

Senate Governmental Affairs Subcommittee on Financial Management

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By: Hon. David M. Walker
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Dear Chairman Carper, Dr. Coburn and Members of the Subcommittee, I appreciate the opportunity to appear before you again – this time as a private citizen and as the President and CEO of the newly established Peter G. Peterson Foundation. As you know, I've changed my position on the battlefield for America's future. However, in my new position, I'm still very much concerned about our nation's financial condition, fiscal outlook and the other serious sustainability challenges we face.

My statement includes comments on four key issues: 1) the progress made in connection with the Fiscal 2007 Consolidated Financial Report and the future outlook; 2) the Foundation's new citizen's guide to "The State of the Union's Finances"; 3) the need for selected reforms and a fiscal future commission; and, 4) some of the Foundation's plans for the future.

Before I address our fiscal challenge, I will briefly touch on the results of the fiscal 2007 financial report and audit. As you know, I signed the report in my capacity as Comptroller General of the United States and head of the U.S. Government Accountability Office (GAO). Fiscal 2007 was noteworthy for at least two reasons. First, GAO was able to express an opinion on the Statement of Social Insurance. This statement includes the largest numbers in the federal government's financial report. Second, the Treasury Department issued the first Summary Annual Report for the U.S. Government. Special thanks go to Treasury Secretary Paulson, Treasury Undersecretary Steele and GAO Chief Accountant Bob Dacey in this regard.

While the above represent noteworthy accomplishments, it is unlikely that significant additional progress will be made in the near future. In fact, the Department of Defense (DoD) recently revised their estimated timeframe for achieving an opinion of the Defense Department's consolidated financial statements until 2017. In my view, this is too far out to be acceptable. As you know, my term as Comptroller General was set to end in October of 2013.

With regard to the Defense Department audit, in my view, the GAO should ultimately assume responsibility for the DoD audit. They will need to partner with the Defense Department's Inspector General and make extensive use of contractor support from one or more CPA firms to do so. They will also need additional resources which should be funded by DoD with the cooperation and consent of the Congress.

Now back to the bigger picture, just two days ago, the Foundation issued a publication entitled "The State of The Union's Finances". This citizen's guide provides a clear and compelling picture of our nation's true financial condition and longer-range fiscal outlook. Every member of the Congress, all Cabinet members, and each of the major Presidential candidates will be provided with a printed version of the Guide. It is also available electronically online at www.pgpf.org.

While the graphics and tables in the Guide look nice visually, they present an ugly picture fiscally. As the cover graphic depicts, based on historical tax levels and absent meaningful entitlement, spending and tax reforms, the United States will face debt burdens in the future that would make a third-world nation look thrifty. Furthermore, our related debt/GDP ratios escalate dramatically after the 2040 date shown in the graphic because we will have passed a tipping point by then. Furthermore, as one table in the guide notes, we are currently in a \$53 trillion fiscal hole. This hole gets deeper by \$2-\$3 trillion a year on autopilot. We need to stop digging and start figuring how we are going to start climbing out of it. The time for merely saying how one will pay for new spending increases or tax cuts is over.

What do we need to do? First, as I have testified before, we need to provide more transparency in connection with our current accounting and budgeting systems. For example, steps need to be taken to provide a fuller and fairer disclosure of where we stand financially and where we are headed fiscally. The Congress needs to consider the affordability and sustainability of major entitlement, spending and tax proposals over the longer term before they are passed into law. Congress must never allow what happened in connection with the Medicare prescription drug bill to happen again.

Federal financial reporting should, among other things, place more emphasis on fiscal sustainability and inter-generational equity. In addition, a Summary Annual Report should be issued every year. Furthermore, a longer-range Fiscal Sustainability Report should be issued by our federal government every four years, as is the case in several other industrialized nations. I have included in Appendix I of my testimony a summary of the types of reforms I advocated as Comptroller General of the United States. My views of these issues have not changed just because I'm in a new position. These reforms need to be aggressively pursued and acted upon.

In addition to the above steps, we need to re-impose tough statutory budget controls on both the spending and tax side of the federal ledger. After all, both sides of the books contribute to our nation's bottom line. Unfortunately, as we have seen in recent years, Washington still has not learned the first rule of holes: "When you're in a hole, stop digging." This must change, and the sooner the better.

In my view, the regular order for legislation is not adequate to deal with the number and magnitude of the reform efforts we must undertake if we expect to return to a more prudent and sustainable fiscal path. As a result, I support the need to establish a capable, credible and bipartisan commission to address at least four issues: statutory budget controls, comprehensive Social Security reform, and round one of comprehensive tax and health care reform. The SAFE Commission Act that is co-sponsored by Congressmen Cooper and Wolf in the House is intended to do just that. Similar proposals have been discussed by Senators Conrad, Gregg, Voinovich and others. In my view, if properly structured and staffed, such a commission could make at least a \$10-\$15 trillion down payment on our \$53 trillion federal fiscal imbalance. This would be a significant accomplishment toward addressing our nation's financial challenge, as well as a positive step that would help improve both the confidence in and the credibility of the Congress in the eyes of the American people.

- PV of projected receipts and outlays of federal programs and activities for 75-year and infinite horizons, including separate reporting for social insurance programs
- Statement of annual cash flows for programs and activities
- Reconciliation of changes from prior period Statement
- Presentation of information using different measures of sustainability and estimates of financial burden on different age cohorts and other demographics
- Explanation of assumptions used and sensitivity analyses
- First Statement of Fiscal Sustainability due no later than March 31, 2008

Additional Cost Information on Legislative Proposals before Adoption

- Before a Member of the House or Senate calls up for consideration on the floor of either House a bill or joint resolution or an amendment thereto that contains a proposal that would result in a significant increase or decrease in revenues or in mandatory spending, that Member shall obtain from CBO a statement of the long-term costs of such bill, joint resolution, or amendment.
 - CBO and Budget committees to jointly define “significant” for each Congress
 - “Long-term costs” are those financial costs over at least a 40-year period
- The statement from CBO shall be provided to the Members of either House, as applicable, and shall be published in the Congressional Record

GAO Report on the Financial Condition of the U.S. Government

- The Comptroller General shall annually report to the Congress his assessment of the financial condition of the U.S. Government. Report shall include analyses of—
 - the Consolidated Financial Statement (CFS) and the Summary Financial Report
 - results of GAO’s latest long-term fiscal simulations
 - the President’s Statement of Fiscal Exposures
 - the adequacy of information regarding long-term cost implications of existing and proposed policies
 - the Statement of Fiscal Sustainability
 - statutorily-required CBO and JCT reports for the prior fiscal year
- First annual report due no later than January 31, 2009

I believe that such a commission will likely be necessary in order to achieve timely action in connection with several of the major reform efforts that lie ahead. At the same time, we need to more proposals from individual members of the Congress and major Presidential candidates to help increase public awareness and stir debate.

We must keep in mind that, while Washington is a "lag indicator", gridlock in Washington is not good when we face a range of serious sustainability challenges that grow with the passage of time. The truth is that there are a number of very disturbing parallels between the factors that contributed to our recent mortgage-related sub-prime crisis and our nation's federal finances. These parallels have gone largely unnoticed. However, absent meaningful and timely action, we are likely to see an economic crisis that will make the current sub-prime challenge look like a bump in the road.

The parallels between the mortgage related sub-prime crisis and our federal financial sub-prime challenge include: 1) a disconnect between the parties who benefit from current practices and those who bear the risk; 2) a lack of adequate transparency and understanding regarding the nature and magnitude of related risks; 3) a re-enforcement of the importance of maintaining lender confidence and adequate cash flow as well as the limitations of credit ratings, and; 4) an illustration of what can happen when there is a lack of effective oversight and action to address large, known and increasing risks before a crisis occurs. These parallels are real. What is Washington waiting for?

Given the importance of our sustainability challenges, we at the Foundation believe it is important to find new ways to communicate the various sustainability challenges we face as a nation. We also believe that in this great nation, it is "We the People" who are responsible for what does or does not happen in capitals around the country. At the same time, the people cannot be expected to act if they don't have the facts, haven't been told the truth, or don't understand the consequences of failing to act.

As a result, in addition to publishing the new citizen's guide, the Foundation has decided to support the distribution of a feature documentary entitled I.O.U.S.A. This film addresses four key deficits facing America -- our budget, savings, balance of payments/trade and leadership deficits. It also highlights the efforts of the Fiscal Wake-up Tour in which representatives of the Concord Coalition, the Brookings Institution, the Heritage Foundation and I continue to participate. This film will be released in August in selected cities around the country, including the Washington, D.C. area. However, we believe that the film's message is so important, the Foundation has decided to hold a private showing of the film for members of Congress and selected other invitees on the evening of Wednesday, July 9 at the Library of Congress. I hope that all of you will be able to attend and that you will encourage your colleagues to do so.

Mr. Chairman, I have a DVD that includes a two-minute promotional trailer of the film you have kindly authorized me to show. Before I do, thank you again for the opportunity to testify. I look forward to answering any questions that you or the other members of the Committee may have.

Appendix: Transparency in Accounting and Budgeting

Appendix. GAO, *Long-Term Fiscal Challenge: Additional Transparency and Controls are Needed (Appendix I)*, Statement of David M. Walker, Former Comptroller General of the United States, GAO-07-1144T (Washington, DC: July 25, 2007)

Appendix I:

Transparency in Accounting and Budgeting: Legislative Recommendations of the Comptroller General

Supplemental Reporting in the President's Annual Budget Submission

- Produce as supporting information to the budget an annual Statement of Fiscal Exposures, including:
 - a concise list, dollar estimates, and descriptions of exposures, including—
 - information from Consolidated Financial Statements of the U.S. Government on total liabilities, contingencies, commitments, and net present value of social insurance program payments, and
 - long-term cost (> 40 years) of major tax expenditures, presented together with related spending or credit programs in the same policy area , if appropriate
 - dollar estimate of the effect on these exposures of all major spending or tax proposals
 - an assessment of methodologies and data used to produce such cost estimates
 - a graphic presentation of the dollar amounts of exposures presented as percentage of GDP for each year covered
 - Budget horizon expanded to cover 10 fiscal years
 - President shall include in the budget a statement of the President's budgetary goals for a 10-year period in terms of surplus or deficit and in terms of surplus or deficit as a percentage of GDP

Summary Financial Report for the General Public

- Pursuant to OMB form and content guidance, Treasury shall annually publish a summary financial report on the U.S. Government derived from the information in the audited annual Consolidated Financial Statements of the U.S. Government.
 - Report shall be in format and of length, content and sophistication for general American public
 - Report shall include condensed summary of CG's audit report on the CFS
- First annual report due no later than January 30, 2008 [Note: This requires an amendment to GMRA (31 USC 331(e)(1)) to make audited CFS due by January 15 each year and an amendment to the Accountability for Tax Dollars Act (31 USC 3515(a)) to make agency financial statements due by November 30 each year.]

Statement of Fiscal Sustainability

- Pursuant to OMB form and content guidance, Treasury to prepare and make public every four years an assessment of the long-term sustainability of all major federal programs and activities. Statement of Fiscal Sustainability shall include: