s, when we worked together to balance the budget and did this in 1997. Five years of prosperity followed. Then came 9/11. The world changed, and our budget discipline collapsed, and now that vote – that 1997 vote, 15 years ago, seems far, far away.

On Wednesday, the Wilson Center will roll out the election edition of Budget Hero, a serious game that enables people to see the hard choices necessary to regain fiscal sanity. More than 1.2 million people have played the game already, and this audience should check it out on our website. I've devoted decades to protecting our national security and still serve with some others here and with Mike Mullen on boards relating to our defense and intelligence agencies. I know that we cannot maintain our national security without economic security. I also know that

we won't restore economic security without – (audio break) – the hard choices about spending, tax policy and entitlements.

When I was elected to Congress in 1992, we were expecting a peace dividend, but a peace dividend is still not here, and I fear it never will be unless we correct our economic course and do something. May the year 5773 bring us peace, prosperity, bipartisanship and fiscal health.

MR. NUNN: Thank you very much, Jane, and thank you for your service in Congress and your leadership of the Wilson Institute. We at CSIS value our many working relationships on different projects with you all.

Bill, do you want to say a few words, do you want to reserve a time for asking long questions?

MR. : I would like to reserve my time so that I can ask questions.

MR. NUNN: (Chuckles.)

MR. : You don't need a speech from a former member of the House and a Baptist preacher and a college professor. (Laughter.) We don't have enough time. (Laughter.) I'm just honored to be here, and I'm particularly honored to be sitting next to my dear friend, Pete Domenici, whom we had many, many discussions back in the '80s when he was chairman of the Senate Budget Committee and I was chairman of the house, and I think we cut the deficit in half back in that four-year period, but everything that Pete has said, I would agree with, as well as Jay. Thank you.

MR. : Thank you very much.

MR. NUNN: Thank you very much. Any other member of the panel want to make any comments at this point?

Admiral Mullen, we're delighted to have you here today, and so if you could go up.

(Applause.)

We're honored to have Admiral Mike Mullen with us today, the 17th chairman of the Joint Chiefs of Staff. Admiral Mullen spent 43 years in the U.S. military after graduating from the U.S. Naval Academy – an incredible life of leadership to our country. Many of you know that Admiral Mullen is – (audio break) – since 2010. Admiral Mullen has said a number of times that he believes the national debt is the single biggest threat to our national security. When Mike Mullen says this, he is not trying to enter or shape a political debate. He is simply giving his best advice and counsel to a country that is served – he has served for four decades. I know that Mike steadfastly believes that the military, active and retired, needs to stay above the political fray, particularly in this environment, and I'm certain that he will do that today. But he agreed to join us, from my perspective, for a very simple reason: his continued love and service to our nation.

Admiral Mullen knows that our national leaders of both parties need to address the debt or it's not going to – or it is going to undermine everything our war fighters need to succeed in everything they are willing to fight and die for. Admiral Mullen, I'm deeply grateful for you being here today. I can't think of any two people more qualified to speak to this issue than you and Secretary Gates, and he will be coming in by satellite. It's my understanding that you will go first. Is that the preference?

ADMIRAL MICHAEL MULLEN: Your understanding is always correct.

MR. NUNN: Thank – introduce Bob Gates in just a few minutes. I'm not sure whether Bob is on yet – is he on, do we know?

(Off mic.)

OK. So Admiral Mullen, why don't you go ahead?

ADM. MULLEN: Senator Nunn, Senator Domenici and other distinguished panelists, I greatly appreciate your putting this group together and your leadership on this critical issue. Actually, when you're serving in uniform as I did for many years and you go to so many different hearings, you're always looking forward to the last one, and I guess this proves that there may never be a last one, even after you leave. I really do appreciate the opportunity to be with you today, along with my good friend and colleague Bob Gates, to say a few words about the difficult and critical issues of our country's national security and economic health.

More than two years ago, while serving in the position of chairman of the Joint Chiefs, I was asked a routine question by a reporter that went like this: What is the most significant threat to our national security? My response was straightforward and simple: I said, our debt. Since then, I've been asked time and time again about that threat, and I've answered the same way. A nation with our current levels of unsustainable debt, being this far out of fiscal balance, cannot hope to sustain, for very long, its superiority from a military perspective or its influence in world affairs. That was not intended as a partisan statement then, and it has no partisan meaning now. To broaden somewhat that two-word answer, I was using our growing and unsustainable debt as shorthand for the abundant disorder in our fiscal house, brought upon us by ourselves by our own doing.

While much has been said since then, little has changed. In fact, I would argue that the mere passage of time, combined with a lack of solutions in the interim, has compounded the problem as our debt increases seemingly exponentially, and solutions that require compromise seem but a figment of the imagination. In approaching this issue from a national security perspective, it is the brutal combination of the passage of time and no solution in sight that so intensifies both the crisis and the threat. Already, the president has reduced the fiscal year defense – fiscal year '13 defense budget by almost a half a trillion dollars, a reduction which I supported when I was chairman, and still do. Under the current construct, DOD will soon sustain another half a trillion dollar cut not shaped in any way by any kind of national security strategy. Civilian agencies, mind you, will undergo the same meat ax treatment, unable to tailor

necessary spending reductions in such a way as to strengthen, not weaken our country and its future.

And all of this will take place in a world of great and growing uncertainty. One only need look at the events of the last week, even as some areas of the world grow increasingly dangerous and hostile to the United States. The fiscal crisis is peaking at a time when our extraordinary military and their families are stretched and stressed as we begin our 12th consecutive year at war. It would also behoove us to remember that while we remain mired in the fiscal morass, almost 70,000 troops are still in harm's way in a war in Afghanistan. We also have a couple of hundred thousand more deployed and stationed around the world doing our nation's bidding in faraway places as they have done for decades.

Our military missions and requirements abroad must and will continue while our ability to resolve our own differences here at home remains paralyzed. I'm also mindful that today is the 225th day of the signing of our Constitution, one of the most important and ageless documents in political history, whose very framing signals the compromise that was necessary to found this country. Our tendency after war has always been to come home and isolate. This response could be accelerated by dramatically and recklessly reducing budgets, following no principle except the need to hit a number. Our isolation would make us – make a dangerous world more so. These times are different from the '40s and the '70s and the '90s. Huge and poorly targeted national security budget reductions will badly undermine our national security interests. I recognize that we face historic economic challenges that every – at this time, and that everything must be on the table, including defense spending, which I have said before. DOD must pay its fair share, but if we actually zeroed the defense budget, we would hardly make a dent in our debt. It is possible that our continued irresponsibility could cause huge and poorly targeted budget reductions in defense, unless we arrest and turn around the decline. This virtually guarantees that we would end up with a hollow force, a force unable to conduct its training, a force unable to maintain its equipment, and a force unable to fight, a force also unable to readily recover from the ravages of over a decade of war.

My intent today is not to point a finger, for I don't have enough fingers to point, nor to affix blame, for there is plenty of that to go around. My urgent appeal is to get to the higher ground, and to do so sooner rather than later, together. There will come a time when we try to kick the can, but we will find that the can will not budge. Resolving this crisis will be a process that needs to start now. Engaging it with determination will assure the prosperity of our children and our grandchildren. Doing nothing will compromise it.

Since I retired almost one year ago, I have visited many parts of our great country. I have not met one American citizen who is not extremely worried, and who does not want this problem of our growing debt solved in a mature and foresightful (ph) way. I worry that the time to do so is actually shorter than we realize. We are steadily being drained of our great economic strength, while our national security strength is being sapped as well. Lastly, I worry that my generation, the boomers of the Vietnam era, will, for the first time in American history, leave our precious country to those who follow us in worse shape than when we received it. This is a legacy for which we should all hang our heads. We are bigger and better than this. We are Americans, and nothing is impossible.

Let me – (audio break) – also just pick up on one point that Senator Nunn mentioned in his opening comments, with respect to Cordesman’s quotes, and that is the cost per – (audio break) – soldier, sailor, airman, and Marine of our force, which has doubled to trebled, depending on which statistic you believe. But this has been something that we’ve all participated in, and strongly endorsed since the mid-’90s. And in doing that, we invested in our people. And it is – this – actually less than 1 percent – it’s a different 1 percent comment. It’s this less than 1 percent who have borne the burdens of these last two wars, who have in – (audio break) – too many cases, paid the ultimate price by over 7,000 or so, tens of thousands who have been wounded physically, visibly and invisibly, and hundreds of thousands who bear other wounds of these wars, to the tune of over 2 million who have served in Iraq and Afghanistan, and over 2 million today who are making us proud. So as we take up this debate in terms of our future, and in particular, with respect to defense, I’ve said many times, the thing we need to get right to ensure our military is in good shape for the future, is make sure we get it right for our people and their families. That’s not just a cost or a budget item, that is the strength of who we are as a military; and as a military, having fought two wars in this all-volunteer force for the first time, that we have a pretty healthy discussion about what that means, coming out of these wars, even as we have 70,000 still exposed in Afghanistan today; what that means for us as a country, and what that means for us as a military, as we look forward to the security requirements, which seem to always be there, that will challenge us both here at home as well as globally around the world.

Thank you again for the opportunity to speak to these critical issues. They touch the core of our future as a nation of greatness, and I believe that greatness can and must be sustained. And I also begrudgingly look forward to your questions. No, I’m kidding. (Laughter.)

Thank you, sir.

MR. NUNN: Thank you very much, Admiral Mullen – (applause) – for your powerful testimony and your continued service to our nation. I’m not informed as to whether Secretary Gates is – (audio break) – the satellite yet, can somebody inform me of that? Not yet? OK. (Audio break.) – the good and bad news is, we can start asking you questions. (Laughter.)

AUDIENCE MEMBER : Can I take attendance?

(Audio break.)

(Laughter.)

MR. NUNN: I’ll just start with a question about – very simple. What makes this unique? You’ve been through wars, you’ve been through a career where we’ve had the budget, defense budget going up and down after wars, as you’ve already observed. Is there anything particularly unique about where we are right now, compared to previous periods of history, on the fiscal side?

ADM. MULLEN: Before I was chairman, I spent a lot of time in the Navy, in the money world. So I grew up in that world, intimately familiar with both the programming and the budget side of that. And right after the Cole, actually, and just prior to 9/11, I returned to the Pentagon to be the Navy’s budget and program officer. And part of what then-Vern Clark, who was the head of the Navy, was certainly counseling us on, and what I focused on, was the historic ups

and downs of the defense budget. And in fact, if you go back and plot it to as early as 1935, you would see it goes up and down at a pretty steady pace, over the course of 18 to 19 years, through peace and through war. So I certainly as a budget officer over 10 years ago fully expected that we would tip – the budget would tip over. What I didn't anticipate was that it would be at a time where the country was in such a fiscal crisis.

So it makes it much more difficult on the, from the defense standpoint, to basically plan for the future. I mean, Chairman, you know we typically do this about five years out, and it is a, it is – historically, it's a pretty good plan. Oftentimes, over program, sometimes, more hopeful in certain areas, but it's a long-term plan that looks at capabilities that we need. That is not done so, in other portions of our government, and that just speaks to the degree of difficulty that other portions of our government will have if this budget reduction happens as it appears to be slated to in January.

So I think more than anything else, Senator Nunn, it's the intensity of this, the inability to plan for it. I'm enough of a budget guy to know that, you know, budget people love just to go to numbers. And so from a macro standpoint, we're really focused on doing that without any thought or strategy, as soon as January comes around. I'm not as hopeful as others that we won't drive off this cliff. I'm worried sick about it, quite frankly, and I certainly hope we don't. It already – and this is – goes to another quote from Andrew – already the controllers in our government are pulling back. Already there are plans, wherever the – this ax may fall, to not spend money this year, as we get to the end of fiscal '12 and get into '13. So probably more than anything else, I think it's just the intensity of it, and at a time obviously when we have fought and – fought in Iraq and come home and are still fighting in Afghanistan. So from my perspective it's somewhat unique.

MR. NUNN: Thank you very much, Admiral Mullen.

I've got good news: the secretary of defense is no longer AWOL – (laughter) – so he's coming – ready to come in on satellite. So we'll come back to the questions for both Secretary Gates as well as for Admiral Mullen. Let me introduce Secretary Gates briefly, and then we'll hear from him. And this will be a very abbreviated introduction; could go a long time talking about his record – as well as, of course, Admiral Mullen's record.

On June 30th, Secretary Gates retired after serving four-and-a-half years as secretary of defense under President George W. Bush, as well as President Barack Obama. Dr. Gates has served eight presidents in a number of leadership roles, including director of Central Intelligence Agency and deputy national security adviser. Dr. Gates was sworn in on December 18th, 2006, as the 22nd secretary of defense. Before being named secretary of defense, Dr. Gates was the president of Texas A&M University, the nation's seventh-largest university. Prior to assuming the Texas A&M presidency, Bob served as dean of the George Bush School of Government and Public Service at Texas A&M from '99 to 2001.

Dr. Gates has been awarded the National Security Medal, the President's Citizens Medal – or Presidential Citizens Medal and has twice received the National Intelligence Distinguished Service Medal and has three times received CIA's highest award, the Distinguished Intelligence Medal. On his last day in office, President Obama awarded Dr. Gates the Presidential Medal of

Freedom, America's highest civilian honor. Suffice it to say that Bob Gates is one of the most honorable and effective public service – servants I have known.

Secretary Gates, we are deeply indebted to you for being here, and I'm told that you're about to appear on our screen. And Admiral Mullen has made a statement, and we will have a few questions for both of you at the conclusion of yours.

(Technical difficulties.)

ROBERT GATES: All right. Well, thank you for this opportunity to address a topic of immense importance to the future of this country. And thanks also for the opportunity to be back in harness with my good friend and colleague, Mike Mullen. First, I'd like to share my personal perspective on how the American political system reached the current impasse. And second, I'd like to address the role of defense spending in the context of the country's wider fiscal troubles.

No doubt the United States faces a serious fiscal predicament that could turn into a crisis of credit, of confidence, of our position in the world if not addressed. At some point, financial insolvency at home will turn into strategic insolvency abroad. We are not there yet, but the longer the United States government delays in dealing with the country's long-term fiscal problems will only make dealing with them later more painful and potentially more risky in terms of national security.

We will get a preview of how damaging this scenario could be at the end of December, when hundreds of billions of dollars in mindless across-the-board spending cuts will take effect for 2013, adding up to more than \$1.2 trillion in reduced discretionary spending over the next decade, half of that coming from defense. The result would be grave damage to the U.S. military, homeland security, aviation safety and virtually all other essential government operations. According to most experts, taking so much money out of the U.S. economy so soon and without any strategy, rationality or prioritization would likely send the country back into recession, thus only worsening the government's fiscal situation.

In order to maintain strong institutions of national defense and international influence, the United States must get its government finances in order. Doing so requires our country's political class to show leadership and make decisions that may be unpopular in the short run but will strengthen the country for the long haul. So far there appears to be little evidence that this is taking place. Though American politics has always been a shrill and ugly business going back to the Founding Fathers, as a result of several polarizing trends we have now lost the ability to execute even the most basic functions of government, much less solve the most difficult and divisive problems facing this country.

There are a variety of reasons, some structural, some historical, some outside the control of government: first, the highly gerrymandered system of drawing congressional districts to create safe districts for both Republican and Democratic incumbents, leading most elected representatives being totally beholden to their parties' most hardcore ideological base; second, wave elections that sweep one party into power after another, each seized with ideological zeal and the rightness of their agenda, making it difficult to sustain policies and programs consistently

over time; third, the decline of congressional power brokers, particularly the committee chairs, who might have been tough partisans but were also people who could make deals and enforce those agreements on their committees and their caucus; and fourth, a 24/7 digital media environment that provides a forum and wide dissemination for the most extreme and vitriolic opinions, leading, I believe, to a coarsening and dumbing-down of the national political dialogue.

As a result of these and other polarizing factors, the moderate center, the foundation of our political system, is not holding. Moderation is now equated with lacking principles. Compromise means selling out. So just at a time when this country needs bipartisan strategies that can and must be sustained through more than one presidency and more than one Congress to deal with our most serious long-term problems, most of the trends are pointing in the opposite direction.

Critical ideas and progress in our history often have come from thinkers and ideologues on both the left and the right. But the laws and policies that ultimately implemented the best of those ideas have come from the vital political center, usually as a result of compromise.

At a time when our country faces deep economic and other obstacles at home and a world that just keeps getting more complex and more dangerous, the inability of so many political leaders today to step outside their ideological cocoons or offend their most partisan supporters has become a real threat to America's future.

Across the spectrum, too many of our politicians seem more concerned with winning elections and scoring ideological points than with saving the country. My hope is that following the presidential election, whatever adults remain in the two political parties will make the compromises necessary to put this country back in order. Doing so would remove the economic pall that hangs over the American economy at home and American power and credibility overseas.

Now let me address the defense budget and what role it may play, or, in my view, does not play, in addressing our country's fiscal challenges. As a starting point, it's important to remember that defense expenditures are currently a lower share of our gross domestic product than for most of the last 60 years, and a much lower percentage than during previous major wars. And lest anyone forget, there is still a war going on in Afghanistan.

Consider that when President Eisenhower warned of the military-industrial complex in 1961 defense consumed more than half of the federal budget, and the portion of the nation's economic output devoted to the military was about 9 percent. But comparison, the defense budget, when I left the Pentagon, was \$530 billion. A huge sum, to be sure, yet that budget represented less than 15 percent of all federal spending and equaled roughly 3 ½ percent of GDP – a number that climbs to a little more than 4 percent when the war costs from Afghanistan are included.

Seeing the bleak fiscal outlook ahead, during my last two years as defense secretary I sought to prepare the Pentagon for the inevitable flattening and eventual decline of the defense budget. The first stage, beginning in the spring of 2009, dealt with procurement. And all told,

more than 30 defense modernization programs were cancelled or capped that if pursued to completion, I was told, could have cost the taxpayers \$330 billion. The last budget I – request I submitted in February of 2011, included nearly \$80 billion in additional reductions to the five year defense program.

Then the Budget Control Act, signed later that year, required nearly \$490 billion more in defense cuts over a decade. So by around the time I retired as secretary of defense in the summer of 2011, defense spending had already been cut by nearly \$900 billion over the next 10 years. And that was before we have to deal with the nearly \$600 billion in defense – in reduced defense spending authority that would result of sequestration takes place.

In short, contrary to popular concession – conception, the defense budget already has been cut, and substantially. What remains in our military modernization accounts are much needed capabilities relating to air superiority and mobility, long-range strike, nuclear deterrence, marine – maritime access, space and cyberwarfare, ground forces, intelligence, surveillance and reconnaissance – capabilities that our nation’s civilian and military leadership deem absolutely critical to the future. And while there’s no equivalent of the former Soviet Union looming on the horizon, I do believe the threats America face today and down the road are, in many respects, more dangerous for their complexity, variety, unpredictability and likelihood.

Let me be clear, not every defense dollar is sacrosanct. One need only spend 10 minutes walking around the Pentagon or any major military headquarters to see excess and redundancy. That’s why I initiated an effort in 2010 to wring \$100 billion more in overhead efficiencies out of the department over four years. Yet we should not fool ourselves that significant defense budget savings are possible, the kind that might put a dent in the annual federal deficit, without making substantial and, in the case of sequestration, very destructive cuts to the ability of our military to defend the United States and our vital interests around the world.

Consider also the wider fiscal picture. The defense budget may have to be on the table as a matter of political reality, but as a matter of simple math it is not fundamentally the cause of the long-term debt problem. Roughly two-thirds of all federal spending going to entitlements whose share of the budget is escalating rapidly given the changing demographics of the U.S. population. Reducing defense spending by, say, even 15 to 20 percent in the near term would reduce the current annual budget deficit by just one-tenth – ten percent. But cuts on that scale would require dramatic reductions in the size, reduction and overall – size, readiness and overall capabilities of the U.S. military.

And we need to be honest with the president, with the Congress, with the American people and with ourselves about what those consequences are – that a smaller, less ready, less modernized military will be able to go fewer places and be able to do fewer things. And the risks to our men and women in uniform will only increase. If our elected officials and body politic conclude that they truly want a diminished role for the United States in the world, then we can start paring back missions and ratcheting back the corresponding military investments in force structure. If future defense reductions cannot be avoided, they should be phased in slowly, methodically and strategically, in a way that protects our core security interest and does right by those in uniform.

But the history of past defense drawdowns is not encouraging in this regard. We almost never get it right because no matter how many times we say never again to particular kinds of military operations, America's adversaries will always have a vote, as will our future presidents. And if the history of the past century teaches us anything, it is that cutting defense too deeply too quickly, will lead ultimately to higher costs in blood and treasure later.

Since I entered government 45 years ago I have shifted my views and changed my mind on a good many things as circumstances, new information or logic dictated. But I have yet to see evidence that would dissuade me from this fundamental belief: that America does have a special position and set of responsibilities on this planet. This status provides enormous benefits for allies, partners and others abroad to be sure, but in the final analysis, the greatest beneficiaries of American leadership in the world are the American people in terms of our security, our prosperity and our freedom.

In closing, while my presentation today is no doubt sobering and at some points dire, I still remain fundamentally optimistic about the future of this country. Even though the United States faces enormous obstacles, most of them self-inflicted, we also have the power and the means to overcome them, just as America has done in the past. Think about the early years of the Cold War in the late 1940s, an era in which politics was every bit as ugly and confrontational as this country has seen before or since.

MR. GATES: President Harry Truman was a loyal Democrat and a tough partisan. In his 1948 acceptance speech at the Democratic convention, Truman referred to Republicans as the, quote, common enemy who want to stick a knife in the backs of the poor. Republicans called for Truman's impeachment or worse on a regular basis. Senator Robert Taft, the de facto Republican leader in the Senate, said famously, the purpose of the opposition is to oppose, and he meant it.

Yet in the end, it was that early – in that that earlier, hyperpartisan environment, it was members of that opposition, Republicans like Senator Arthur V. – Arthur Vandenberg and Representative Richard Nixon, who in the face of a war-weary and skeptical American public helped Truman pass the Marshall Plan that saved Western Europe from Soviet domination. Republican support was also critical to the passage of aid to Greece and Turkey, which first put the strategy of containment into action, to the creation of NATO and to virtually all the farsighted policies and institutions that have sustained American security for the past seven decades.

Looking ahead, it is unrealistic to expect partisanship to disappear or even dissipate. But when push comes to shove, when the future of our country is at stake, ideological zeal and short-term political calculation on the part of both Democrats and Republicans must yield to patriotism and the long-term national interest. All told, whether the United States sustains our global economic, political and military pre-eminence will depend not on the actions of other countries, but on what we choose to do, the compromises we forge, the sacrifices we accept and the courage and unity we demonstrate.

Thank you. (Applause.)

MR. NUNN: Thank you very much, Secretary Gates, and I hope you can hear us. We heard all of your statement. It was loud and clear. You and Admiral Mullens (sic) have made two very powerful statements that I hope will be heard throughout our country, and particularly by policymakers and elected officials.

I'm going to turn to my colleague Pete Domenici for a first question here, and then we'll rotate to the panel.

MR. DOMENICI: First of all – first of all, let me thank you, Senator Nunn, for asking me to be a co-chair of this with you. I never thought that we would be this far, this quick in getting the issues formulated and out to the public, and I believe today is an exemplary one of getting the true facts as to how bad off and – the United States is because of the lack of leadership, the lack of comity, the lack of getting together and agreeing, the lack of, in some way, the leaders of the – of our – (audio break) – bodies, our legislative bodies and others in leadership positions don't quite get it.

Secretary Gates said that the – we'd wait for the adults to come back from – (audio break) – campaigning. Let us hope that those adults from – are from both parties. Let's hope they are willing to give and compromise in the best interest of this great country.

I had the chance to talk to you, Admiral Mullens (sic), before this event, and seek, as strongly as I could, that – your affirmance – (audio break) – coming here today, and I can't – I can't say it any other way but that it was absolutely imperative that your answer was yes and that you came here today. Between you and the secretary, we have heard the best evidence, in my opinion, on the need for adequately providing for our defense on the one hand, and on the other hand, for not enforcing the sequester, which is upon defense and all of the other domestic programs of our country.

So let me ask both of you a question. I would assume that both of you have had an opportunity to review the sequester and what it – what its effects on the Defense Department and our people and personnel will be. Is that a – is that a fair assessment, that you're aware of the sequester's – both of you are nodding yes.

So let me say to just back up your testimony that sequester is an across-the-board cut order of defense and of domestic programs from – (audio break) – a given point. It is already a law – (audio break) – public – people should know that. It became a law by default. Is that not correct, Admiral Mullens (sic)? When the – when the supercommittee did not get its work done, the backup position was, therefore we will get savings by a sequester. And this document was written, and this document called sequester was passed by the Senate, by the president, as part of that package – (audio break) – that encompassed the supercommittee.

Now, I would like you to answer it with as much – (audio break) – adding to it as you can and want. Do you think we should render the sequester valueless? Do you think it should be

pulled? Do you think that we should – that leaders of this country should take it out now so it will not become effective? I guess I'm saying, what will the effect be if this sequester is permitted to be carried out? Would you answer that question, please? Let's start with the admiral.

ADM. MULLEN: This – with respect to the damage of the sequester specifically – and I don't know if it's widely known; certainly it's widely reported that the president both has the authority and would intend to exempt military personnel from sequestration. Obviously what that then does is put the full burden of the amount on the remainder of the defense budget. And going back to my times when I was the head of the Navy, roughly 50 (percent) to 60 (percent) to 65 percent of my budget went to – (audio break) – people, active, retired. This is benefits, et cetera. So, in fact, the full burden of sequestration would be put on roughly 50 percent of the entire defense budget, which makes its implementation that much more extreme.

Secondly, from my perspective, it's really why I talked to a hollow force, because in execution, which is what we would be in, it's very difficult to find monies – significant amount of monies, which will be under contract already, so you can't undo that. So you get to the operations and maintenance funds, if you will, which are significant, and you start pulling the training money, the logistics money, the maintenance money, because it's money you can get your hands on in the very near term. So the intensity of moving to what I would call – despite the Pentagon's strong desire to not go there, to move to a hollow force is that much more significant.

And then thirdly, I would speak to just the sequestration part of the act itself. And I think many people know this. It was described by Bob Gates' successor to me as – Secretary Panetta – as a neutron bomb, and the idea being that it would be something that would be unthinkable in any way, shape or form so that a solution or a compromise would get generated.

With respect to answering your question about whether it should be pulled or not, I guess I'd think about that in terms of motivation. I think we need to really take steps to solve this problem now. I think sequestration and execution would be incredibly damaging to – (inaudible) – defense and our national security interests. That said, if there isn't that hanging over their heads – and you would be much wiser in terms of reading this than I – what hangs over their heads to get them to a point where they would make the decision? I just don't know the answer to that.

MR. : Secretary Gates, I hope you're following this from your locale, but anyway – (audio break) – each question is also to you, if you want to take a crack at it.

MR. GATES: Sure. Sequestration reminds me of the scene in “Blazing Saddles” where the sheriff holds a gun to his own head and warns the crowd not to make him shoot. This is no way to run a government. Across-the-board cuts are the worst possible way to exercise – (inaudible) – discipline. Even before sequestration, when Mike and I were working together, my guidance was that if we had to deal with budget cuts or we needed to find more resources, we would never resort to across-the-board cuts. I referred to it as managerial cowardice – a refusal to make choices and establish priorities. Sequestration does all of that on steroids. And I think

Mike has spoken to the problems that we will face. But the realities are you're talking about pilots – fighter pilots who will have less time in the cockpit, less time flying, soldiers who have less time to train and fewer bullets to – (audio break) – train with – these are the concrete realities – ships that have to stay in port because they can't – we can't afford to run them.

And that's what I was referring to in my remarks when I said, sequestration will increase the risk to the lives of our men and women in uniform, because the things they do to be prepared, they will have to stop doing. And so, again, as Mike has suggested, I don't know the right solution for getting out of the sequestration mess, whether it's pulling it or trying to buy some time or whatever. But what we do know is that the consequences for our military will be dire. And I think the administration during this past week has outlined what the other costs will be outside of the Defense Department, in terms of air traffic control, in terms of the national parks, in terms of virtually everything the national government does. And so – and they will be hit with the same kind of mindless lack of prioritization that everything takes a hit, the important and the unimportant. So it is – it is a – it's a catastrophic way to deal with the deficit issue, and in some way needs to be found to do what Mike has suggested, and that is, how do you sustain the leverage on the members of Congress and the president to come to the kind of agreements that are necessary to get our fiscal house in order without threatening to shoot ourselves in the head.

MR. : Thank you, Bob.

Bill Gray (sp), let me call on you as first and then we'll rotate.

BILL GRAY: First of all, let me just say I'm glad to be here and hear both Admiral Mullen's testimony as well as Secretary Gates'. I have one question which I hope you might be able to answer, and that is of approximately \$670 billion budget, what is the size of the first-year cut in defense that each of you think is appropriate, and what is the implication of a five-year basis of savings?

ADM. MULLEN: I think Secretary Gates has pointed out very clearly that there have been significant reductions thus far, but obviously the 490 billion (dollars) or so that are – that are resident in the '13 budget that the president sent to Congress and other reductions that he took under his stewardship while he was secretary.

It – I think if it executes as I recall, it will be upwards of 50 billion (dollars) a year or – in sequestration, if you will. And so that's notionally – and if you – and if you pull the costs of Afghanistan, of the wars overseas out, which I think people do and don't, at their convenience, depending on how they want to talk about this problem – but that's operation costs, which I think obviously we have to fund – then the – particularly in the year of execution, if you will, it just devastates the kind of accounts that both Secretary Gates and I were talking about in terms of training and maintenance and – I mean, and I think we far underestimate how quickly we could get there, despite not wanting to get to a hollow force. There are some instinctive things inside defense that would put us there as well, just how we do things inside, with how we execute, because everybody's fights – everybody fights for the money, if you will.

But it would principally be executed there. I think clearly, as quickly as the department could get to not issuing contracts – so we talked earlier about many programs which are over cost. And I understand that, and that is something that needs to be contained, although an awful lot of smart people have tried to figure this out in the last 10 to 20 years, and we haven't quite gotten there yet. But you would see, actually, (for ?) programs that you then agreed or desired to keep, those costs would automatically go up, because those contracts would get – would get spread out over future years. So in fact, when you're trying to save money, in fact, for the programs that you want, you could have a pretty serious impact very quickly on those kinds of things as well.

And then lastly, I talked earlier just about the cost of people. I think clearly – and with these kinds of cuts, you have to go where the money is, and certainly half the money is with our people. And I would just want to be careful. That doesn't mean we shouldn't take reductions, because I think there's certainly an opportunity to do that, but I think we need to be careful about our people and their families in which we have invested so much over the course of these two wars, so that on the right hand side of all of this, the force is very much intact, can still represent us globally, as we've been asked to, both in peace and in war, and also to be preventative in that regard and certainly prepared to – (audio break) – should the circumstances warrant as well.

MR. : What do you think – what do you think, Mr. Secretary? Is it an appropriate reduction given all of the things that you as well as Admiral Mullen have talked about, avoiding sequestration but doing what would be appropriate? Do you have an idea of what amount that would be in the first year and out years of five years? Because I agree with you. I think it would be a disaster to have sequestration occur in the Defense Department. (Audio break) – and I think, overall, as you said in your presentation, it really boils down to a lack of management and a willingness to make decisions, if we have sequestration across the board. Do you have any idea in your mind as what would be the maximum amount that you would reduce in the first year and then a five-year approximation?

MR. GATES: Well, one of my – one of my concerns in terms of talking to the Congress and to the president before I left office was the reality that we were already looking at a \$900 billion cut in defense over a 10-year period. That's already programmed in, \$900 billion. I haven't heard anything like that on the domestic side in terms of specific programs, specific plans. But to pluck a number out of the air, I told the president and the Congress, was math, not strategy. And I instituted, before I left, an approach that basically said, before you make any specific decisions on that next sized cut, that \$490 billion that the president asked for, let's look at the strategy – (audio break) – so that the president and the Congress can make choices about what they don't want to do in the future. Where do you want to cut the budget? That strategy was completed under Mike and Secretary Panetta in the fall, and I think – so that 490 billion (dollars) is based on a look at strategic things rather than just doing it as a math problem. So when you ask me how much I think the defense budget should be cut for the next fiscal year, my argument, first, would be, it's already been cut substantially, and the question is then, to the president and the Congress, what do you want to stop doing? It's not just a math problem.

MR. NUNN: (Off mic) – Gates.

Bill Brock, let me turn to you. We've got about 10 or 12 more minutes, so I think we've got time for everybody to ask a question. Bill?

MR. BROCK: I think I'd like to get back to the question of the Congress itself. You both have mentioned some of the issues. Every one of us has served in the Congress; every one of us can tell you countless numbers of members who we respect; their honor, their integrity, their patriotism, their willingness to work across party lines. There are people trying to do that today. I just would like to ask, this is such an obvious issue. What does a member say to you when you have this conversation with them about these choices? How could they possibly give you a rational excuse for what they've done?

(Laughter.)

MR. GATES: Most of the time, what I get – when I've got – when I was still in office – happily I've not had to testify since then, so my information's a little over a year old, but what they would say to me, for example, when I was trying to cut or cap the several dozen programs in 2009, everybody agrees on the importance of acquisition and procurement reform. Everybody agrees that we need to do these cuts in a rational way. Everybody agrees on the need for prioritization, but when it comes to specific votes on specific issues, they vote parochial interests. The F-22 had suppliers in 44 states. That's 88 senators. Now, in that instance, under a veto threat from the president, we were able to prevail in terms of capping that program, which every secretary of defense since Dick Cheney had cut. So the question is, how do you – how do you get the members of Congress to forgo parochial interests in terms of what's doing in the best – what's in the best interest of the country as a whole? And I ran into this, Mike and I ran into this on every single specific program that we wanted to do.

Everybody agrees Department of Defense health care costs are completely out of control. We will spend probably 60 billion dollars on Defense Department health care. Nobody wants to touch the health care that goes to our active force. But what Mike and I proposed, and what the president proposed, was a very small increase in the health care premium and fees for military health care insurance for people between the ages of 45 and 60, working-age people. And yet the Congress will not go along with that. It's absolutely necessary. There has not been an increase in those premiums in 15 years. Now people say, well, we had a deal and the government was always going to provide free medical care. That deal was off the table when the Congress voted to impose a fee in the mid-1990s in the first place, and nobody ever promised at that time that that insurance fee would never increase, and so we were talking about the difference between \$420 for a full family of four going up to something like \$520 a year, which is a sixth of what most federal employees pay. So even in an area like that, where everybody in principle agrees that something has to be done, the Congress will not go along with it. So figuring out how to get these people to rise above their parochial interests and frankly be willing to put their re-election at risk to do the right thing for the country, I think is what's critical.

MR. NUNN: Let me rotate to –

ADM. MULLEN: Chairman, could I just make a brief –

MR. NUNN: Sure.

ADM. MULLEN: My own experience in that regard, very similar. In fact, we testified – I testified five or six years for these modest increases in health care rates, if you will, and I think – actually, I think, unless I’m – I think we finally actually – Bob, after you left, I think we finally got it through, but it really is modest, and it’s the first time. It does speak to the power of the veterans’ service organizations, with respect to that, and the votes that are tied to that.

But my own experience was – this is four or five years ago – (inaudible, audio break) – actually was at a small dinner on the Hill with brand new congressmen from all over the country, and it was about a dozen, and they were – this was in the winter, so they were five, six months into their first term, or maybe not even that long, and I said, so what strikes you? And their response to me was the power of the gavel specifically. And from my perspective, it gets to how – (audio break) – the – that then translates to what, certainly that I’ve seen in terms of the power of the leaders.

Now, Bob Gates in his statement talked about the chairman, the positions of chairman before, and their willingness to – despite the partisanship of it, to broker deals. That was a requirement. That’s what they did, and the feedback I’ve gotten from members over a period of time goes right back to – including members who have been there a fair amount of time – (inaudible, audio break) – goes right back to that comment that that one congressman made to me five or six years ago, is the power of the gavel, period. And it is – the message I get from them, individually, is, we want to solve these problems. There’s not one that doesn’t speak to that, but collectively, and then you speak to the leadership piece of this, their – the ability to move from the desire to execution is what does not appear to be there based on the solutions that haven’t been generated so far.

MR. NUNN. OK, Tim Roemer and then John Tanner, we’ll give you the last question.

MR. ROEMER: Thank you Senator, and thanks again for the great representation up here on the panel. Bob Gates, Mike Mullen, thank you again for your superb service to our country. I’ve seen you work here domestically; I’ve been fortunate enough to see you work abroad and how efficient you are abroad. Thank you for your valuable time today.

I’d like to continue on the theme of the politics of this, and how do we try to get the politics right in order to solve this problem? Bob, you gave a very eloquent litany of reasons of why Congress doesn’t work very well. You talked about redistricting and the problems there, you talked about the decline of congressional power, you talked about wave elections, you talked about the media. One of the things that you didn’t mention, or I didn’t hear, was the amount of moneys in campaign today, and that oftentimes, the effect of fundraising is that members of Congress aren’t doing their committee work and getting rewards for doing good things up there. As Mike said, they want to do good things, they intend to do good things, but oftentimes there are forces pulling them away from those responsible positions. I’d like to ask you both, as really masters of, you know, how this system works, how do we put this compelling narrative together today, maybe it’s a combination of nation-building at home, and national security abroad. How do we get our members from both parties to show the kind of leadership for positive reasons to

make these decisions, which will result in fiscal responsibility at home so we can project this power abroad and take on the kind of threats that are coming at us, whether they be nuclear nonproliferation, whether they be Afghanistan, whether they be threats on our embassies? What's that narrative?

ADM. MULLEN: Bob, you want to go first?

MR. GATES: Well, I think that the – I mean, it's a tough question. And first of all, in terms of the impact of money, I mean there was an effort to try and get control of that. The Supreme Court overturned it, so I don't know what the solution to that piece of it is. I would hope – I mean, the history of democracies dealing with problems on the doorstep or on the horizon is not encouraging in this respect. Most democracies seemed to have to have a crisis before people rise above parochial or political interest to do what is the right thing for the country.

I think many of us would argue that the crisis is here, it's not on the doorstep, and it's certainly not on the horizon. It is here and it is here now. And I think, in some ways, it's too abstract, and so one of the things that I have found in dealing with members of Congress, but also in dealing with the public, that – that specifics in terms of consequences are more compelling than broad generalizations. So the reason that I referred to pilots not being able to fly as often, soldiers not having as many bullets – getting down to the specifics – for example, of what sequestration will mean in the daily lives of Americans, and in terms of what the federal government delivers, I think is one aspect that's important.

I think having bipartisan leadership is very important, as well. And with all due respect to the members of the panel, and frankly, Mike and myself as well, what's really important is having people who are in government today, on the Hill and in the executive branch, talking about these consequences – (audio break) – if they don't reach agreement, if this thing is not solved. It's all well and good for the rest of us to talk. And George Schultz and some others a very compelling article op-ed in "The Wall Street Journal" this morning on the crisis that we're facing. But it seems to me that it's those who are still in government, still have the responsibility, and, frankly, are the ones who will be taking the risk for taking bold stands that have to speak out on these issues.

MR. NUNN: Mike, we'll give you a shot at that question, and this is going to, I think, wind us up for this panel, because we're going to run out of satellite time.

Bob, we thank you very much for coming in.

I appreciate your leadership, continued.

Mike.

SEC. GATES: Absolutely.

ADM. MULLEN: And I'd actually just take a few seconds to say thanks to Bob.

I guess the way I would summarize it, and I think Bob has very eloquently hit the key points, but, you know, fundamental to me – and it's why I was in the military forever, because

the military had a way of putting me in leadership positions my whole life, and I loved that and thrived on it, and the challenges that were associated with that.

So getting – and I don't know how to do this. I just think getting to a point where the leaders will, you know, reach across the boundaries, if you will, recognizing the severity and the criticality of the crisis, because I think it's here as well, as Bob said, more than anything else. And to his point, it is all well and good for us to raise the issues, and I think that's very important, but we're not the only ones. And we don't have the direct responsibility now, and it's really for those that are in those positions to forge, somehow, the kind of solutions that make it better for America. And that, fundamentally is tied, I think, to leadership from everybody, every sector across the board. More than anything else, I think leadership really can solve this,

MR. NUNN: Thank you very much, Mike.

John, we're at the position where, I was told once I was a panelist on "Meet the Press" who had the little earpiece in, somebody said to her as she was about to ask the last question: You've got time for one more question and no more answers. So – (laughter) -- would you want to use 30 seconds here? I don't think we've got time for an answer, though, because we're about to run out of time.

MR. : Thank you very much, Mr. Chair. I was just going to say something that Senator Brock and I have been interested in for a long time, and others and Secretary Gates mentioned it, is one of the farthest of factors of the breakdown of the political mettle. And I view sequestration as a failure, or the result of failure of our collective national political will. And one of the questions that I think specifically we could address is a gerrymander, but we'll do that a later day because – (audio break) – I spoke on it last time I was here, and I guess I will do it the next time I'm here.

Thank you, sir.

MR. NUNN: OK, well we're running right on time. Mike Mullen, thank you so much. Bob Gates, thank you so much. (Applause.)

Next, we're going to talk about some of the solutions, and before we do that, we're going to have a little background with some charts and we're going to have Steve Bell, who is a director of the Economic Policy Project at the Bipartisan Policy Center, and Bob Bixby, executive director of the Concord Coalition, to sort of take the, take the podium at this stage, and then we'll go through a set of charts. Then we'll have Simpson and Bowles, theoretically are coming in on satellite at 2:15, and we will have Pete Dominici and Alice Rivlin, who are already here. So that's the plan.

And, Bob, thank you for your leadership. Bob and Steve have been instrumental in putting these forums together, and both have done a sterling job for years, and particularly in the last several years and months and working – both these panels, we're going to hear from today, that have tackled these issues in very specific ways.

So, Steve, I think you're going to lead us off and walk us through a few charts and then Bob, we will turn to you. And I'll ask the panel members if we need clarification on any chart as

to what it means, let's chime in and ask the question, because I think it's important for people to try to understand the message coming from these – this presentation.

Steve?

STEVE BELL: Mr. Chairman, thank you. I think the first question that occurs to everybody is this: Is this debt really that bad? Is it unsustainable? So the first chart is, is the debt unsustainable? Well, clearly it is, our – (inaudible) – our jet to – debt to GDP ratio, right now is higher than it's been any time since end of World War II. And that is when it was coming down, after that conflict.

Yes, sir, you do. Let's take a look at it. A hundred percent of GDP, we reached it during World War II. The projection by the Congressional Budget Office and GAO is that we will now reach 100 percent of debt, held by the public, sometime around 2020. Now, at that point, the debt is growing faster than the Gross Domestic Product of the United States.

Let's take a look at the next chart: Interests costs on the public debt. The most direct consequence of the growing debt is the cost of servicing that debt. How bad is it really? Right now, we spend about \$200 billion a year on

servicing that debt. How bad is it really? Right now we spend about \$200 billion a year on servicing the public debt. We have exceptionally low interest rates to do that. However, we will probably see – under normal interest rates that have prevailed, at least for the 10-year note, over the last 30 years – a rising debt burden that, at some point fairly soon, will crowd out all other spending from the federal budget, so that by 2022 interest on the public debt will be bigger than what we spend on all of our national defense put together.

MR. NUNN: So the chart you're showing us now assumes what on interest rates?

MR. BELL: We assume that we gradually get back to about 4.75 percent as the 10-year note.

MR. NUNN: And that occurs where? The 2016-17 time frame somewhere?

MR. BELL: Sir?

MR. NUNN: I mean assumption.

MR. BELL: Yes, sir. I used to work for Mr. Buffett, and Mr. Buffett told me the way to go bankrupt quickest is to guess on interest rates. I don't know when that'll happen. (Laughter.) But I – but somewhere about 2018 –

MR. NUNN: But when you – but when you show the 2022 \$900 billion in interest on debt and – per year, that is assuming we go back to normalized interest rates.

MR. BELL: Gradually that we do; not on a spike, which is a question for others.

Let's take a look at the next chart. This is about interest and entitlements. Let me explain what entitlements are because some people get confused. Social Security, Medicare, Medicaid, interest on the debt are things that people are entitled to receive, sometimes because of deals that we've made called issuance of sovereign debt, sometimes because of court decisions that say that even if we don't have the money, these people who are in the beneficiary class are allowed to get this money.

So if we take a look at Social Security and Medicare and these other so-called entitlements, notice that in about 15 years they consume all federal revenues. And what does that mean? That means transportation; scientific research, whether it's health or basic science; energy research; it means education. Those things, in fact, will all have to be paid for out of new debt.

Let's go to the next one.

MR. NUNN: Let me ask one question on this one before you go to that next chart.

MR. BELL: All right; go back.

MR. NUNN: OK, you're saying that that revenue line, the hundred percent revenue – is that assuming the revenue is going to stay at about historical average?

MR. BELL: Yes, sir, about 18 percent.

MR. NUNN: About 18 percent of –

MR. BELL: Yeah, between 18 (percent) and 19 percent. Yes.

MR. NUNN: So basically you're – this chart shows that Social Security, Medicaid and Medicare – if we keep an 18 percent – approximately 18 percent of gross national product as revenue – if we do that, then these three programs and interest will eat up the entire budget?

MR. BELL: Yes, sir, that's correct.

MR. NUNN: And the rest of it would have to be borrowed?

MR. BELL: The rest would be borrowed. So everything for defense, everything for education, everything for transportation, all of our research – all of that will come from borrowed money, the things we think of as investments for the future. This chart, more than anything, I think, shows us how something like a sequester is an example of eating our own seed corn.

MR. NUNN: OK.

MR. BELL: Let's go to the next one. So let's take a look at this chart and talk about what is discretionary spending. And I've talked about entitlements. One way to think about discretionary spending for budget wonks is this way. When the Congress passes every year their

individual appropriation bills – the spending bills – that is discretionary spending, by and large. The Congress has the discretion to pass those bills or not to pass those bills. They do not have the discretion to refuse to pay Social Security, Medicare or Medicaid.

So discretionary spending, which makes up a relatively small and slowly growing part of the federal budget, is going to take 100 percent of the hit if we go off the fiscal cliff and sequester occurs. So you can see that that just doesn't make sense – less than a third of the budget taking 100 percent of the hit, and that third growing more slowly than almost any other part of the budget.

MR. : I have a question.

MR. BELL: Yes, sir.

MR. : When Gramm-Rudman-Hollings was adopted and the first time sequester appeared in the – in the language of the federal government budgeting, did they contemplate and pursue entitlements as – in their sequester, or was it only these annual occurring expenditures?

MR. BELL: Mostly it were these annual recurring expenditures. We negotiated out 47 programs in the domestic area that were not subject to sequester. Most of those were a variety of entitlements and –

MR. : Those were negotiated. They did – they were not the actual result of the knife cut that –

MR. BELL: No, sir. That was a result of negotiation. And if you take a look at what's exempt now under the Budget Control Act of last August, more or less all of those exemptions remain in there. So this is very similar to the Gramm-Rudman-Hollings bill that was passed in 1985 and the first sequester that we had under President Reagan in 1986.

MR. : How much money was that? How much money was that?

MR. BELL: That was approximately \$30 billion in budget authority. We – without getting too much in the weeds, we did it backwards back then. We said, we have to save this much money in outlays, because we were talking about deficits. And then we kind of figured out how much in budget authority that would yield.

MR. : But even back then, the sequesters were not of the magnitude imposed upon defense and domestic spending now, 20 years after the adoption of that so-called successful way to cut the budget, according to Senator Gramm from Texas.

MR. BELL: That's correct. And I should add that one major sequester – only one occurred. And it very quickly became clear in two years – and we were going to have to cut 36 ½ percent out of defense in one year – that perhaps this was not a good thing to do.

MR. NUNN: OK, thank you, Steve.

Bob Bixby.

ROBERT L. BIXBY: Thank you, Senator. And thank you, Steve. And Steve has talked about the growth of the major entitlement programs – Social Security, Medicare and Medicaid – and identified that as a big problem, a cost-driver. I want to look at some of the factors why, because they have to do with the solutions that would be adopted and the timing and the magnitude.

So if we could see the first – the next slide, please – one of the factors driving the cost of those programs is simple demographics. That is to say, we're going to have many more beneficiaries because the population is aging. I feel that every day when I get out of bed, so there are a lot of us baby boomers who know what that's like. Part of that is – and obviously this is a good thing, that people are living longer. And of course the baby boom generation is a fact that we need to deal with; there's not anything that we can do about that factor. So demographics alone are going to add substantially to the cost of these programs.

And of course that also has economic effects. It means that there are going to be fewer workers paying into the programs, Social Security and Medicare, relative to the number of beneficiaries. It means that the elderly population is going to be growing much faster than the working-age population. And so those are things that are going to not only affect the budget but the economy.

Let's look at the next slide, please. The other big factor is rising health care costs. Certainly this affects Medicare and Medicaid. It affects the entire health care system. But in this country, we have not found the magic cure for how to slow the growth of health care costs. We tend to spend much more per capita than other developed nations – nearly twice as much than our closest competitors. So we have two factors at work here: health care costs per capita, health care spending per capita, growing faster than the economy and an aging population that is going to be drawing more and more on this health care system. Those two factors will have a profound impact on the federal budget, as we can see in the next slide.

And when we see the next slide, we're going to see – (chuckles) – a major impact. I want to explain – take a minute to explain this. What this is showing is that the cost of the three major entitlement programs – Social Security, Medicare and Medicaid – will expand over the next couple of decades from about 10 percent of the economy to around 16 percent of the economy. Now, in and of itself – and it shows that the health care programs, Medicare and Medicaid, are much more of a factor than Social Security, which is just affected by the demographics alone.

Growing by 6 percent of GDP might not sound like too much, and maybe this is not, in the way it's presented, the most dramatic chart one would ever see, but it is in fact quite a dramatic growth. If you're talking about gradually adding 6 percent of GDP to federal spending, consider a couple of points. Today, the entire Pentagon budget, the defense budget is around 4.3 percent of GDP.

So we're talking about adding an annual – (inaudible) – to federal spending that's more than the entire defense budget. If people were talking about gradually more than doubling the defense budget, that's what we'd be talking about. And keep in mind that this is all happening on autopilot because these are entitlement programs, as Steve mentioned, so they don't go through the annual appropriations process.

If you want to look at it on the tax side, I think the federal income tax – individual income taxes are now about 7.2 percent of GDP. So if you're adding about 6 percent that's – you know, you could – you could pay for that by raising income taxes across the board by about 80 percent.

So that's the magnitude of the federal budget challenge over the next couple of decades simply because of these factors, demographics and rising health care costs, that are running on autopilot. And that's really the nub of our problem – much more than waste, fraud and abuse or things that get so much more attention.

Could we see the next slide?

So what do we do about it? Well, one of the things you could do about is say, gee, maybe we should cut that waste, fraud and abuse. Let's get into the weeds on those discretionary programs and make them more efficient. How about eliminating them all together? Because that's basically what you would have to do in order to lay off the costs of these rising entitlement programs.

And what this is showing is just a simple illustration of if you took all the discretionary spending, including defense, and tried to pay for the rising costs of the entitlement programs by cutting all their spending you would get to implausibly low levels and eventually have to zero the whole thing out. There are some other ways you could deal with it. The next slide Steve will pick up on.

MR. BELL: Thank you, Bob. Fantasy number two, can we raise taxes enough to pay for the projective growth in entitlements? Well, you could do it, theoretically. By 2030, federal income taxes would have to go up by 65 percent. That sounds like a long way away, but it's within the lifetime of most of the people in this room – the working lifetime of most of the people in this room. That's a 65 percent increase.

If we decided we wanted to limit the tax increases to the top 5 percent income earners, their income taxes would have to double. And if we limited it to the top 1 percent, their taxes would go up by 169 percent. Our suspicion is that that would cause some political turmoil and that there would be somewhat less incentive for people to grow and that it would – or to work, and it would have a very substantial negative impact on economic growth for the country.

So when you hear people say we can raise taxes enough or we can cut spending enough, they probably need to go back to grade school and take arithmetic.

MR. BIXBY: And Steve and I will end our presentation with the next slide, which just shows what we are – what we need to confront. A realistic projection of budget deficits over the next 10 years is about \$10 trillion. That's a projection from the Congressional Budget Office and basically what that's assuming is let's say that we just fully kick the can down the road. Let's just say that we extend all current policies and tax cuts and we don't do the spending cuts that are programed under current law. You get about \$10 trillion worth of deficits over the next 10 years.

And so a calculation of an illustrative plan that would stabilize the debt-to-GDP ratio over the next 10 years would save roughly \$4 trillion. So our illustrative line there is not any particular plan, it's just one that would save about 10 – you know, \$4 trillion, in a way that would stabilize the debt-to-GDP ratio so the debt is no longer growing faster than the economy. But keep in mind where that happens – where it would stabilize the debt-to-GDP ratio at today's level, which is around 70 percent of GDP – a little bit more than that – very high above, almost double what it has been in the post-World War II period.

So for all of these changes that we're talking about – the \$4 trillion worth of savings and the plans that we'll hear about from our next panel – is really just the first step because it goes – it would still leave accumulated deficits over the next 10 years of about \$6 trillion even if you say \$4 trillion. And keep in mind that we're a long way from talking about anything like balancing the budget or, you know, reducing the debt-to-GDP ratio.

So a plan that has to deal with this really needs to be of sufficient magnitude, it needs to be phased in properly and it needs to be capable of producing long-term savings and not just for 10 years. And so fortunately, Senator Nunn, I'll toss it back to you and we have two good panels.

MR. NUNN: That's a perfect – that's a perfect segue. I'm told that our friends Alan Simpson and Erskine Bowles are more than theoretically but I'm informed that they're on the line now. A very brief introduction – I'm going to cut the introduction very short just because of the time. But as we've seen, it's going to take a very big and substantial deficit reduction plan to even begin to address our fiscal challenges.

We're very fortunate today to have the leaders of two groups that were able to meet this challenge in a bipartisan way. They are, of course, Alan Simpson and Erskine Bowles, who chaired the president's bipartisan Fiscal Commission, and my colleague here Pete Domenici and Alice Rivlin, who co-chaired the Bipartisan Policy Center's Debt Reduction Task Force. Both groups spent nearly a year debating the issues and working out consensus solutions. Each issued reports late in the year of 2010. Both plans dealt with the deficit challenge in a comprehensive way. They put everything on the table. Both of them required compromises between Democrats and Republicans, but they did it. And we'll hear more about that from them.

I'm – a lot of people are frustrated because they think these plans are no longer applicable. I don't agree with that, I think that they're very much alive and well. I think there are a lot of people on Capitol Hill who understand that we have to deal with this in a comprehensive way. I think there are lot of people that are now growing – there's a growing

support for some emerging plan that would be very much like the plans we're going to be discussing. And we have the Committee for a Responsible Federal Budget led by Maya MacGuineas that are helping organize for some of the events that will happen after the election.

So the plans are alive and well and so are our next guests, Alan Simpson and Erskine Bowles. So if we can find the technological genius to get them up on the line – and then you – Alan, you look just as good as ever, whatever that means.

ALAN SIMPSON: (Chuckles.) Well, I'm alive, whatever that means. Yeah.

MR. NUNN: Alan, we're delighted to hear from you today. So whatever little statement you'd make. I got a glowing introduction but just say that – suffice it to say that you and Erskine have not only done tremendous work for our nation but you're continuing to do so every day and we're indeed grateful to you.

Alan Simpson, senator from Wyoming and eminent American. Alan.

MR. DOMENICI: Before you proceed, might I say hello to him? Hello, Alan. I'm – it's only been – (inaudible) –

MR. SIMPSON: Well, yes, yes. How are you Peter?

MR. DOMENICI: Thank you. Nice to see you.

MR. SIMPSON: Pete and Sam and Erskine is out there in the vapor somewhere. Steve – oh – anyway, I usually let Erskine go first because – (inaudible) – him.

MR. NUNN: OK, we got to have some volume here, folks.

MR. SIMPSON: Can you hear it – can you hear me all right? There's a double sound coming back. You there? I don't hear anything. Gone. There's nothing there. Hello?

MR. NUNN: We hear you, Alan.

MR. SIMPSON: Oh, you do? You were cutting out. Now –

MR. NUNN: We can hear you.

MR. SIMPSON: You want me to go ahead?

MR. NUNN: Go ahead.

MR. SIMPSON: Yes, well anyway, it's been a remarkable long haul, because we met all those months, took us three months to establish trust – just to establish trust, a lot of backbiting, stabbing, terrible stuff. But we have five Democrats, five Republicans, one independent. Sixty percent of the group voted for it. And a range, a remarkable range, between Dick Durbin, I

would consider a very liberal and progressive person, and Tom Coburn, a remarkable conservative. And they concurred. We had Andy Stern, who did not vote for the final package, but certainly he and Tom Coburn put together a lot of our recommendations with regard to what to do with the defense budget.

The – there are so many things that are just goofy. We thought the easiest thing to do would be to fix up Social Security, not to balance the budget on the backs of poor old seniors or, you know, throw old ladies off of bridges in their wheelchairs and all that jazz. We did that for its own sake. And what is going to happen to it if you do nothing, which apparently is the recommendation of the AARP and other senior groups: Don't touch Social Security. Well, so we won't, and 21 years from now, 2033, you're going to waddle up to the window and get a check for 25 percent less. And you may not like that, and you say, wait a minute; I've got this little thing in the mail that says I get scheduled benefits, and I want those. Well, the law, ladies and gentlemen, says you will not get scheduled benefits; you'll get payable benefits. And this baby is running short every month, every year, right now. And you're going to get payable benefits, and you can whine into the vapors, and that's the way it is.

And then, of course, we said, we can't let this happen. So we'll do something with Social Security. We'll give the lowest 20 percent of poverty, give them 125 percent of poverty. That'll cost some bucks. Then we take people 80 to 85, the older old, and kick in an extra percent per year for them, 5 percent on the way up, do things with the cost of living index, do things with the progressivity in the code, do these things that have to be done, raise the wages subject to the tax to get it to about, you know, where it should be, 200,000 dollars, 190,000 bucks instead of 110,000 dollars) now.

And then we did a hideous things; it was just ghastly. To think that we suggested that the retirement age should go to 68 by the year 2050. Now, don't forget, it's going to go to '27, and it's going to go to 67 in the year 1927 – 2027. And the howls from the senior groups would like – be like the keening wail of a coyote. So there you are, stalled again. We asked the AARP, could you help? I mean, you got 38 million members paying 12 bucks dues, and you must have somewhere you're rat-holing the money. Maybe you could help us here. Well, we will. And they never did. Never did a lick.

They know what to do. If you look at their publications, there's a little thing appears in their columns along with the ads, of course, that says, "The things to do to strengthen Social Security." And guess what they are? Just what we've been saying. And they don't support any of them. I said to the heavyweights up there, I said, are there any patriots here, or just marketers? That is all they are. They're a marketing agency. And the poor old young people have nothing, except there's one group cooking now called The Can Kicks Back, and I hope that can is about a 55-gallon drum when it kicks back, because you can't win against these entrenched groups.

The mailings that come out from the AARP and the committee to – Social Security and Medicare. And don't forget, even in Ryan's plan, which they all go crazy about – and I'm not into politics, Lord's sake – but even in his, he said, we're not touching anybody over 55.

I had to testify a couple years ago with Mike Oxley, who was doing some great work, and a – and a bipartisan panel. And the people from the committee to protect Social Security and Medicare put on some 75-year-old flight attendant, looked like “The Wreck of the Hesperus,” and they said, this poor woman will fall over on her head any day now because of you cruel people. I said, she isn’t even affected. And I turned to the executive director; I said, you know this. It was Barbara Kennelly. I said, come on. She said, this is the way we do our business. Well, it ain’t the way I do my business.

So I go along, and you’re thinking – (inaudible) – thinking, you’re going to, but take a look at that defense budget business. Hollowing out America? You’re hollowing out your brain. I mean, \$750 billion or 740 (billion) – it shifts around – that’s ours. 740 (billion dollars), 750 billion (dollars), that’s our defense budget. And the defense budget of the other 15 top countries on earth, including Russia and China, combined is 540 (billion). Now, you know, have one on me.

And then we said to them, how many – how many contractors do you have in this Defense Department? They said, well it’s quite a range. It’s between a million and 10 million. Oh, we said, well, that is quite a range, no question. And then – and then I think my pal asked for a – one of the Dems on the committee asked for an audit. Got an audit? Kent Conrad asked that. No, we – you can’t – we’re an unaudit agency. (Audio break.)

We – you can’t believe – if I had stayed in the reserve another six or seven years, I would be a military retiree. Nothing wrong with that. They’ve given up a lot. Let’s all admit that. They gave up time, family, absence, the whole works. But for heaven’s sakes, there’s only 2.2 million of them. Many of them – the majority never were in a combat area or combat theater, and they have their own health care plans called TRICARE. And the premium is \$470 a year, and no copay, takes care of all dependents, costs you and me 53 billion (dollars) a year.

We got 61 Department of Defense schools in America a bus ride from a public school. Every one of them has a superintendent and the principals and the teachers. What’s that about? You have no need for those anymore. Got bases in Europe, 81 of them. Hell, there were 500 when I was there, but you don’t need 81.

I’m going to quit so that you can ask me questions. And I hope I’ll be able to hear them, because something is going on here, and I don’t want to go over my 10 minutes. But I could, though.

MR. NUNN: Thank you very much, Alan.

MR. SIMPSON: I could rant. (Applause.)

MR. NUNN: I think you had to take on a few special interests as you went through your procedure. (Laughter.) That sounds – (laughter) – Erskine Bowles –

MR. SIMPSON: (Inaudible) – to take away my life membership. (Laughter.)

Erskine has been a great partner with Alan. Have we got Erskine coming in? I hope so. Hope you can hear me. Erskine, did you hear Alan? Did you – Alan went through a very analytical and detailed presentation.

ERSKINE BOWLES: Yeah, I heard – I heard most of it. (Laughter.)

MR. NUNN: Erskine Bowles, we hear you. (Chuckles.)

MR. BOWLES: Thank you. I deeply appreciate what you're doing, Senator Nunn. I also want to thank John for being there, and Senator Domenici who, along with my – (chuckles) – really the godmother of all deficit reduction work, Alice Rivlin, for the great work they did on their panel. And I appreciate all of you being there today.

I'm glad I'm getting a chance to talk to you too, because I am really worried. I'm – I am afraid that if we can't get the members of Congress and the administration to put this ultrapartisanship aside and to finally pull together rather than pull apart, we face the most predictable economic crisis in history. Bob and Steve did a good job of discussing it, but there's no question if you look at just the plain math, the fiscal path that the nation is on is simply not sustainable today. And for me, you know, these deficits are like a cancer. And I say that because they are going to destroy our country from within if we don't do something about it and do it very quickly.

Let me give you my one piece of math, because I heard Steve and Bob talking about 20 years from now. But if you look at right now, if you look at the total income statement of the country and you look at every dollar of revenue that came into the country last year, every bit of it last year was spent on our mandatory spending and interest on the debt.

Mandatory spending, as you all well know, is principally the money we spend on the entitlement programs of Medicare, Medicaid and Social Security. And what that means is every single dollar we spent last year on these two wars, on national security, homeland security, education, infrastructure, research, every single dollar was borrowed, and half of it was borrowed from foreign countries. That is a formula for failure in anybody's book. And what I want people to do, and what Alan and I have been going around the country talking to people about is, you know, we've got to face up to what the real challenges are. The real challenges aren't waste, fraud and abuse and foreign aid and Nancy Pelosi's airplane, but, mean, the real problems are – there are really five of them, and I'll describe them really quickly because lots of people have talked about it, but I think if we focus on these five, we could get this deficit under control.

The first is health care. We do spend twice as much as any developed country in the world on health care, and that's true, senators, if you talk about it as a percent of GDP or on a per capita basis. And you know, that might be all right if our outcomes were twice as good as anybody else's, but if you look at almost any outcome measures, you know, while we spend twice as much, we rank somewhere between 25th and 50th in things like infant mortality and life expectancy and preventable death. And anybody who doesn't believe those 32 million people who don't have health care insurance don't get health care, they're just wrong. They get health care today, they just get it through the emergency room at something like five to seven times the

cost it'd be in a doctor's office. And that cost doesn't disappear, it gets cost shifted, and it gets shifted to the taxpayers in the form of higher insurance costs and higher taxes. You know, and you can see these results in the statistics that come out today. In 1981, we spent about 10 percent of the budget on health care. Today, we spend about 25 percent. By the end of this decade, we'll be spending a third, and it won't be long before all of the money we have will be spent on taking care of a couple of old coots like me and Al and buying a few tanks. So health care is literally the number one problem.

Number two is defense. You know, we spend more on national defense than the next 15 largest countries combined, and that includes both China and Russia. I personally think that we are bearing a disproportionate responsibility for global world peace, and I don't think America can afford to be the world's policeman. And I think Admiral Mullen, who you had testify, was right. You know, when asked what he thought the biggest national security problem was, he said it was these deficits, because they will consume every single dollar of resources that we have.

The third biggest problem we have, in my opinion, is our income tax code. You know, we have the – I think, the most inefficient, ineffective, globally anti-competitive income tax code that man could dream up. You know, we netted last year about \$1.3 trillion in taxable income, and that was because we had \$1.1 trillion of backdoor spending in the tax code. What we recommended was that we start off with a plan that wipes out all of this spending in the tax code and uses about 90 percent of the money to reduce income tax rates, and about 10 percent of the money to reduce the deficit. 10 percent of about \$1 trillion worth of spending would be about \$100 billion a year; \$100 billion over ten years would be \$1 trillion that we could apply to reducing the deficits. What would happen to income tax rates under our plan? We could take rates to 8 percent up to \$70,000, 14 percent up to 210,000 (dollars) and have a maximum income tax rate of 23 percent. We could take the corporate rate to 26 percent and therefore be globally competitive, and we could pay for a territorial system so that one and a half trillion dollars that today is captured overseas could be brought back to this country to create jobs over here. Now some of my Democrat friends complain about that, they say all that money will be used to be dividended out or to buy in stock, and I say, so what? That's good, because that money will now be circulating in this country. Rather than staying overseas and creating jobs over there, it will be creating jobs over here.

The fourth biggest problem that we face is one that Al's already dealt with, and, you know, we never talk about it in terms of deficit reduction, but we do need to make Social Security sustainably solvent. Over the next decade, Social Security will be \$900 billion cash deficit. Our plan makes it solvent.

Fifth biggest problem is one that I heard I think Steve or Bob talk about, and that is simply interest on the debt. We are spending \$250 billion a year on interest alone. To put that in some kind of relative quotient, that's more than we spend at the Department of Commerce, the Department of Education, Energy, Homeland Security, Interior, Justice and State combined, and if interest rates were at their median level they were in the 1990s or in first decade of this year, we'd be spending over \$650 billion a year on interest alone. And if we do nothing, we'll be spending over a trillion dollars on interest every year before you know it, and if you think about that, that's a trillion dollars we can't spend to educate our kids or to build infrastructure in this

country so we can move our services and goods to the marketplace, and it's a trillion dollars we can't spend to perform research in this country so the next new thing is created here, and making that doubly bad is that's a trillion dollars that will be spent principally in foreign countries where we're borrowing most of this money from to educate their kids to build their infrastructure and to do the high value-added research over there so the jobs of the future are there, not here.

I think that is crazy, and – look, this is not a problem that we can solely grow our way out of. It's not a problem that we can solely tax our way out of, and it's certainly not a problem we can solely cut our way out of without disrupting a very fragile economic recovery, without hurting the truly disadvantaged or without making cuts so deep in things like education, infrastructure and research that America is no longer competitive in what is today a knowledge-based global economy. That's why we recommended a plan that was hopefully balanced, reasonable, responsible, that was – that would reduce the deficit by \$4 trillion over the next decade. People ask us all the time, why four trillion (dollars)? You know, did we make that number up, is that – did we pick four trillion (dollars) because the number four bus passes on the street?

The answer is no. Four trillion dollars is not the maximum that we need to reduce the deficit over the next 10 years, it's not the ideal amount. Four trillion dollars is the minimum amount we need to reduce the deficit to stabilize the debt and get it on a downward path as a percent of GDP. We got a majority of Republicans, a majority of Democrats and a supermajority of our commission to vote for this. The breadth of support was truly amazing. Of the six sitting U.S. senators on our commission, five voted yes: all three Republicans, two out of the three Democrats. It was everybody from Dick Durbin, the liberal senator from Illinois voting yes, to Tom Coburn, the conservative senator from Oklahoma voting yes, and they did it because they thought it was the responsible thing to do, because they thought it was the right thing to do. I'm convinced that if we do this, the future of this country is very, very bright, and we can compete with anybody, with the best and brightest wherever they are. And if we don't, we're well on our ways to becoming a second-rate power. That can't happen, and that's why we continue to work on it so hard. Thank you for giving me a chance to testify.

MR. NUNN: Thank you very much, Erskine and Alan. (Applause.) I think your effort is alive and well, thanks to your leadership and continuing explanations all over the country.

We're going to hear from Pete Domenici and Alice Rivlin, and we hope, Erskine, you and Alan can stay with us, and then we're going to have some question and answers for all of you. Let me – Pete's been introduced – well-introduced, but let me give Alice a very brief introduction. Many people – everybody's who's followed the budget for the last 20 years knows Alice. She is a senior fellow in the Economic Studies program at Brookings and a visiting professor at the Public Policy Institute of Georgetown University. Before returning to Brookings, Miss Rivlin served as vice chair of the Federal Reserve Board, 1996 to 1999. She was director of the White House Office of Management and Budget in the first Clinton administration. In February of 2010, Alice Rivlin was named by President Obama to the Commission on Fiscal Responsibility and Reform. She also co-chaired, with former Senator Pete Domenici, the Bipartisan Policy Center's Task Force on Debt Reduction.

And Alice, did I say that you were also head of CBO at one time? But you've done so many things, and Alice is a well-known commentator in – on an awful lot of business programs. So we're delighted to have you. I don't know who's going to lead off, but we're delighted to have you and Pete. And we'll hear from you and then go to questions for all four of you.

MR. DOMENICI: Thank you very much. (Clears throat.) Thank you very much, Senator Nunn. Excuse me a moment. We have an agreement among ourselves that I will speak first. She will speak second and answer all the questions. (Laughter.)

You all don't know what a fortunate man I have been here in my – as I approach old age to be asked to join with Alice Rivlin in forming a task force to attempt to address the issue of the debt of the United States. It has been truly a pleasure working with her, and you will see in the next half hour why it's a – such a wonderful thing for me, because since we're partners, that assumes that I don't have to learn anything that she knows. (Laughter.) And she knows everything. Therefore I have reached a point where I don't have to know anything, except I have to be there and assist her and back her up and make sure that everybody understands we really did have a totally bipartisan group.

Let me make sure that you all know that this group was appointed by the – by the Bipartisan Policy Center, and it was a group of 19 and split as close as you could get, with one extra Democrat, that made up that assemblage. We worked on the proposition that I think is – as I listened to today's testimony and how tough it is to get things through, we worked on the opposition – on the proposition that we wouldn't vote on special – specific issues. We would go through the issues, and everybody would understand them, and then we'd package the whole thing and ask them whether they wanted to vote yes or no on all the work they had done as we went through each issue. And lo and behold, they all wanted to vote after they had done the work, but they didn't vote on each issue, and they voted rather handsomely. In fact, I believe, nobody entered a “no” vote, and we came out with a truly bipartisan budget.

So what we have put forth is already bipartisan because the participants were bipartisan. And – (inaudible) – I mean, the kind of people that you would – you would know you would respect, you would understand, everywhere from labor to industry, business, education and significant number of politicians who are out there in the real world, Democrat and Republican.

We found without question – and I want to go right to it and put up a chart that I want out; there it is. That chart that's in front of you shows that the problem has gotten even worse with reference to health care costs, the aging population and everything that's been spoken of today. If you just look at those lines, one, two, three, four, they all represent a huge expenditure of the federal government. But if you were to let all of them except the blue one proceed in a normal manner, the only one that would be out of control, which I call the blue line that is up, up and away, that's health care. You see it there?

And as you look at that and see – do charts mean anything? I can tell you. I can tell you certainly, Chairman Nunn and members and all of you are listening, it means that in order to solve the federal deficit, you must bend that line. You see that blue line? It cannot continue going that way, because it by itself makes the budget unattainable. You cannot live with it. So

you must turn it at some point and cause it to come from this kind of mode upwards to a balanced out approach, and that's exactly what we did.

And if you want to know whether that's doable, that is not an enormous cut in the programs that are health care. In fact, they grow enormously. It's just an approach that says, we know how, and we think it is feasible to change that line and cause it to come downward. And when it does, you don't have to change very much of the recipients' – very much of what they're getting, but you can't pay for as much as everybody wants. You have to have some kind – something holding it down.

So I believe one of the most significant evidences of the problem we have is that. And if any of you as members can make it into a small chart, you can carry it around as your blue chart, your chart which shows that without fixing health care costs of the federal government under the programs we have already agreed to give, you can't solve the budget problem.

Now, in addition to what we are talking about, it's obvious that we learned an awful lot that we want to share with you, but we don't want to take the whole afternoon. One of the principles was that we couldn't pretend that growth and just tax increases or spending cuts alone would move this – move us forward. So we concluded, and we tried each one on. And they wouldn't work. You couldn't possibly survive. We don't have the numbers for you, but you couldn't survive with the taxes necessary. You couldn't survive if you were going to take all the cuts out of discretionary, which, for those who know the budget, the ordinary debts of the federal government and obligations that occur each year, if you want to solve the budget on that, you just don't have any budget left. And you don't have any in the defense budget either if you want to just cut defense.

So we went through, and none of them would do it alone. We concluded that all of them combined could do their fair share and you might come up with something good. And lo and behold, that's correct. The discretionary bears its share, somewhat like Mr. Bowles told you about, that the defense comes down there. The discretionary, the rest of it comes down somewhere close. We were a little bit more generous on it than they were. And then we have Medicare, that we say we've got to save a certain amount.

And then we're leftover with one, big, monstrous thing. If ever I saw in 36 years of being a United States senator I saw a rare opportunity to do two or three things this country desperately needs with one shot, it is to reform the tax code of the country. We did that, and I guarantee you that if you put together a package that can be voted on in – as a package eventually in the – in legislature, be it the House and the Senate – the House and/or the Senate – if you can do that, where you put a package together and they can vote on one package, they will vote for reforming this tax code. And this Congress and any Congress will vote to change it dramatically in favor of growth and against the cumbersome, anti-growth policies of the tax code of the United States, no doubt about it. Any payment, any attempt to get at this debt says reform the tax code simultaneously. I say do the Medicare at the same time, and I say do it all at the same time and eventually find a method that can solve that problem of how do we do it.

And I will tell you today – let me find the exact part that I want to read to you, because I'm letting this out, because I have so much respect for you and for this assemblage that I want to – want to talk about it today. You heard what I was thinking. The opposite of what we were talking about in sequester and these details where the – (audio break) – to vote – (audio break) – on each item. Obviously, they have to vote on each item now. There's no way to avoid it. But we are going to be talking about developing a process that we're going to call an accelerated regular order. Now, Sam, in the Senate, we just yell – stand up and yell, regular order, when we want senators to behave. And when you want them to sit down, when they don't care to, we just say regular order, and everybody understands.

MR. NUNN: It never worked, but I know what it means. (Laughter.)

MR. DOMENICI: That's correct. They just move to the back of the room and talk louder in the Senate – (laughter) – when you say regular order. They're up front gabbing, and you say, regular order – you remember it, Bill – and they go backwards, and then they talk more in the back of the room louder.

But we're talking about an accelerated regular order process that would enable a lame-duck Congress, this next one, to put into law a structure that would allow the 113th Congress, if it chooses, to actually produce and pass a truly historic fiscal reform plan, including the – some of the Bowles-Simpson and some of ours, but the Bowle(s) plan, it would be like it. Our idea would allow full participation of members of Congress and all committees with a full floor consideration in both chambers. Our idea would give authorizing committees clear deficit reduction goals, and allow the full participation of the membership in arriving at these fast – these cuts, but they would be fast-tracked by operation of law. A law that would be passed in advance would make them fast tracked. That means there would be no filibuster, there would be time limits agreed upon in advance for how the business would be conducted, and all of it would be done with the idea that you get a chance to vote in your committees, but in the final analysis you will vote on a package to save the country.

Now I'm pretty convinced that we have smart enough people – you heard two of them up here, including Mr. Bell was one of them. You – (inaudible) – smart enough people to try to work this kind of thing out. And then you understand from Bowles and you'll understand from Dr. Rivlin, that the two plans do – even though they're two years late, and would have to be adjusted for certain things, they do provide an opportunity to solve this debt problem. It is not insolvable. Somebody wonders, why are all people like Pete Domenici involved when it ought to be the members of Congress? Well I would love to be the members of Congress. Let them have some forums like this. I'd be glad to do anything they desired in order to encourage them, one, that it is a big problem, big enough to ruin this; second, that it can be solved without wild things that have to occur, that they were talking about in Greece, as Greece was trying to lower its – lowers it – its debt. They can – there are reasonable things, I say to all of you and everybody listening, that should be done.

Now, with that background, I want to ask Dr. Rivlin – and let me one more time tell you how our understanding came to be. The Bipartisan Policy Committee asked me if I would like to co-chair, with a Democrat, a task force to solve this debt approach – (inaudible) – solve this problem. I said, well, not just any Democrat. I mean, I know a lot of them, they wouldn't want

to serve with me, so that's kind of mutual. (Laughter.) I said, if Alice Rivlin would it, I'd be glad to. I had no idea that somebody was asking that: Dr. Rivlin, would you like to do this on a bipartisan basis with a Republican? And she said, not any Republican, but if you can get Pete Domenici to do it, we'd – and look it there, we were far away, and we'd agreed that this should be the committee.

And so, from that time on, we have had innumerable meetings. I am pleased to tell you that the plans are pretty close together. I will say that I think that I like our tax reform better, although I like their rates better, but we can't get them down that low. And the rest of it, I like our approach to health care and health delivery increases, and I like ours better, because we do insist that the entitlement, per se, get reduced, get changed, get modified, and we have a system to do it that is tried and old and not brand new. And so, with that, if you would let her explain some of the details, I think you will understand where we've been working for the last two years.

MR. NUNN: Thank you very much, Pete.

And Dr. Alice Rivlin, we'll hear from you.

ALICE RIVLIN: Thank you, Mr. Chairman, and thank you, Pete.

I'm honored to be the clean-up batter in this extraordinary lineup of experienced and dedicated players who care deeply about the future of the country. I don't think the problem facing us is mysterious, or hard to understand. It's crystal clear. America faces two big challenges: We must grow the economy faster, and spread the benefits of that growth more widely, and we must put our federal budget on a sustainable track, so that the debt is no longer rising faster than the economy can grow. That's not very sophisticated. It is really obvious and – when you think about it. And getting this debt under control requires a bipartisan compromise on a grand bargain, as they say, to control the future of the debt.

Now, these two challenges must be addressed simultaneously. We can't grow the economy without fiscal sustainability, and we can't have fiscal stability without growth. So we have to do these two things together. Failure to address the looming debt weakens the confidence in both consumers and savers, and inhibits faster recovery, and job growth. But sharp, immediate cuts – as everyone has said in this lineup, sharp immediate cuts in spending, and increases in taxes, that is, going over the fiscal cliff, risks derailing the recovery now. In this fragile economy raising taxes for everyone – and remember, that's part of what happens at the end of this calendar year if we do nothing – and making big, senseless cuts in both domestic and defense programs, would be really stupid policy. And it would show that our democracy is too broken to function.

This fiscal cliff wasn't supposed to happen. It was supposed to be so scary that elected leaders wouldn't do something more sensible. So now we've got to do something more sensible. Our military colleagues have emphasized that the projected growth of federal debt is an enormous threat to future American prosperity, and hence to our national security and our world leadership capacity. If we don't take immediate action to stabilize the future growth of debt, we're going to be in real trouble. If we continue down this dangerous path, we'll be using a growing part of our tax revenue, as the charts earlier show, just to service the debt. We'll be vulnerable to the demands of our foreign creditors; we will risk rapidly rising interest rates, more

rapidly than we're shown in the charts, actually, that could lead to a deep and prolonged recession.

And we could possibly experience a sovereign debt crisis, like we're witnessing in Europe. We used to say with great confidence, we're not Greece. Well, we're not Portugal, we're not Ireland, we're not Italy, we're not Spain, we're not France – wait a minute, this is getting to be a very long list of countries that are facing a sovereign debt crisis, and we could be there, but we don't have to be.

The Simpson-Bowles commission and Domenici-Rivlin task force and – (inaudible) – I got to serve on both of them, proved that Republicans and Democrats can engage in serious and civil dialogue about how to get the debt under control. Even people currently serving in government – and most of the Simpson-Bowles Commission were – they can work along party lines to produce policies that will gradually and sensibly slow the growth of debt, and begin to reduce it. Moreover, as Pete has pointed out, the Simpson-Bowles and Domenici-Rivlin plans are very similar. And that's not because we colluded. It's because the arithmetic drives any bipartisan group using realistic projections to the same conclusion, bringing the debt under control without derailing the economy must involve a combination of three elements: entitlement reform, reducing the rate of growth of Medicare and Medicaid by delivering health care more efficiently and effectively, and putting Social Security on a firm foundation for future retirees. That part, the entitlement reform, is the hard part for Democrats, but it's absolutely necessary. We can't solve this problem without it, although it – entitlement reform won't help very much in the near term.

Second part is tax reform that raises additional revenues from a tax code that is simpler and less of a drag on economic growth, and remains at least as progressive as the one we have now. That's the part – the more revenue, that's the part that's hard for Republicans, but it's absolutely necessary. We can't solve this problem without it.

And thirdly, we do need reductions in the growth of defense, and domestic appropriations designed to improve the efficiency and effectiveness of both sets of programs. This is hard for everybody, but actually, the good news is, it's already happening. The Budget Control Act of 2011 already reduced discretionary spending by about a trillion dollars over 10 years, or about the same amount that both the Simpson-Bowles Commission and the Domenici-Rivlin task force recommended. We've done it. We can find ways of running both parts of the government more effectively, but we do need to defend the country and provide basic public services. And I think it's important to understand that the cuts involved in the sequester are over and above that trillion dollars that we have already done.

So let me say just a few words about Medicare and tax reform because they're the two most controversial keys to fiscal responsibility going forward. Pete has emphasized the importance of health care to stabilizing the federal debt, but reducing the growth of health care spending is not just essential for the federal budget. It's crucial for private-sector growth and state and local fiscal sustainability as well as for the federal government. The growth of federal health spending must be slowed in ways that lead to more effective, less costly health care delivery for everyone, not a shift from the federal government to the private sector. But we've got lots of room to do that.

Right now the – if you listen to the political campaigns, they're all on scare tactics. Each side is trying to say the other side is going to get rid of Medicare. Nobody's going to get rid of Medicare. Can you imagine that? It's ridiculous. (Chuckles.) Seniors are a growing and very powerful set of political forces. But we do have to make it more effective.

And although health care has become a hot-button issue in the campaign, the parties are not nearly as far apart as their political rhetoric implies. Both political parties recognize the importance of using Medicare to lead the way to a more cost-effective health system for everyone. And both recognize that the current Medicare reimbursements on a fee-for-service basis provide incentives to emphasize quantity over quality of care. And if you're in Medicare, you know that already. Both recognize that over time Medicare and health spending generally cannot grow much faster than the economy itself is growing. Indeed, the growth rate for Medicare enshrined in the Affordable Care Act and in the Republican budget proposals is the same; they just get there by different paths.

And just as there's no simple one-dimensional solution for the debt problem, there's no single approach to bringing health care costs under control. The Affordable Care Act emphasizes demonstrations and innovations aimed at discovering more cost-effective ways of delivering care and incentives for providers to deliver results. It focuses on reducing the growth of spending by putting those innovations into practice in our largest health program, namely Medicare. Republicans tend to emphasize competition among health plans as an avenue for adopting these same cost-effective innovations and improving results with slowing costs.

And Pete and I said, why not both? And with our colleagues on the task force, we crafted a proposal which we believe is an effective compromise. Our proposal for Medicare reform relies both on preserving and improving the efficiency of traditional Medicare and enhancing competition from private health – among private health plans on well-regulated Medicare exchanges.

And finally, tax reform offers a major potential for bipartisan compromise. Everybody's agreed the current tax code is riddled with special provisions that inhibit growth and narrow the tax base. It's possible to raise revenue substantially by broadening the base and lowering the rates and having a tax code that is more progressive than the current one. But this means reducing and eliminating deductions and exclusions and other special provisions that benefit middle-class taxpayers as well as more affluent ones. But that's doable. And both commissions actually did it. And we came to the same conclusion: that the best way, and perhaps the only politically feasible way, to reform the tax code is blow it up and start over with a simpler, fairer system.

Now, you need to be honest and specific about what a new tax code would look like and who are the winners and the losers. But when you do, it actually looks pretty attractive. For example, you would have lower rates. You would have a simpler code. You would have – you would retain some of the most necessary provisions, but you'd change them. For example, a home mortgage credit would replace a deduction. And that would help many more middle-income taxpayers but not give such big subsidies to high-income people who buy big homes. And we've just done too much of that.

Now, none of this would be easy. Compromise means no plan is exactly what any of the other – any one of the players wanted. But only compromise will avoid gridlock. And we cannot afford gridlock or no action. Gridlock means going over the fiscal cliff and risking another recession. It means not addressing the challenge of mounting future debt until events overtake us and we lose control of our economic destiny. We need to act now to preserve a more prosperous future and to show that our democracy actually works. Thank you. (Applause.)

MR. NUNN: Thank you very much, Alice. Thank you, Pete. Thank you, Alan. Thank you, Erskine. And we're going to have a few questions. We've got, my clock says, exactly 21 minutes – so enough time, I think, for everybody to ask a question and get some more information on the table. I'm going to start with John, who didn't – John Tanner, who did not get to ask a question. And then I'll rotate, Bill, to you.

JOHN TANNER: Thank you very much, Mr. Chairman. And thank all four of you for your excellent work. It's been constructive to the process in an imaginable (sic; unimaginable) way, in my judgment.

I think we've had a structural deficit situation for at least six, maybe seven or eight, years. And one of the frustrations that I have had is trying to explain the difference between a cyclical deficit and a structural deficit to people, number one; and number two, trying to instill in the general public the sense of urgency that I think this matter and situation requires. Do any of you all have any suggestions about how we can, one, explain to the American people that we can't raise taxes enough and we can't cut enough to get out of this if we only do one or the other, number one, on the structural part? And number two, how do we engage the general public to instill what I think is a lack of a sense of urgency about the – what I consider the dire consequences our country's in at the moment?

Thank you very much, Mr. Chairman.

MR. NUNN: Let me go to either Alan or Erskine, whoever would like to take a crack at that. And then we'll come back to Pete and Alice.

MR. SIMPSON: Erskine is the numbers guy; I do the color. But I can tell you what I tell people. I just say, pull up a chair; we don't do B.S. or mush; let's just tell you where your country is – and tell them what a trillion is. If you spent a buck a second right now, you wouldn't hit a trillion for 32,500 years. If you spent a million (dollars) a day since the birth of Christ, you wouldn't be at a trillion. And the big bang theory of the universe happened 13,600,000,000 years ago; now, that would – (inaudible) – even close to a trillion, and we owe 16 of those babies. And for every buck we spend, we borrow 41 cents of it. And today your country borrowed 3,600,000,000 bucks, and they'll borrow 3,600,000,000 bucks. So showing them the massive stupidity, and see how far we get with this.

MR. NUNN: Sounds like Alan's a numbers man to me. (Laughter.) (Inaudible) –

MR. SIMPSON: Well – (chuckles) – no, no. Erskine, tell us the cyclical versus – the cyclical versus the structural. That’s for Erskine. That’s Erskine’s baby. He’s good at it.

MR. BOWLES: You know, the real problem is that we can’t simply grow our way out of this problem we’re in today. You could literally have double-digit growth for a decade and not solve the problem. And you can’t simply tax your way out of the problem because raising taxes doesn’t do a darn thing to change the fact that health care is growing at a faster rate than GDP or the fact that the demographics of the country are changing quite rapidly.

And we can’t simply cut our way out of it. And the biggest problem with trying to do it all with just cuts alone is you end up having to make cuts so deeply to the income support programs that help the truly disadvantaged – things like SSI, food stamps, workers comp – and you also have to cut those things that we depend on so greatly for the future growth of the country, whether it’s investments in education, infrastructure or high-value-added research.

John, but none of that means that you can’t make cuts in areas that people like me really want to see us make future investments in. Let’s take something like education, that is – you know I was president of the University of North Carolina for the last five years. One of the things I wanted to do above all else was to do our part to improve K through 12 education. And I thought we were not only part of the problem but we were also part of the solution.

After all, we produce most of the teachers. So I turned to our staff and said: Gosh, how can we improve the quality of teachers that we’re producing? Surely there’s some federal programs out there that we can use to do that. They went and took a look and yes there are. There are 82 programs to improve the quality of teacher education. Now, do we need two or three good ones? You bet. But we don’t need 82.

Another example is we do \$1.5 billion worth of annual federal scientific research at the university. Is all of that high-value-added research? No. Nor is it at the other 3,000 colleges and universities that do federal scientific research. What we have to do is use the money we have more wisely. And if we do that we can get more bang for our buck and I’m confident we can compete with anyone. But you can’t take in a total of 2.3 trillion (dollars) and spend 3.6 trillion (dollars) and think you can do that indefinitely. It just won’t work.

MR. NUNN: Thank you, Alan – Erskine. Alice, you want to take crack at that – or Pete – the structure on cyclical – Alice?

MS. RIVLIN: I actually think that average people get this better than the politicians do. And there’s some evidence on this supported by many organizations like The Concord Coalition and others. When you get a group of average people in the – in a room and say, here’s the problem. Here are some numbers from a respected source, and this is what is going to happen if we don’t do anything. This is how much our debt is going to grow and here are the possible solutions.

And what do they do? They come up with a solution that looks a lot of Simpson-Bowles or Domenici-Rivlin. They say, let’s do some of this and some of that and some of the other

thing. And then you get to the question of how fast do we do it. People are perfectly able to understand that you can't have a big tax increase or a big spending cut when the economy is weak. So they say, let's do it gradually and let's do it in the future. And you have to do that if we're reforming the retirement programs anyway.

So it isn't that complicated, it's just that the politicians are in – are stuck in this groove of it's either one way or the other. Average people aren't.

MR. NUNN: Thank you, Alice.

MR. DOMENICI: I think that in my getting around and during the last two years when I was – when I took this assignment that Alice is right. I think you just use very conventional and typical language. You know, and it – people understand the word broke. We're broke. It's a terrible thing to say – or we're almost bankrupt. Or, would you ever believe it, but your country is bordering on bankruptcy and then you tell them why. So I don't think once we have the leadership at the top that's decided that we are going to take this on as a nation, I believe we can make the people understand.

To be truthful, I think the more difficult thing is that the rules and procedures that Congress has at its disposal can make things so difficult that you can't get them done – get anything done even if the majority wants them done and even if they're most sensible. If you get five stubborn people in the U.S. House under an open rule, they can stop anything. And in our body, the one we were in, you don't even need that many.

You need two or three with one of them either knowing the rules or having one sitting at his side, you can – you can keep anything – or you can make them vote on each item such that they're embarrassed to vote for it at the end because they don't want to be of record. So that's what – we got to find a way to get around that to help them, otherwise they got to lead themselves and I'm afraid it's not going –

MR. NUNN: And that's what you were talking about a few minutes ago when you mentioned the procedural fast track.

MR. DOMENICI: That's exactly correct.

MR. NUNN: I agree with you completely on that. It's got to be done. Bill Gray, we've got 12 ½ more minutes. So, Erskine and Alan, we're going to let you go at 3:30.

MR. GRAY: First of all, let me just say how delighted I am to hear both presentations, and I wish I could find a way to go over the House and Senate and pass them this afternoon because they are exactly what we've got to do. We've got to do something on the revenue side and we've got to do something strong on the spending side – not only discretionary but also entitlements.

The one I'm fascinated with is the fact that both of you have included tax reform. And I think that's a powerful engine, particularly when the tax reform is going to lower the rates, not

only for individuals but for corporations as well, and be very pro-growth. And I think Alice is right and Pete is right, if you roll it together instead of breaking it apart on individual votes you might have a chance to pass it.

I'd like to ask my friend Senator Simpson, who looks great in retirement – I haven't seen him in a long time – and also Erskine, on the tax reform that you all have, which lowers the rates, which I think is great – same as Alice and Pete – do you have any deductions at all and if so, what are they?

MR. SIMPSON: Bill, first of all, a delight to hear you. We used to work together. And Alice Rivlin, what a joy. She's the one who first mentioned a whisper about doing something with the solvency of Social Security when she was first on board. And they said, oh, Alice, you don't mean that. Surely there's something silly coming. Let me tell you, that lady – Margaret Thatcher, the iron lady, you name it – but she's a beautiful grandmother too.

But let me tell you, you – we did – what we said – one – at one point we said, let's get rid of all of them. And, Bill, you know what they are. I mean, there's stuff in there for – well, may I mention oil and gas? That's bloodstream to me. You got realtors, you got insurance people, you got Blue Cross, you got parking for employees, you got earned income tax rate, you got kids always – I mean, come on.

But we said, OK, let's get to where everybody wants to go – lower the rates, broaden the base and get spending out of the cold. And Erskine and I said get rid of all 180 of those babies and go look at them. I mean, you will barf when you get into some of it. And it's all put in there by big time guys and probably only 15 percent of the American people use it. On 25 or 27 percent of the people of American itemize. They've never heard of that joyous collection of stuff.

So we said, get rid of it and then give what Erskine has described – get 8 percent, zero to 70, he described it beautifully and he didn't leave anything out. And they said, well, how about municipal bond interests? What will happen to the cities? And I said, I don't know, it's already happened to them. Home mortgage interest at a million bucks? Who does that help? Give them a 12 ½ percent nonrefundable tax credit and help the little guy.

But the saddest part of this whole scenario is that the markets will call the shots eventually – they don't care about Republicans or Democrats or presidents. They care about their money. And they're going to ask for more money for their money, and when they do inflation will kick in and interest rates will go up. And the guy that gets hurt the worst is the little guy. What hypocrisy. What mush.

MR. NUNN: Erskine.

MR. BOWLES: In our original plan we put forth one option which got rid of all the deductions and all of the credits, just to show people exactly how low you could get rates if you got rid of all of them and the fact that none of them are free because if – when you start to add back one of these deductions or credits, somebody's got to pay for it. That's how we got rates to

8 percent, up to 70,000 (dollars), 14 percent up to 210,000 (dollars) and a maximum rate of 23 percent for individuals and 26 percent of corporations and a territorial system.

We did show an alternative. We said, look, some people want to keep the earned income tax credit, some people want to keep the child tax credit, somebody want to – some people want to keep the employee exemption for employer health care. Some people want to keep the mortgage interest deduction, some people want to keep the charitable deduction. Let's say we add those back as credits. If you add those back, somebody does have to pay for them, and when we did that, you could take rates to 12 percent up to \$70,000, 22 percent up 210,000 (dollars) and have a maximum rate of 28 percent. So that kind of shows you, you know, the fact that none of these are free, and if you add any of them back, somebody has to pay for them.

MR. NUNN: Thank you. Alice and Pete?

MS. RIVLIN: Well, Erskine got to their, I think, preferred plan, which was very similar to ours. But to answer your question, Chairman Gray, we did preserve an earned income credit, a child credit, a mortgage interest credit at our lower rate. We only had two rates, 15 and 28. And we did the same thing with charitable, and basically, we removed other things, but that was what got us to the solution.

MR. GRAY: Just for the benefit of those, I must express my biases. I'm a Baptist preacher, that last one was the one I wanted to hear.

MR. NUNN: OK, I'm going to – we got six and a half minutes left. Bill, why don't you and Tim both ask your question and then we'll shop it out there and do it – however's much time for answers as we can, but let's get them both on the table here since we're going to run out of time in a minute.

MR. BROCK: Alan, I won't even submit my parking ticket for a deduction. Just put it in a bank, I'm sorry. (Laughter.) I don't think there's a single that thing you all have proposed that can pass the Congress one by one. I really don't believe there's a single proposal from either group that can pass the Congress today on a standalone basis, and I am just captured by the idea that we simply have to present this as a package, the whole caboodle. We went through it with a group of 12, some of us were working with him, a group of six – everybody was trying to go big, and we collapsed because of some individual stuff, Pete. How do we get what you call accelerated regular order? How does it apply? Tim? Answer. How does it apply in the House? Because if we don't get this as a package, I don't think we'll get it.

MR. DOMENICI: Well, all I can say from my standpoint is that it is being worked on now by the best people around, bipartisan. It's being shopped to people with – that are real kind of people on the House and that Senate side, that would be interested, and I know there's enough chatter about it that I said, this is as good occasion as any to say it's being worked on and to explain a little bit of how it is. I don't know all of the details other than it is being worked on so that it will work. Some of those who are working on it happen to be old like I am and were part of the one time we used a word called "reconciliation" that's found in the innards of this called a budget act. It's just sitting around there, called "reconciliation." Never been used, never been

defined. So we used it and we defined it, and one thing it does, is it – be honest, it eliminates from the United States Senate the right to use filibuster on a bill that has it because the bill is a budget bill, and Senator Robert Byrd, the only thing he ever agreed to that he was sorry he did was the budget act, because he found that he had to agree that reconciliation made the affirmative bills not subject to filibuster and subject to limited amendments with limited time. Now you don't have those problems in the House, you do it by rule, but in the Senate, they are the beginning and the end of one package. Is that not right, Sam?

MR. NUNN: Right.

MR. DOMENICI: You can't have – (inaudible) – forever, and you have to have limited time and you can't have filibuster. So if you can do that and get these arranged where they fit within that nomenclature and that definition, then the question is, does leadership want to fix the country bad enough that they'll help get it started? And that will be forthcoming in the X now amount of time. I don't know when, but I thought it would be a good time here while we had a wonderful forum to tell you about it. I stand on the proposition that the majority of the leaders – majority of the House members, Democrat and Republican, the majority of senators, Democrat and Republican, are just as frightened as we are about the country going bankrupt and losing the big sovereign dollar and everything, and that could happen. Nobody that knows about our problems could say the only thing we're going to get is a recession out of this. It could fall apart with the kind of debt we've got and the kind of holdings and the people that own that debt.

MR. NUNN: OK. We've got two minutes and 37 seconds. Tim Roemer's going to ask the final question.

MR. ROEMER: Thanks Sam, that's plenty of time. Us House members, we don't filibuster anyway, so we don't – (laughter) – we don't go on talking too much about these issues. We've heard from Erskine and Alan about all the problems in this deficit and debt. It makes you sick to your stomach, but the good news – I'm an optimist, I like to look at this glass is half full – we've heard a lot of good news today, too. In fact, Erskine and Alan, I know you're traveling across the country. It is wonderful to have you go across east to west, north to south and talk to people about this problem and get attention to it and get people supporting efforts to balance the budget. I know you're going to Wake Forest University where my son Matthew goes. I hope you fire up those young people and get that next generation interested in this problem and solving this problem, and I guess I just end on this positive note and ask for your comments on it.

One of you said earlier that five of the six United States senators, including a liberal democrat, progressive democrat, Dick Durbin from Illinois, as well as somebody I serve with in the House, Tom Coburn, all voted for this proposal. Five of six. So if we can get people running for election to pledge to work on the deficit, sign a petition that they're going to come to Washington and work together, and we can get Alan and Erskine going all across the country building support for it, hopefully there will be some impetus and some momentum to do something about this. What are you hearing out there Alan and Erskine, and is there going to be a groundswell for this in the election?

MR. NUNN: Alan, you and Erskine have the final word here. This will wrap us up.

MR. SIMPSON: OK, I'll just take a minute. You've got to clean out the real underbrush of Grover Norquist. I mean, this guy got these people to sign up, some in the '80s, when inflation was, you know, whatever, and unemployment was three or four percent and everything is out of kilter now from where it was. And this guy, wandering the Earth in his white robes – (laughter) – getting this commitment of people – how would you ever go to Congress and sign something before you got there, you hadn't even heard the debate, and ten years later, 15, they've got you ready to hang. And I – you got to take this guy on because if you can't – if you can't get Grover Norquist and shoot him over the moon and you can't do something with the AARP – and these congresspeople are enthralled to the AARP and Grover, we ain't got a prayer.

Now that's where I – I've been saying that for months and it's still there. Gutsy, tough guy this guy. He's not it for anything but – I think it's almost like domestic terrorism. (Laughter.) He is – he is – he is probing the Congress and threatening them and so on. What can he do to you? He can't murder you. He can't burn your house down. The only thing he can do to you is defeat you for re-election. If that means more to you than your country when it needs patriots, hell, you shouldn't even be in Congress. (Applause.)

MR. NUNN: OK. Alice, last word. I think Erskine has just dropped off. Alan, thank you very much. Erskine, thank you very much.

MR. ROEMER: Grover's met his match, Alan. (Laughter.)

MR. SIMPSON: That's right.

MR. NUNN: Pete, thank you very much. Alice, last word.

MS. RIVLIN: I think the key really is the public demanding not just that the politicians face up to these choices, but that they do it together. The key really is bipartisanship and compromise. And not anybody is going to get exactly what they want, but it's much better to solve the problem than to get exactly what you want.

MR. NUNN: Thank you all for being here. We appreciate it. Thank you. (Applause.) Just for the information of the audience, we'll have the third forum in New York City on September 27th. It'll be on taxes and growth. We'll come back here on October the 1st; it'll be on health care and entitlements. So –

(END)