

The Economic Club of New York

413th Meeting
104th Year
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**Erskine Bowles, Co-Chairman
National Committee on Fiscal
Responsibility and Reform
and
Retired Senator Alan Simpson, Co-Chairman
National Committee on Fiscal
Responsibility and Reform**

Questioners: Glenn Hubbard - Former Chairman of
The Economic Club of New York
and
Senator John Kerrey - Nebraska Senator

Introductory Comments

Andrew Tisch

Good afternoon everyone. Welcome to the 413th meeting of the Economic Club of New York in our 104th year. The Economic Club is the nation's leading nonpartisan forum and today, bipartisan forum, for the discussion of economic policy. We have had more than 1,000 guest speakers who have appeared before the club in the last century, and we have established a strong tradition of excellence and timeliness.

First I would like to recognize the 141 members of the Centennial Society. These club members have made personal contributions in order to assure the financial stability of the club into its second century. The names are in your program and on our website. And as in the past, we welcome any new members who want to join the Centennial Society.

We would also like to welcome students from Adelphi University, from Columbia University School of Business and International and Public Affairs, from Fordham University and New York University. The club and its trustees are committed to economics education for our future leaders. And as such, are sponsoring students at today and at future events.

We are honored today to welcome retired Senator Alan Simpson and Erskine Bowles, the Co-

Chairmen of the National Committee on Fiscal Responsibility and Reform. The Deficit Commission. They were appointed by President Obama and announced their recommendations in December. Significantly, they and the Commission will be meeting with Congress later on this week. So gentlemen, we are hoping to have a preview of that meeting.

Erskine Bowles was president of the University of North Carolina until December of 2010. He served as Chief of Staff to Bill Clinton, and he was the Director of the Small Business Administration. He began his business career at Morgan Stanley and now serves on that companies board. He graduated from the University of North Carolina at Chapel Hill and from Columbia University Graduate School of Business.

Alan Simpson was elected to the United States Senate in 1978 and served as a Senator from Wyoming until 1997. He was Assistant Republican Leader for ten years. Following his term he was a visiting lecturer and Director of the Institute of Politics at Harvard University, John F. Kennedy School of Government. He is a partner in the Cody Wyoming law firm of Simpson, Kepler and Edwards, and graduated from the University of Wyoming.

After the Senator and Mr. Bowles speak, they will be questioned by two designated club members and if you have any questions, you can email them to our President Jan Hopkins at questions@econclubny.org. Senator Simpson, do you want to start. The floor is yours,

welcome.

Senator Alan Simpson

Well thank you very much. It is a great pleasure and honor to be here. They have given us a very truncated schedule and said, just knock it off in three minutes and then go to these questions. So it is an honor and a privilege for Erskine and for me to be here to join with a very vital group of American citizens, and I can assure you, you are, to share with you the work of the National Commission.

Erskine and I have met furtively with various groups around the country and we both leave the witness protection program from time to time to make sporadic appearances wherever we might be unknown. So it is this day, but there is one thing I have to say, they told me it would be a cold day if I ever came back here and got on a program with Bob Kerrey and look at it. It is a cold day. And that is because of Kerrey. Well enough of that.

Let me just say that I got into this game, he is out there somewhere, he will always get rebuttal. Let me just tell you quickly. I was called a year ago January, by Joe Biden. He said, Al, I got a real deal for you. You are just going to love it. And I said, what is it Joe, let me bring Ann here and she can laugh along with me. So when he told me that my co-chair would be this splendid man, Erskine Bowles and Bob Dole and Elizabeth called me within moments of the time, and said, this is one of the finest men we have ever worked with. So we started up. And it took us

three months to establish trust. There was no trust among the A team. The first slap was, who is the biggest spending president in the history of the U.S. before this person. The answer, George W. Bush. Never vetoed a single spending bill in six and a half years until it came to stem cell research which really wasn't a spending bill. Then the scrap would go to the other side, but this guy has outdone him, 3 to 4 to 1. So finally Erskine and I said, look we will tell you what we are going to do. We are just going to do a two man report. We don't care if anybody joins it, but we are not going to do.... There is too much ... that comes out of commissions. So as we worked, they came forward and we got 60 percent of the commission to vote for it. Five Republicans, five Democrats and one Independent. If you want to give accolades, give it to the four Senators who are still there, Crapo, Coburn, Dick Durbin, remarkable person, and Kent Conrad. So as we go around telling this story of a situation which is unconscionable, unsustainable and totally predictable, and people just sit out there and blink like a frog in a hailstorm. They don't have any idea what the hell is going on. So we are going to share that with you today. And I just usually start my remarks, which I will do, it is very simple, if you spend more than you earn, you lose your butt and if you spend a buck, and borrow \$.40 you've got to be stupid. And that is where we are. (APPLAUSE)

Erskine Bowles

You have now seen Cher, I am Sonny. I tell you traveling around the country with this guy, Al Simpson, has been the greatest experience of my life. I know I am a Democrat and he is a

Republican, but I am telling you, I have never enjoyed, respected, or liked anybody more than I do this guy. And if you want to know why our commission was successful, you need to look no further than right here. He has that kind of wisdom and that kind of sense of humor and warmth that can bring a diverse group together to find commonsense solutions to a really tough problem. He is the best. I want you to give him a round of applause. (APPLAUSE)

I also want to thank Dave Cote. Who brought some commonsense and some business acumen to our commission. Dave is the CEO of Honeywell. And how he did it, I will never know, but he made every single one of our meetings, so Dave thank you for all you did. (APPLAUSE)

I didn't bring any notes, so I am going to go straight to the point. I think this country faces the most predictable economic crisis in history. It is as plain as the nose on my face. I think the fiscal path we are on is totally unsustainable and if I had to characterize the countries position today, I would say this debt is like a cancer that will truly over time destroy this country from within.

I will give you just one example and I got it from Bob Kerrey about a year ago. He said, "Erskine if you look at today's federal income statement" and unfortunately if you put an income statement in this hand and a balance sheet in this hand and you ask most of the members of the Congress which is which, one or two might get it. But he said, "if you look at the current

situation of a country, 100 percent of a revenue that flows into the country is being consumed by mandatory spending and interest expense". That means every single dollar that we were spending on that day for these two wars, for our military, for national defense, for homeland security, for education, for infrastructure, for high value added research, every single dollar was borrowed and half of it was borrowed from foreign countries. That is a formula for failure. And if you just think about where we are going, if we stay on the current path, if we do nothing, by the year 2020, we will be paying annual interest cost of over \$1 trillion a year. It is crazy.

This is a problem that we can't grow ourselves out of. You could have double digit growth over the next two decades and not solve this problem. We can't tax our way out of this problem. Raising taxes don't do a darn thing to change the demographics of a country or the fact that the healthcare costs of this country are growing at a faster rate than GDP. And for those of my friends in the Democratic party who think we can solve it all with taxes, well to do that you would have to raise the highest marginal rate to 80 percent, the corporate rate to 70 percent, the capital gains rate to 50 percent; now how many people want to start and grow a business in that kind of environment. Think what that would do to the economy. That is not a solution. And for those who think we can cut our way out of this problem, nothing drives me crazier than to watch these guys go on television and say, oh yeah, let's just cut spending. But just don't touch Medicare. Don't mess with Medicaid. We can't do Social Security. We have to pay interest on the debt, and for God's sake we can't touch defense. You know because we have to stay safe and secure. So you take all of those things off the table, and you have to cut everything else by

75 percent. That simply won't work.

So what Alan and I did, we tried to come up with a commonsense, balanced, reasonable approach to balancing the federal budget and getting our fiscal house in order and we based it on six really easy principles.

1. The first is that we didn't want to do anything that would disrupt a very fragile economic recovery. That is why when you look at our forecast, you will see that the major cuts in spending occur in 2013, where we do get spending back to 2008 levels in real terms. Pre-crisis levels. I think you will hear the Republicans talk about getting it back to 2008 levels in 2012. We weren't willing to take that risk because we didn't want to do anything that disrupted a very fragile economic recovery.
2. The second basic principle was we really wanted to do everything we could to protect the truly disadvantaged. We think that is what America is all about. And that is why when you look at our Social Security plan, you will see that we have made our job more difficult by actually upping the payment, the minimum payment to 125 percent of poverty and by giving a bump to the people who are called the "older old", people between 80 and 86, because every economist that came in to see us said that is when people need Social Security the most. So we tried to do those two things.

3. Thirdly, we did want to make sure the country is safe and secure. But I personally don't believe that America can afford to be the world's policemen and I certainly don't believe that we can spend on national defense 14 times more ... well I guess it is more than the 14 largest countries combined, that come after us in size. We just can't do it. It doesn't leave enough resources leftover to invest in this country.
4. That was our fourth criteria. We did want to make sure, as the president said, that we invested in education and infrastructure and high value added research, so America could stay competitive in what is today a knowledge based global economy. But we only want to do it, if we could do it in a fiscally responsible manner. That is why when we looked at research we were able to make some cuts in research. As Andrew said I spent the last five years as president of the University of North Carolina, which is a 17 university system and we did beat Duke. I am looking right at John Mack. But you know, if you think about it, the U.S. has today, over 375,000 research projects going on, on 3,000 different universities. I can tell you, in a time of limited resources, we can cut some of that research out and reinvest it in other areas or use it to pay down the debt.
5. Fifthly, we wanted to make sure that we reform the tax code. We wanted to broaden the base, simplify the code and eliminate tax expenditures and use the proceeds to bring

down rates and to reduce the deficit. Today we spend \$1.1 trillion on these tax expenditures. The whole total income that comes into the country, from tax revenues, is only \$1.1 trillion net. If we eliminated these tax expenditures, we can reduce tax rates to 8 percent, up to \$70,000, 14 percent up to \$210,000 and the maximum tax rate would be 23 percent. We could take the corporate rate to 26 percent and we could put in a territorial system which would bring all of that money back to this country, and I think America would once again be competitive and it would be a great place to start and grow a business.

6. Lastly, we wanted to cut spending and we wanted to cut spending wherever it is. All of the arguments you read about in the paper today is a Republican saying we want to cut \$61 billion and a Democrat saying we want to cut \$10.5 billion. Let me just put that in perspective. A \$61 billion cut on a \$3.7 trillion budget, is a 1.6 percent cut. There is not a sole sitting out here today or behind me that couldn't cut their budget 1.6 percent. The whole problem in where we are today is all of the discussion is focused on the domestic discretionary spending budget, instead of focused on the whole budget at large. We have to make real cuts. And that is what Alan and I recommended.

Our recommendation was and we recommended that we reduce the deficit by \$4 trillion over the next eight years. We took the debt to GDP ratio to 65 percent by 2020 and to 60 percent by 2023, which was our goal. We cut the deficit to GDP ratio to 2.3 percent in

2015. The president gave us a goal of three percent, so we cut it in half and we cut it by three-quarters by 2020 to 1.2 percent of GDP. About two-thirds to three-quarters of our deficit reduction was on the spending side. A quarter to a third was on the revenue side.

That is what we did. We think it is a balanced, reasonable, supportable plan and what we need, if we can answer your questions and answer them accurately, is your support, to go out there and help us sell to Congress and this administration, on taking this plan or something as serious, forward. Thank you very much.

QUESTION AND ANSWER SESSION

Andrew Tisch: Gentlemen thank you. You are going to be back up here in about one second but to continue with today's theme of bipartisanship, sitting on your left is our Glenn Hubbard, former chairman of the club and Dean of the Graduate School of Business at Columbia University and former chair of President George W. Bush's Council of Economic Advisors. And on your right is former Senator Bob Kerrey of Nebraska. Senator Kerrey was also president of the New School here in New York. So these are our questioners today and gentlemen if you would come back up here into the firing line and Senator Kerrey, the first question is yours.

Senator Bob Kerrey: Well Alan, to either you or Erskine, I mean Alan was on an Entitlement Commission with me back in 1994, so both of us have experience in trying to present to the Congress, relatively modest changes. The two that we did was Social Security and means testing of Medicare. Neither one of them went anywhere in a political environment that was considerably easier than today. You both have had plenty of opportunity to speak with President Obama. What is it going to take from Republicans and Democrats to get him to come publically and lead on this issue.

Alan Simpson: Well first of all I would not have taken the job until we visited with him, which we then came back and we said, look, I am only going to do this if your healthcare proposal is on the table with everything else. He said, that is fair. He then brought the commission together to tell them the same thing. It has been ... you can tell that it is vexing for him. He knew that if he came out with anything close to this full package first, that he would be savaged. And he would have been. So then the Republicans watched that and belittled it and then came out with their mountain roared and they gave birth to a mouse too. But they weren't going to do anything great because they would have been savaged by the White House. This will end. There are things going on now and I have to rely that we have a lot of allies in this game, on both parties; Joe Biden, Steny Hoyer, Dick Durbin, President Clinton. There are a lot of guys. Jim Baker. I mean, it is people from the whole spectrum of politics in America who go to the president and say, you have to do it. Someone described it as maybe in a very charitable way, as

Nixon/China experience where with courage he did something that was sweeping. But I can tell you that at some point, very soon, when that limit extension comes up, I am sure there will be a room, a dark room somewhere, where they will all take the pledge, so no one will say that this person presented this and we all bought it. And it will come. But there are new people around the president, who is very helpful; Jack Lew, who is a very close friend of Erskines. Bill Daley who you know, whatever party, he knows how to make the trains run. Gene Sperling, our Executive Director, Bruce Reed, is now the Chief of Staff of Joe Biden. You have six U.S. Senators who had a retreat yesterday to visit with 31 other colleagues to see about putting this into legislative language. The president, at some point....all leaders have to lead, and anyone who is a leader takes a lot of flack. And if you don't want to take the flack, don't lead. And that eventually will have to be him leading. He's your man...you go ahead.

Erskine Bowles: This is a process. It is like any other negotiation that you all do. I remember back, and Bob you remember back in 1997, I was President Clinton's point man to negotiate the bipartisan balanced budget. And I spent literally months and months locked up in conference rooms with Newt Gingrich and Trent Lott and you all owe me a lot for that, I am telling you. But it was the right way to go about it. The only way you ever reach a deal is to listen to the other side, to know what they can do and what they can't do and to build up some trust and confidence and mutual respect. Then you can go together and you can find out what you can do, and get a deal done. That is what we did in 1997. I believe that is what will happen this year. We had both hoped the president would do more early on, but I think he is engaged in

a process that can lead to the promise land. He showed us a little leg in the State of the Union. He showed us a little bit more in the budget. I think he has, by appointing Joe Biden, and again as Alan said, Joe Biden's Chief of Staff was our Executive Director of our Commission. By appointing Joe Biden I think he has appointed the right guy to lead the negotiation efforts. Now, what I hope they will do is they will go down and they will meet quietly. You are not going to get there if you go on television and you talk about the few little things like these cuts that the Republicans are oh, they are going to hurt your grandmother and your mother and all of your children and your dogs ...dogs are really important in the South. The Republicans go on to say, all these guys want to do is tax, tax, tax. What we have to do is go in there and really work this out. I think the leadership of what Senator Coburn and Senator Crapo and what Conrad and Durbin and then now Senator Warner and Chambliss have done, is the right step forward. I think they are going to come forward with a proposal in legislative language that is very similar to the plan that was developed by the fiscal commission. I think you will see the president lean into that plan. So I am hopeful that we are going to have some results at the end of the day, the president and the leaders of the House and Senate, in both parties, in both houses, have to get on board if you want to get a deal done.

Glenn Hubbard: Well thank you, Erskine and Senator Simpson. I know I would join everyone in thanking you for the leadership that you are bring to probably the most important domestic topic in the country. If I go back and think about the question Bob Kerrey led off with too, if you take the topics you have teed up, comprehensive tax reform, entitlement reform, a

broad based entitlement reform, home mortgage interest deduction, federal, civilian and military retirement, I could be reading, and in fact I just did, from the 1994 Danforth/Kerrey Commission Reports. So these topics have been around a long time. What will it really take to bring people together. Bob asked you about the president, but what kind of sign do you think he is looking for from the Republican leaders and are there any specifics, particularly in Social Security and healthcare, that the two parties should be able to come together on?

Alan Simpson: Well I think one of the greatest motivators for a politician is fear. I think you have an interesting thing happening here. It is tough for the House and the Senate to find people to serve on the Appropriations Committee. Well let me tell you, when I got there, you fought and clawed your way to get on the Appropriations Committee. So they are having trouble getting people to come on because for years you were hired on to go get this, go get the YMCA, get the grants, get this, tariffs, all the things that go with it, work the tax code, bring home the bacon. And now the pig is dead, and there is no bacon to bring home. People now are concerned. These people, all of us at one time, worshiped the God of re-election. And that is a very subtle and seductive Messiah. We are almost like people who learned too much. Here is one for you. Now don't throw anything because now you are into the real reasons why things aren't working. I was in the military for two years, active duty and I was in the Reserve. If I had stayed another few years I would be what is called a military retiree. There are only 2.2 million of them. Their lives have been disrupted. Many saw combat, many didn't. They have their own healthcare plan which is separate from the VA, Veterans Administration, separate from any healthcare system.

The premium is \$470 a year. They use the commissaries and the Class VI stores, that is the booze, it's cheaper there. Class VI was a great phrase. And they have no co-pay and they take care of all of their dependents. And as I said, the premium is \$470 a year and the cost of that system is \$53 billion a year. And we said, you know, don't you think maybe you could pay \$4,700 a year which would be like....pretty good, and we said to Gates, why didn't you ever get that one done? He said, are you kidding, here come the VFW, the American Legion, the DAV, the military retirees, you can't even budge. So you haven't seen anything yet. Look at the AARP, those are 38 million people bound together by a common love of airline discounts and automobile discounts. We went to them and said, can't you help... you know what we have to do with Social Security. They said, we have two modest things to suggest at appropriate time. We said, could you share it with us, what they might be. Well we will, as you get towards the end of your fine work. I like the new guy, Rand, he is a good egg. But John Rother has been there 35 years, smiling, as I have stumbled around trying to get them to do something. And so, we said, when will you tell us, and they said, well we will, I promise you we will. And right now, we have this situation where these people have done nothing and if they continue to tell people to do nothing, when you waddle up to the window in 2037 to get your check, it is going to be 22 percent less. And I think that is just cheap and cheating. So I said to the other hierarchy, are there any patriots here or just marketers. They are the biggest marketing system, they are 1.5 percent of all mailings under that permit. And they said, well they helped with the prescription drug issue. Why not, they are the biggest drug company in the world. So tear up your card and we will move on to the next item. I didn't hear a lot of applause on that.

Erskine Bowles: But he is right.

Alan Simpson: No, nobody applauds whenever Erskine and I are out doing this stuff.

Erskine Bowles: Let's talk about Social Security first. We have two very controversial recommendations. The first controversial one is we raise the retirement age. Yes we do. We raise it in 40 years and we raise it again in 65 years. Now some of you sitting out there today may believe that you are eligible for Social Security when you turn 65. You are not. Today, eligibility begins at 66. And under current law, it goes to 67 in 2027. We raised it to 68 in 2050 and to 69 in 2075 when my grandchildren will finally be eligible for it. I think that gives people long enough to prepare. Now some people said, well what about if you are going to raise the retirement age, what about those people who have backbreaking jobs that are involved in physical labor who can't really wait that long to retire. We said that is a really good point, let's address it and we did put in a hardship provision for the 20 percent of Americans who have that kind of job and we would pay for it. The second controversial provision of Social Security was, we raise the cap on payroll taxes. We did that. You all know what the cap is today, it is \$106,800. Well it was originally based on 90 percent of average payroll. Well, now it is at 82 percent of average payroll. We took it back to 90 percent. What does that mean? That means in 2020 instead of having a cap on Social Security and paying taxes up to \$168,000, you will pay it

up to \$190,000. So you will pay Social Security taxes on an additional \$22,000. Now why did we do it? We did it because Social Security is going to go broke in 2037. It is just arithmetic. And when it happens, benefits will have to be cut by 22 percent. That is the law. And so what we wanted to do was to protect the truly disadvantaged. We already talked about that. And we wanted to make it a little bit more expensive for people like us. And we felt that if we did that then we could have solvency in the Social Security fund over the next 75 years. You know, FDR was a pretty smart guy. Life expectancy when he put Social Security in play was 63. You were eligible for Social Security at 65. Today life expectancy is 78 and you get it at 62. So it is a little wonder the arithmetic doesn't work. Healthcare Glenn, you asked

Alan Simpson: Just one thing on the Social Security. There were 16 people paying into this system in 1950 and one taking out. In 1960 there were ten people paying in and one taking out. Today there are 3.1 people putting in and one taking out. And in ten years, there will be two people putting in today, and a senior taking it out the next month. Now that is absolutely unsustainable and everybody knows this. And the trustees are Democrats and Republicans who put out a report periodically and these...you cannot refute these figures. But they do refute them, they just say don't touch our Social Security. Put in it from the beginning, and they want it all out. And I say, well if you are 79 like I am, you never put in over \$874 a year in your most productive years at 30 or 40. And that is everybody. Then it went to \$1,200 and it went to \$1,500, and \$2000 and \$3000. This is real. The reality is not a big staple.

Erskine Bowles: Healthcare. It is by far the biggest single financial issue our nation faces today. Today if you just take three components of federal healthcare spending, Medicare, Medicaid, and the CHIP program, a children's health insurance program, they consume about six percent of GDP. That will be ten percent of GDP before you know it, if nothing changes. That is really a conservative number because it doesn't count, and there are so many things that the Federal Government doesn't count. You remember that Bob. I mean it is just unbelievable. They don't count \$276 billion that it costs to do what is called the DOT fix and they don't count \$76 billion which it takes to repeal what is called the CLASS Act. Never mind what they are. Those are just facts of what it will take. So the cost of healthcare is growing and growing rapidly. Now the Democrats believe that the Affordable Healthcare Act will slow the rate of growth in healthcare to GDP plus one. And they believe that because they put in all of these pilot projects which are supposed to bring down the cost of healthcare. Alan and I and Dave had our doubts about that. And so we put in an additional \$430 billion worth of cuts between now and 2020 to slow the rate of growth of healthcare. These cuts come directly from Medicare and Medicaid and we think they are done in a responsible manner and they are detailed and we can discuss them if you want to. Our hope is that, that actually will slow the rate of growth in healthcare to GDP plus one. But again, we have our doubts. So we put a global cap on healthcare costs at GDP plus one, and we said, if in fact healthcare is still growing at a faster rate than that, then the nation is going to have to take some more dramatic steps and more drastic steps. We are going to have to do things like match the eligibility age for Medicare to Social Security. We are going to have to look at block granting Medicaid. We are going to have to

look at a premium support plan, which is similar to what was sponsored by Paul Ryan, chairman of the House Budget Committee and by former Director of CBO Alice Rivlin. That is basically a defined contribution plan rather than a defined benefit plan. Similar to what many of your companies have had to go to, to control your costs. We will also have to look at things like an all payer plan or a single payer plan. But we are going to have to take really drastic steps because we can't allow healthcare to consume the rest of the budget or we won't be competitive in the future and we won't be safe.

Senator Kerrey: Well Alan, and Erskine ... Alan your quite colorful description of seniors provokes a very narrow question here, because it seems to me as I watch politics, oftentimes, the most interesting is the question that is not being debated. So as you know, the very famous quote, by I think Sam Rayburn or maybe it was you, who said, there are two kinds of people in Washington, people who can count and people who lose. And people who run for election can count. I don't know if you saw the ... I thought quite brave comments by the Republican Governor of Indiana, critical of what the Republicans did at the midterm to go after the \$500 billion for the savings in Medicare over ten, and got a 23 point margin of people over the age of 65. The entitlement problem was made worse in the first decade of the 21st century because a prescription drug was added. Then, long-term care gets added. Prescription drug was made more generous in the healthcare plan, trying to win AARP over. Don't we.... I say to both of you, or ask to both of you... don't we have to begin to debate how much we should be spending over the age of 65. You could actually make the case that it is not excessive today. Although it

has gone from about \$20,000 expenditure per household ten years ago to almost \$38,000 today, don't we have to have a debate about what is a reasonable amount of our income that we are going to transfer to people over the age of 65.

Alan Simpson: Well you get into the moral issues and Bob and I really worked together. We even worked on a balanced budget constitutional amendment, wasn't that another suicide mission that we enjoyed. You know, Dick Lamm, the former Governor of Colorado, a friend of ours, all of us, he speaks like that, and boy I tell you, they ripped him to bits. You know, so you are going to let him die, are you. And it goes to there. And it is very sad. But you have to remember that there isn't one of you here that doesn't know a friend or a relative who in the latter years of life, may be 90 and in good health, a woman in Cody Wyoming the other day, not New York, 90 years old, heart attack, sharp as a tack, off she went. Well we better fly her. No need to take an ambulance to Billings. So you get the night flight and the day flight and the sonar and when it was all over she lived a comfortable 10 years and finally the last few days and died and the cost of it was \$400,000. Now multiply that by Americans and where we are. So it is an issue that won't get debated but I tell you, there is a way to do it with Medicare and try this. You cut providers fees, ie., doctors and others who provide. You increase the co-pay for patients, and you affluence test the patients and then you let hospitals keep only one set of books, instead of two or three, where they can get into the Federal Treasury with greater skill. Those are harsh things. And Medicaid, tell them the gimmick on Medicaid with the states. Listen to this

Erskine Bowles: Here is a perfect example of the kind of thing that we cut out in our plan that happens every day in most states. Most states have started charging a higher tax or higher fees to providers of healthcare. And then they turn around and let the healthcare provider charge a larger fee to the customer for the services they render. Well lo and behold they kind of come out even, the provider does, the state gets a little bit more money coming in and who pays, you do. Because there is a federal two for one match in Medicaid. And so the cost goes up and it is a \$44 billion number that the taxpayers have assumed. We cut that kind of gaming out in order to bring sense to this healthcare spending. That is one of the ways we got the \$430 billion out of healthcare costs.

Alan Simpson: Well Bob is so right because this Social Security system is not a retirement, as I say, it is an income supplement. It had nothing to do with retirement when it was setup. It was an income supplement. The Depression. And it was never built to handle disability insurance which will go broke in eight years. And when it goes broke, guess who picks that one up, the Feds. And the 22 year old thing, students, and so on, it was never built for that. Never structurally sound for that. And this is part of the problem.

Erskine Bowles: To me, the key thing for you all is don't let these politicians get away with talking about \$61 billion and \$10.5 billion worth of cuts just for domestic discretionary budget.

We took \$1.7 trillion out of a discretionary budget. We took \$430 billion out of healthcare. We took \$250 billion out of other mandatory spending. We took about \$238 of additional funding out of Social Security and we took away \$1.1 trillion worth of tax expenditures. You know, that is real money. That really addresses our problems. If people keep talking about 1.6 percent cuts, we are never going to get there. And if we don't get there, we have a hell of a problem on our hands. Admiral Mullen the Chairman of the Joint Chiefs of Staff just said recently, he said, our biggest national security problem is not these terrorists, our biggest national security problem is this debt. Because it will consume every single dollar and we won't have the money to spend to keep our country safe. If you think that investing in education and infrastructure and high value added research is important to be competitive globally, and I think it is, let me assure you, there will be no money for it if we don't address the rapid growth and the cost of entitlements. We have to put everything on the table and we have to have a realistic, commonsense discussion about it.

Andrew Tisch: Glenn, last question.

Glenn Hubbard: Just to underscore the point that you just made, it is true, just in one generation we will become a nation of paying interest on the national debt in entitlements unless we make a change. My question to you is about the length between the short term and the long term. The present course we are on has short term this, short term that, and the long term is just

a rehab center for short term policies. You gentlemen have focused the attention on the long-term, but I wonder if by doing everything in your plan, it becomes then harder. One example might be, starting with something like Social Security which is relatively easy to explain, and the solutions are relatively easy. You have mentioned them. Would be raising the retirement age, say moving to progressive indexing, taking bold moves in an area we know how to do, then perhaps giving us freedom in the short term to do other things that you have talked about like corporate tax reform and things we need to make our country competitive. Any thoughts on such a package?

Alan Simpson: I would just mention, one of the questions asked all during our commission, especially by Dick Durbin is where is the tipping point? Where is the tipping point here? Is it two years, is it three. Is it two months. All we could come up with is this. That we are, I think, of the basic opinion, whether you voted for the plan or not, but deficit denial is dead. And so we think that if these creditors, these people who hold this huge amount of our paper, are going to look this year very quickly before May 1st where the debt limit extension will be asked to be raised. There will be 87 people in the House that are not voting for that, unless you cut spending. And they will say, what spending do you want to cut? And if they say the usual ritual here, you know, Nancy Pelosi's aircraft, Air Force One, foreign aid, all that is a good start, but it is only about six percent. If that is what they say, they are going to watch and I think, I don't think it will be two years. I think it will be one or less when they say, we thought you guys were facing the gun and you didn't do anything of substance with the things that are on automatic pilot and

therefore we want some money for our paper. And all I know about money and paper is that money guys like to keep their money. And money guys panic when they see their money slipping down the rat hole. At that point, something will happen and we will not be destroyed as a country, we will just be a country, a nice country, but not number one. It is very difficult to tell the message without being called fear mongers, monsters, but remember this, everything we did in Washington while I was there, you use a deft blend of emotion, fear, guilt or racism. That is how you pass or kill a bill. You use a very deft blend of emotion, fear, guilt or racism. There will be plenty of savagery on what we are doing, brutal. It is out there, we are fully aware of that. Because all of us have had our skin ripped off in politics. It is a contact sport. That is why Kerrey is so ornery, he has had all of that. My father was governor and a guy walked up to him and said Simpson I wouldn't vote for you if you were Jesus Christ. He said, if I were Jesus Christ, you wouldn't be in my precinct.

Erskine Bowles: I want to answer your question too. Let me just give you one more example of how crazy the situation is. You know we have a treaty with Taiwan that we will defend it if it is attacked by the Chinese. The only problem is, we will have to borrow the money from the Chinese. I originally went into this thing, Glenn, thinking that what you proposed was right, that we would do some discretionary cuts and then we would do Social Security because it is basically arithmetic. It is easy to figure out, and we would build up some trust and confidence and that would be the way to get the deal done. Unfortunately I would have only gotten one vote for that. Until we took a comprehensive all-in approach we didn't pick up any support. But it

seemed like the tougher we made it, and the more realistic way we dealt with the problem, the more support we got on both sides of the aisle. And we ended up getting five Republicans and five Democrats and one Independent to vote yes, 60 percent. So I think that is our best hope.

Thank you very much. (Applause)

Andrew Tisch: Gentlemen you say that nobody applauds for you, well quite frankly we applaud you and we applaud your work, we applaud everything that you are doing to make this country better. It is important work. I think it is the most important thing that we can be doing today. So, again, thank you very much for the work you do and for keeping this as important an issue as much on the front page as you have. We look forward to supporting you in your efforts in the difficult times to come. Please, if you would, accept this token of our appreciation. It is just a little gift from us at The Economic Club and we thank you. (Applause) Just a couple of housekeeping details. The next club event will be a member-member breakfast on April 4th with former Federal Reserve Vice-Chairman and Princeton Economics Professor, Alan Blinder. Our next large event will be here, in The Hilton on April 11th, for lunch, where our guest speaker will be Janet Yellen, the Vice-Chair of the Board of Governors in the Federal Reserve System.

Anyway, again, thank you, and enjoy your lunch.

