

**Testimony of OMB Director Robert J. Portman
President's FY 2008 Budget
Committee on the Budget
United States House of Representatives**

February 6, 2007

- Chairman Spratt, Ranking Member Ryan, and distinguished members of the Budget Committee, it is good to be back in the hearing room with you. Thank you for having me before the Committee today to discuss the President's FY 2008 five-year budget proposal. We have good news for the American people. The President's 2008 Budget reduces the deficit every year and balances the budget by 2012, while meeting our nation's priorities.
- Mr. Chairman, and Mr. Ryan, I have had a number of conversations with each of you about what you are looking for in the President's Budget and how we want to work together to achieve balance. I hope you will appreciate that instead of painting a rosy scenario on revenues to get to balance, we take a cautious approach. I hope you will take note that we have responded to Congressional concerns by showing more war costs, and for the first time we have included these war supplementals as part of the budget in a transparent way. And all of those war costs are included in the calculation of reduced deficits and a balanced budget by 2012.
- I hope you'll see that we have changed our projections from past years from a freeze or a cut to include a slight increase in non-security discretionary spending throughout the Budget window, consistent with what Congress and the President have actually enacted for the past three years. You will also see that we have eliminated some policies that show budget savings but are unlikely to materialize because of congressional opposition.
- I've had many conversations with Republicans and Democrats on this committee about our biggest fiscal challenge: the unsustainable growth in entitlement programs, such as Medicare, Medicaid and Social Security. I will address this further in a moment, but the progress we are making on getting our fiscal house in order short-term must not distract us from this longer-term challenge. In this Budget, we've proposed sensible reforms, primarily in Medicare, that are less than a one percent reduction in the annual rate of growth, but that represent an important first step in reducing the unsustainable growth in these important programs.
- While restraining spending overall, the President's budget also provides new resources for key priorities. It increases funding for our national security to combat terrorism and protect the homeland. It includes new policies to address issues of concern to America's families, including educating our children, access to affordable health care, and reducing energy costs.

- On the whole, we have attempted to give you a credible and more realistic plan to maximize our chances of working together to achieve balance.
- Over the past two years, we have worked together to reduce the deficit by \$165 billion. We have been able to make progress for two primary reasons: first, because we have been blessed with a strong economy that has generated record revenues and, second, because we have done a better job of restraining spending, especially keeping non-security spending under inflation for the past three years. It is exactly these elements – a solid economy and restraint on spending – that can now lead to balance.

[Chart 1: Balancing the Budget Nominal and % of GDP]

- **As you can see from this first chart**, our budget reduces deficits every year and results in a surplus in 2012. In FY 2007, we project that the deficit will decline to \$244 billion – a reduction of \$95 billion since our last estimate in July 2006. The deficit in 2008 falls again to \$239 billion. As you can see from this chart, this projected FY08 deficit is 1.6 percent as a share of our economy, the key measurement of the deficit because it shows the impact of government borrowing on economic activity. The projected FY 2008 deficit is lower than 18 of the past 25 years, as a percent of our economy. The deficit then continues to decline each year, both in nominal terms and as a percentage of the economy, until we reach a budget surplus of \$61 billion in 2012.
- You will recall that three years ago, President Bush established the goal of cutting the federal budget deficit by half in five years from its projected peak in 2004. At the time, many expressed skepticism that this goal could be met, but we achieved this goal last September, three years ahead of schedule. We will now build on that success and work with you to balance the budget within five years.

KEEPING ECONOMY STRONG

Pro-growth policies

- To keep our economy vibrant, we continue pro-growth policies that have helped fuel our robust economy. The 2008 Budget continues to support growth, innovation, and investment by making permanent the President's tax relief, which would otherwise expire in 2010.

Economy/Jobs

[Chart 2: Tax Relief Resulted in Growth in Jobs and Business Investment]

- **As you can see from this chart**, since the tax relief took full effect in 2003, we have seen strong and steady job growth – with the creation of more than 7.4 million new jobs. We've also seen a dramatic increase in business investment. Productivity is also strong. And paychecks are growing.

Revenue

[Chart 3: Steady Economic Growth Continues]

- After 2003, the economy not only strengthened, but Federal revenues surged – hitting record levels over the past two years. The President's 2008 Budget uses five year economic projections that are in line with forecasts by outside experts. **As you can see from this chart**, we assume GDP growth will average about 3 percent over the budget window, closely tracking the forecast of the Blue Chip forecasters. This year, our 2.7 percent forecast is now below most outside forecasts and market expectations.

[Chart 4: Receipts Return to Historical Average]

- **As you can see from this next chart**, with solid economic growth, our total receipts are now slightly above the historical average of 18.3 percent – as a share of the economy – and we project receipts remain at or above the historical average for the five-year period.
- We have what I would term a cautious revenue forecast for this Fiscal Year, and going forward. We forecast revenue growth will be 5.5 percent in Fiscal Year 2007 and average 5.4 percent through 2012. This is below the 40-year average of 7.6 percent, and well below the dramatic 11.8 percent and 14.5 percent revenue growth we've seen for the last two years. In fact, it is below the actual first quarter FY 2007 revenue increase of 8.2 percent over the same period last year. As in the past, our revenue projections are produced by the career professionals at the Office of Tax Analysis at the U.S. Treasury. And, as was the case in the past two years, we may well find that our revenue projections are low.
- Even with a cautious forecast on revenues, this Budget demonstrates we can achieve balance by 2012 without raising taxes. In addition, we have plans to more effectively and efficiently collect the taxes owed. Our Budget helps close the tax gap in two ways. First, we improve the effectiveness of the IRS' activities with a \$410 million package of new initiatives to enhance enforcement and taxpayer service and to improve the IRS' technology. Second, we include in the Budget 16 carefully targeted tax law changes that promote compliance while maintaining an important balance between taxpayers and their government. These changes are estimated to raise \$29 billion over the next ten years.

SENSIBLE AND REALISTIC SPENDING RESTRAINT

- To keep spending under control, our Budget provides realistic spending restraint for the annually appropriated, day-to-day government spending that isn't focused on national security. It strengthens our efforts to better manage taxpayer resources, and it proposes significant budget reforms to eliminate unnecessary and wasteful spending. And as noted earlier, it also takes an important first step in implementing changes needed to address our long-term challenge: the unsustainable growth in entitlement programs.

Domestic Discretionary spending

- The 2008 Budget proposes to hold the rate of growth for non-security discretionary spending to one percent, below the rate of inflation. We believe that this is both fiscally prudent and realistic. As noted earlier, Congress and the President have done a better job restraining spending in this area over the past few years. In fact, the average growth in this area of non-security spending has been about 1 percent over the past three years, including spending growth in the long term continuing resolution that the House just passed. We believe we can address our nation's top priorities at this level of funding.
- Within discretionary spending, the Administration closely examines each program to determine if it is a priority and whether it is effective and producing the intended results. Based on these thorough reviews, the Budget proposes to terminate or reduce 141 discretionary spending programs for a savings of \$12.0 billion in 2008 alone. These reforms will help us reduce the deficit and channel resources to higher priority and more effective programs. We are able to make these judgments of how to spend taxpayer dollars more wisely, in part, with tools developed through the President's Management Agenda.

Management/ExpectMore.gov

[Chart 5: Expectmore.gov]

- Last year, to ensure greater government accountability, we launched a new website: ExpectMore.gov – **which is shown on this next chart**. The site includes information for taxpayers on the programs that have been assessed for effectiveness using the Program Assessment Rating Tool, commonly referred to as the PART. With this website, Congress and the public now have an unprecedented view into which programs work, which do not, and what they are all doing to improve. It's another way we are providing greater transparency, holding ourselves accountable – and demanding results.
- With the new and improved version of this website launched yesterday, we now have program-level information about the performance of nearly 1,000 Federal programs representing about 96 percent of government and \$2.5 trillion of federal spending. I urge Members and staff to check out ExpectMore.gov.

Budget Reforms

- The President's 2008 Budget also outlines a comprehensive series of budget reforms that will improve fiscal restraint, transparency and accountability in Government spending.
- The President has again proposed a legislative line-item veto. Mr. Ryan and this Committee led this effort last year, and both the House and Senate have demonstrated by a majority vote that each chamber supports this legislation. By allowing Congress to take a second look at legislation at the end of the process, we could work together to eliminate unwarranted earmarks and other wasteful and unnecessary spending.

- The Budget also proposes discretionary spending caps, expanding pay-go so it applies to both discretionary and new mandatory spending.
- The Budget contains the President's key reforms to the earmarking process, including, 1) full disclosure of all earmarks, 2) putting earmarks in actual legislation instead of in report language so they can be voted on, and 3) cutting the number and amount of earmarks by at least half.

Entitlements

- Our Budget shows how we can work with you to achieve a balanced budget by 2012, but that accomplishment will be short-lived without addressing our long-term budgetary challenge: the unsustainable growth in Medicare, Medicaid, and Social Security.

[Chart 6: Mandatory Spending is Overwhelming the Rest of the Budget]

- **As you can see from this next chart**, mandatory spending is overwhelming the rest of the Budget. In the space of four decades, mandatory spending has grown from 26 percent of our budget in 1962 to 53 percent of our budget in 2006.

[Chart 7: Current Trends Are Not Sustainable]

- **As the next chart shows**, the current trends are not sustainable. Under current law, we estimate that by 2040, spending on these and other important programs, plus interest on the debt, will crowd out all other spending—for defense, homeland security, and education—unless we make the necessary reforms.
- It seems to me there is now nearly universal, bipartisan agreement that the unchecked growth of these programs presents real long-term threats to beneficiaries, our federal budget, and the economy. We now face a \$32 trillion unfunded obligation in Medicare over the 75 year horizon. Our choices without reform will be massive benefit cuts, enormous deficits and huge tax increases.
- The balanced budget is important, in part, because it better positions our country to address these looming fiscal challenges. But our five-year budget proposal also makes an important down payment toward sensible reform of mandatory spending—reducing spending growth by \$96 billion over five years. These reforms are primarily in the Medicare program, but also in Medicaid and other programs. The proposals are similar in character to those this Administration has offered in the past.

[Chart 8: Past Reconciliation Savings]

- To put these reforms in context – **as you can see on this next chart** – the size of our budget proposal is considerably smaller than the savings in the Balanced Budget Agreement of 1997, the last we worked together on a bipartisan basis to achieve balance.

- Although an important first step, the savings in this proposal would only reduce the unsustainable annual growth rates of mandatory spending by less than one percent. Specifically, over 10 years the annual rate of growth in Medicare would be reduced from 7.4 % to 6.7%. However, while these proposals deliver relatively small savings in the short-term, the effects that build over time are substantial. The changes we have proposed to Medicare would reduce the unfunded obligation of the program by 25 percent or \$8 trillion over the next 75 years.
- Frankly, under our policies, we can achieve a balanced budget within the five-year window without these mandatory savings, but we would only be digging a deeper hole by ignoring it for another year. Balance is not coming at the expense of our nation's commitment to seniors and low-income Americans – quite the opposite. We must begin the reform of these programs now in order to protect those commitments. Addressing entitlement spending is the right thing to do because small changes now have a big impact later. I urge you to take a careful look at these sensible reforms.

INVESTING IN CRITICAL PRIORITIES

- As we restrain spending, we're also investing in our nation's highest priorities: combating terrorism, protecting the homeland and addressing pocketbook issues that affect the standard of living for American families.

Global War on Terror

- The 2008 Budget supports our troops fighting terrorism abroad, strengthens our military for the future, supports our efforts on the diplomatic front, and protects our homeland from attack. It invests substantial resources to maintain high levels of military readiness and to continue the transformation of our military to meet the new threats of the 21st Century.
- I want to make this next point very clearly because I find it is often misunderstood. The cost of the war is reflected in the Administration's deficit projections. In fact, there has been a \$165 billion reduction in our deficit over the past two years even with substantial war costs.
- As noted earlier, the Administration supports greater transparency and accountability, and this budget improves the timeliness and specificity of the information provided to you and the American public about the cost of the war.
- With the 2008 Budget, the Administration goes further than we have in the past – we show the full costs of the war for the rest of the President's term. We are providing our request for the full costs of the war in both FY2007 and 2008 – and for the first time including account level detail and justifications. Specifically, we are requesting additional resources of \$99 billion for FY 2007 to support Iraq, Afghanistan, and the Global War on Terror, \$145 billion for FY 2008, and an allowance of \$50 billion for anticipated war costs in FY 2009. The Administration welcomes oversight of its war spending, and we hope these details will help you more fully understand our war-related requests.

- This is our good faith effort to be as transparent as possible in what we anticipate the needs will be as far out as we can reasonably project.

Education, Health Care, and Energy

- The President's Budget addresses three key issues that are on the minds of many American families: the quality and cost of their children's education, access to affordable health care, and our Nation's dependence on foreign sources of energy from unstable parts of the world.
- Regarding our schools, No Child Left Behind (NCLB) is already working to achieve the goal of all students performing at or above grade level in reading and math by 2014. It has raised student achievement for millions of children in schools nationwide. The 2008 Budget directs more funding to high schools to better prepare our students for college or the workplace, and offers new school choice options so children in low-performing schools have a chance to attend a school where they can learn and succeed. To help low-income families afford college, the 2008 Budget substantially increases Pell Grant maximum awards.
- The 2008 Budget also improves Americans' access to affordable health care through a number of proposals. It proposes a significant change in the tax treatment of health care to expand coverage and bring greater fairness to the system. With more transparency and competition, it will also slow the growth of health care costs, all of which will reduce the number of uninsured Americans.
- The Budget includes a number of proposals to increase our energy security while improving our environment. As noted in his State of the Union speech, the President is proposing to increase the current standards for the use of alternative fuels and for fuel economy in order to cut our domestic gasoline consumption by 20 percent over the next ten years, thereby reducing projected air pollution and CO2 emissions.
- The Budget also continues the Advanced Energy Initiative to make alternative sources of fuel and electrical energy –like cellulosic, hydrogen, solar, nuclear and clean coal – more cost-competitive.

Conclusion

- The Budget before you shows that we can reduce the deficit every year and achieve balance in 2012 by keeping the economy strong and imposing sensible and realistic spending restraint. We are committed to working with all members of the committee to ensure that our fiscal house is in order for the time all of us will be in office – but also for the future. I am optimistic we can do it — across party lines — as the American people expect and deserve.
- Mr. Chairman, thank you for the time, and I look forward to your questions.

BUDGET

OF THE U.S. GOVERNMENT

FISCAL YEAR 2008



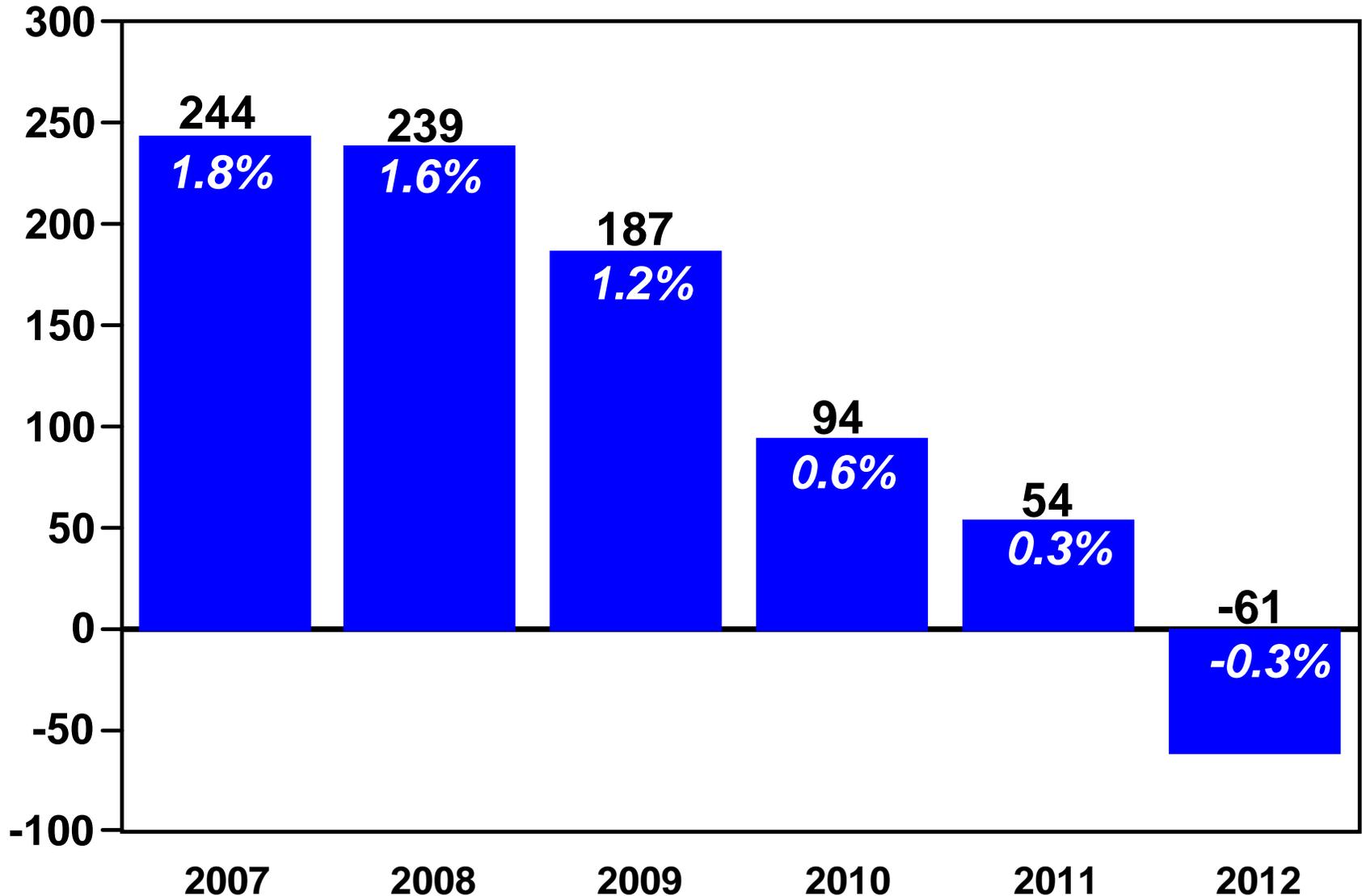
OFFICE OF MANAGEMENT AND BUDGET

Director Rob Portman

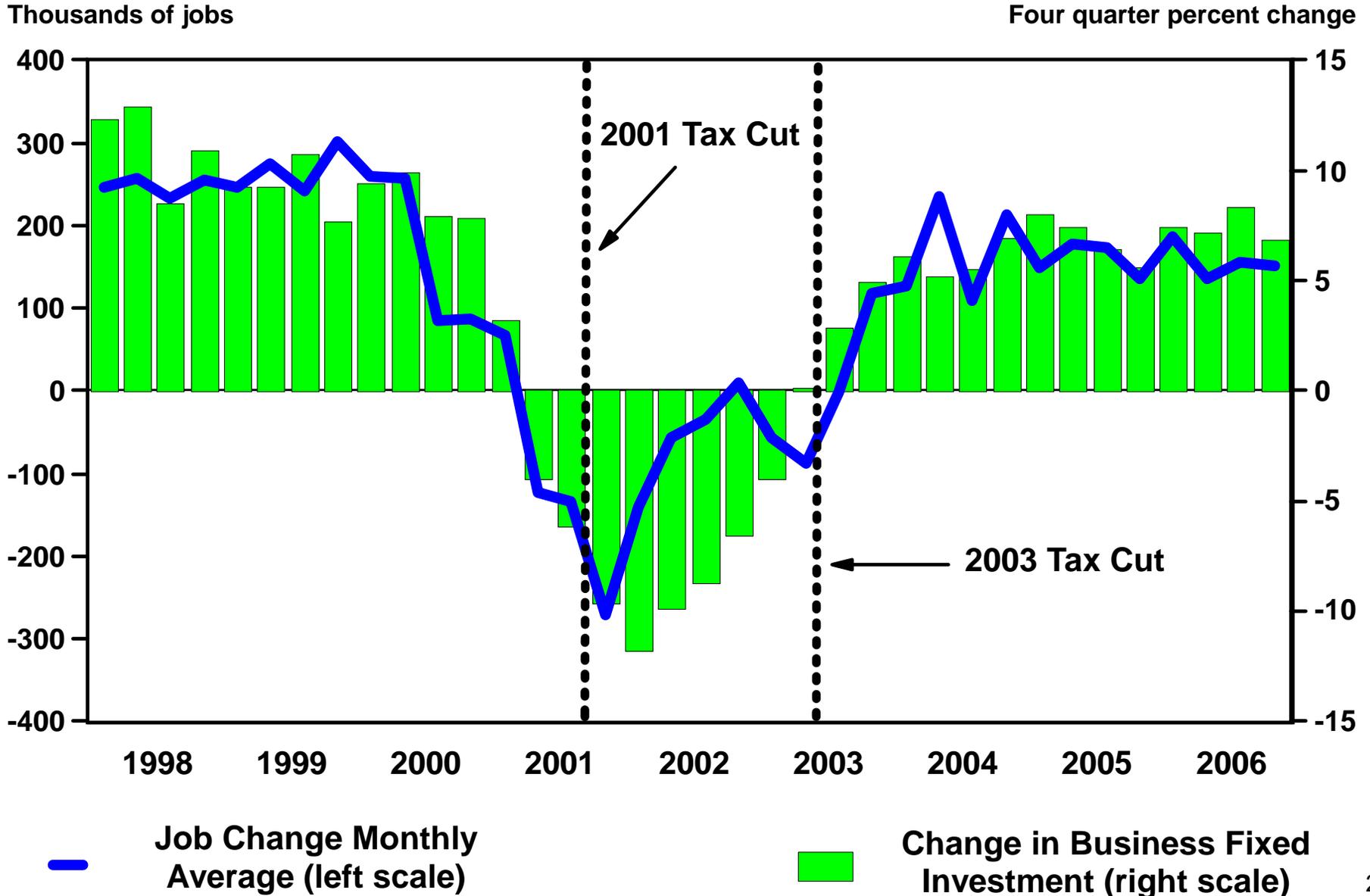
February 6, 2007

Balancing the Budget

Deficit in billions of dollars (*Deficit as a percent of GDP*)

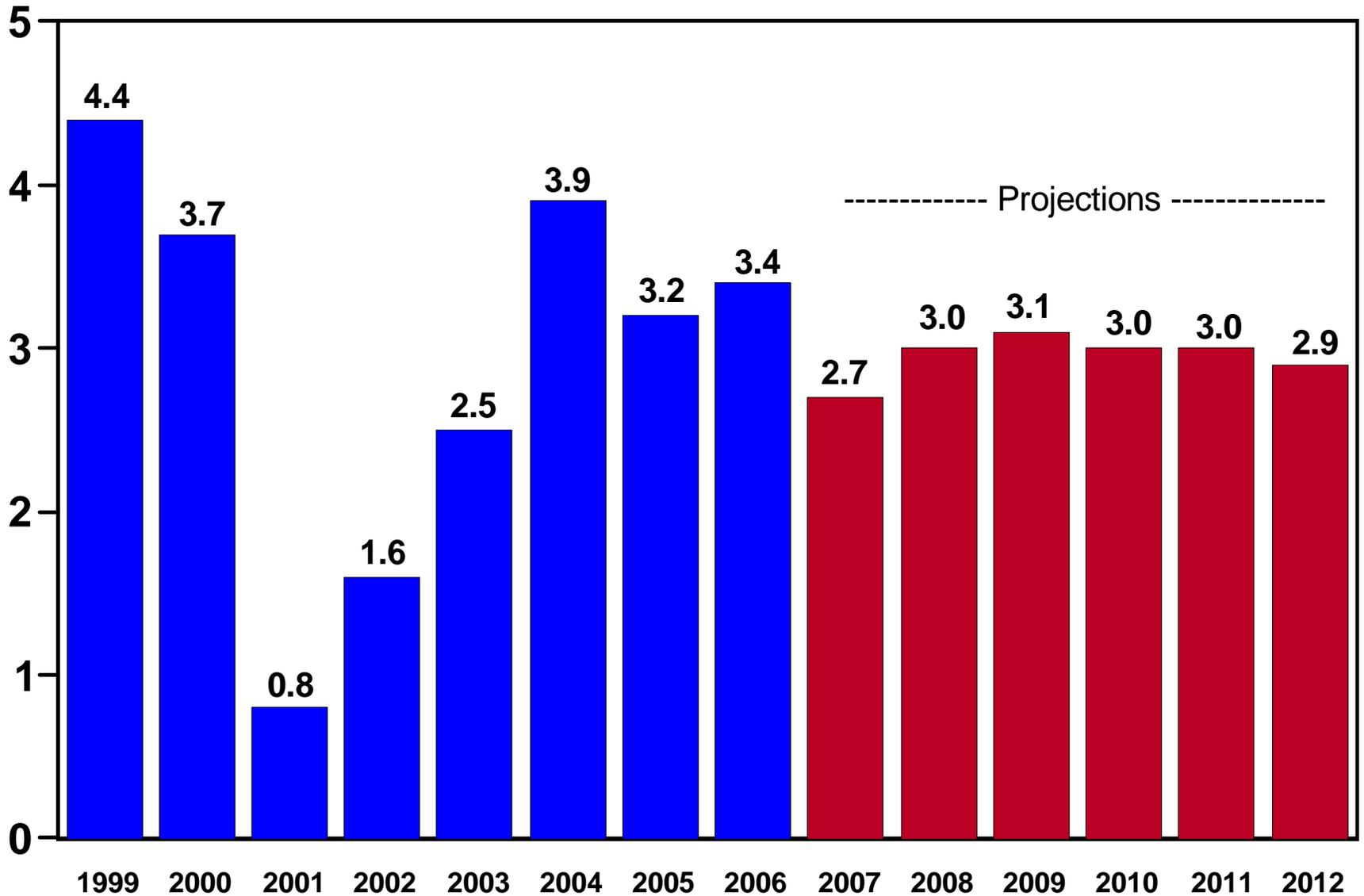


Tax Relief Resulted in Growth in Jobs and Business Investment



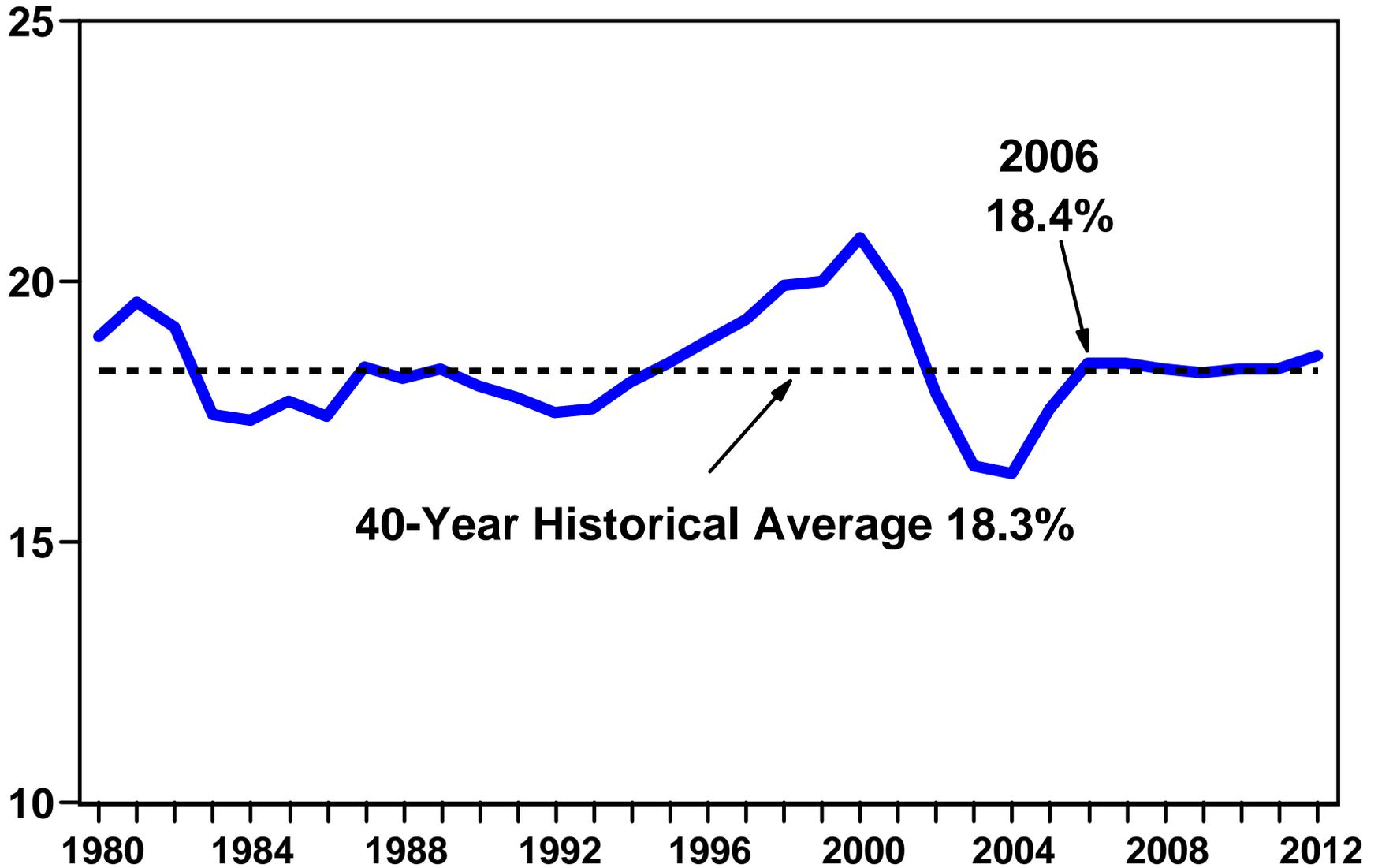
Steady Economic Growth Continues

Percentage real GDP growth, calendar year



Receipts Return to Historical Average

Receipts as percent of GDP



Expect**More**.gov

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The Federal Government is working to ensure its **programs perform well**. Here we provide you information about where we're **successful** and where we **fall short**, and in both situations, what we're doing to **improve our performance** next year.

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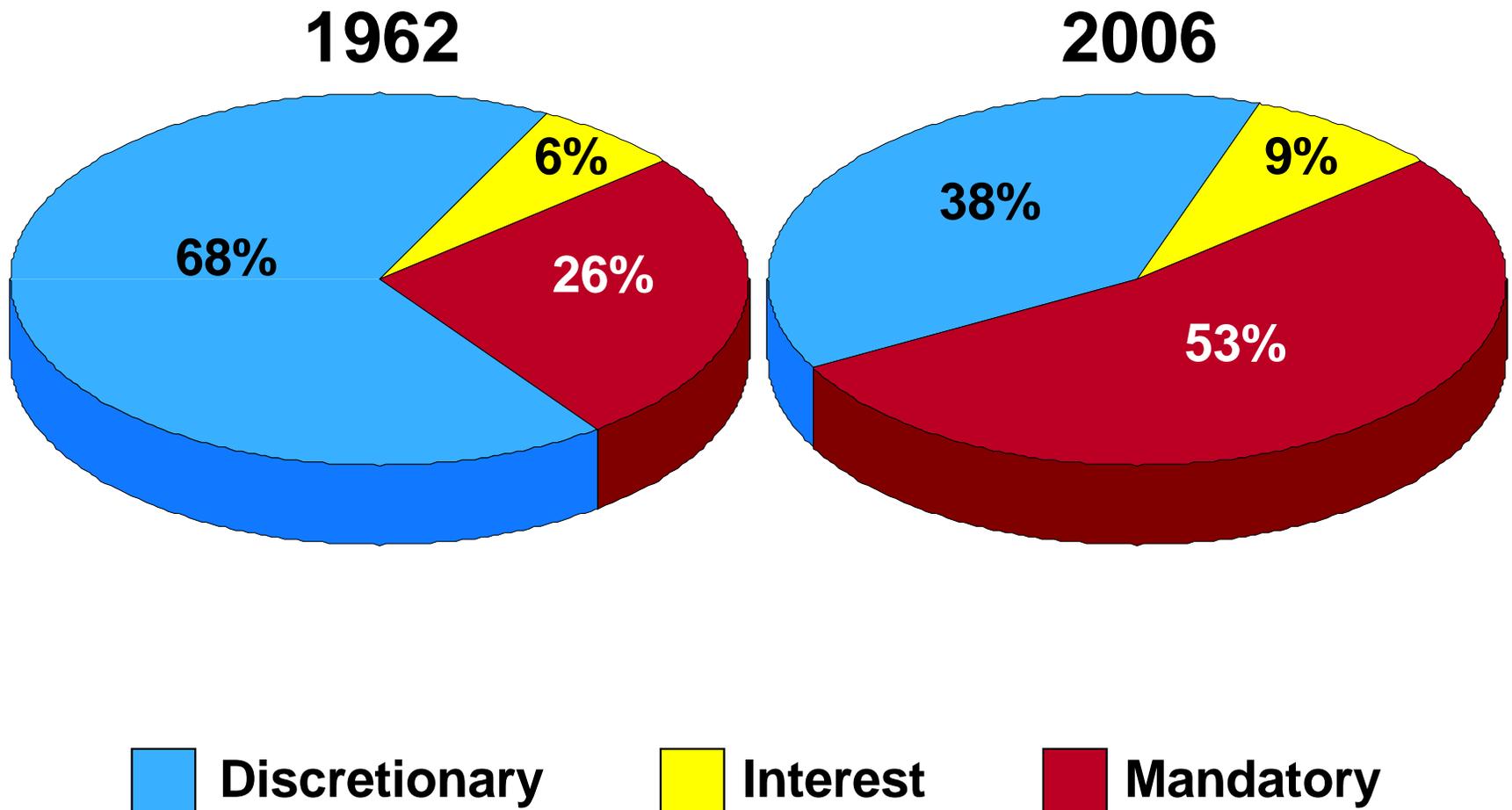
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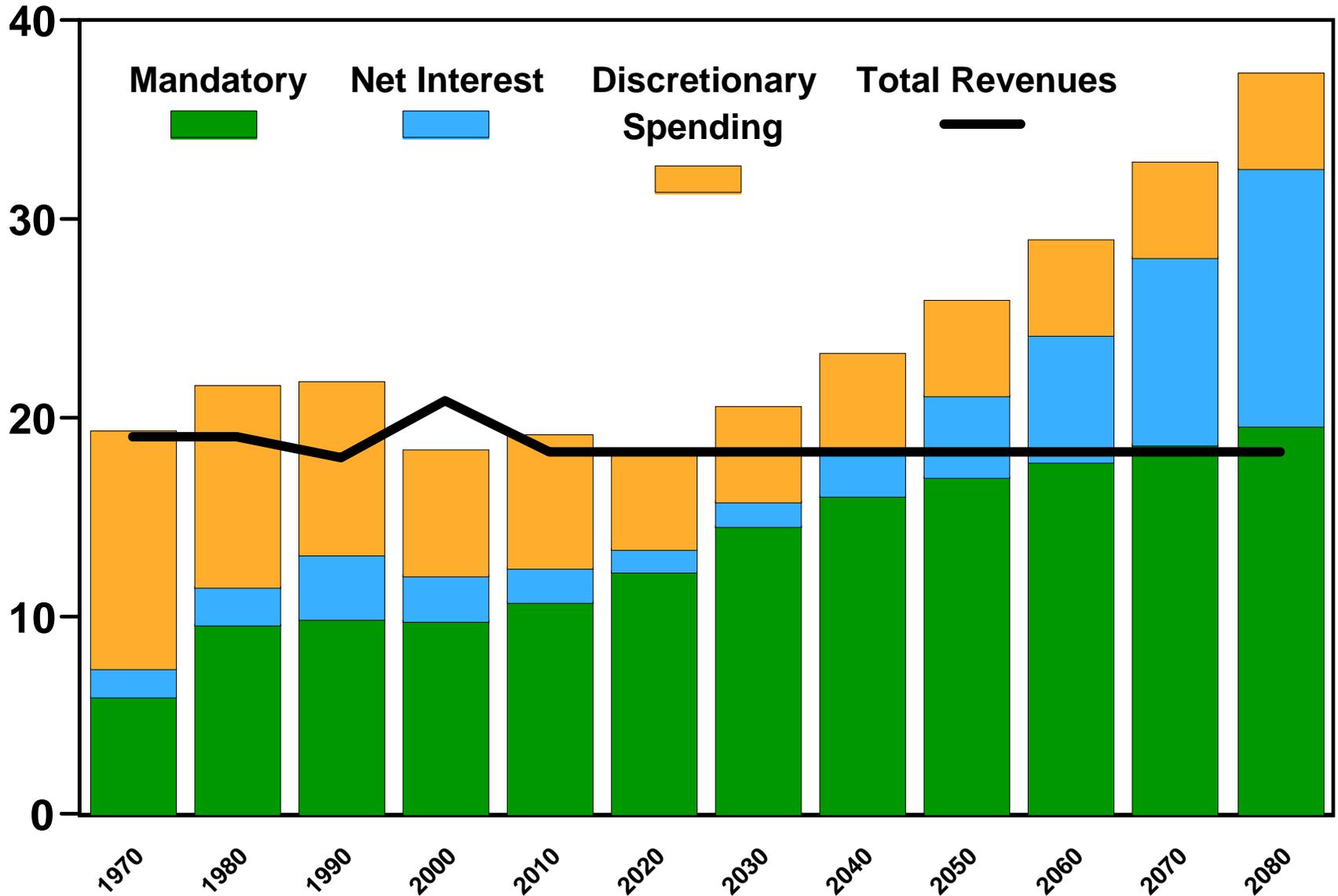
The content on ExpectMore.gov is developed by the U.S. Office of Management and Budget and Federal agencies.

Mandatory Spending is Overwhelming the Rest of the Budget



Current Trends Are Not Sustainable

Percent of GDP



Past Reconciliation Savings

5-Year Mandatory Savings as a Percent of Mandatory Baseline

