Written Testimony of Sen. Judd Gregg

Before the

Joint Economic Committee

United States Congress

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"Flirting with Disaster: Solving the Federal Debt Crisis"

Chairman Brady, Vice Chairman Klobuchar, Senator Coats, Representative Maloney and other members of the Committee, I appreciate this opportunity to discuss the state of the national debt.

Robert Zoellick, the past head of the World Bank, is fond of telling the story of how the Foreign Minister of Australia said to him a few months ago that: "America is one debt deal away from leading the world out of its economic doldrums."

He is right.

Dangerously, some observers believe the country has completed its work on deficit reduction. Despite some improvements however, the debt will continue to rise as a share of our economy over the long-term. This fact continues to present a serious economic danger for the United States.

We are now engaged in the struggle to obtain a debt deal large enough to stabilize the debt and put it on a downward path, at a time when Washington and the media are energized on the issue of dealing with the sequester.

We know the problem. It is that our present rate of accumulating debt due to our historically large deficits will inevitably lead to a fiscal crisis.

The drivers of our nation's long-term debt load

Any debt reduction plan needs to primarily focus on changes to those programs that are driving the problem. These of course are the major entitlement accounts, Medicare, Medicaid and Social Security, along with comprehensive tax reform.

While it is has been good to see progress made over the last two years on enacting some savings, unfortunately all of the measures put in place have ignored smart entitlement reforms to control spending over the long-term and comprehensive tax reforms to make the tax code more efficient. These are the primary fiscal challenges facing us, and we can no longer avoid them. We've done the easy work of deficit reduction – enacting discretionary limits and raising taxes on wealthy Americans. We must renew our focus on

the remaining elements of fiscal reform.

Rising health care costs and an aging population are the central drivers to our rising debt trajectory. We cannot continue to let health care costs rise faster than our national income. We must find ways to adopt sensible reforms to address population aging and rising health care costs this decade before costs reach untenable levels.

Smart entitlement reforms need to involve adjustments which grab hold in five years, ten years, and fifteen years so that they make these programs sustainable and affordable not only in the next few years, but in the long-term.

How deficits and debt inhibit economic growth

Professors Reinhart and Rogoff have done exceptional work on documenting the inevitability of a reduction in economic wellbeing if our debt to GDP ratio passes certain benchmarks, which we are quickly closing in on. A large number of other studies from universities, the Congressional Budget Office, the International Monetary Fund, and other organizations worldwide show us that the conclusion is clear: rising debt will hold back strong economic growth down the road. This occurs as rising debt pushes up interest rates, "crowding out" private investment.

Equally important is the fact that it is a distinct likelihood that the financial markets themselves will at some point, sooner rather than later, look at our massive accumulation of debt and conclude that we will be unable to pay it back. The markets will react to this by assuming that the currency will have to be devalued through inflation and the cost of servicing our nation's debt will jump radically. This will significantly compound what will be a dire fiscal situation.

Debt reduction done right can actually strengthen the economy down the road. A recent analysis from the Congressional Budget Office found that a $2 trillion reduction in primary deficits could boost the size of GNP by nearly 1% over ten years. And in the short-term, there is evidence that just the announcement of a long-term deficit reduction plan could bolster the recovery by improving confidence and certainty about United States fiscal policy.

What amount of deficit reduction is needed

The "deal" that can avoid this crisis is apparent and very doable.

The goal of deficit reduction must be to put the debt on a clear downward path as a share of the economy, this decade and over the long-term. Achieving that goal will require reducing the debt to below 70% of the size of the economy by 2023.

The good news is that the President and Congress has tried over the last several years to grapple with how to come to terms with our debt problems and have accomplished a hard $2.5+ trillion dollars of debt reduction out of the total needed. The Budget Control Act

of 2011 cut $917 billion dollars in mostly discretionary spending, prior continuing resolutions enacted hundreds of billions in discretionary spending savings over ten years, and the fiscal cliff agreement, formally known as the American Taxpayer Relief Act, generated over $600 billion dollars in new revenues. These were serious steps down the road of putting our fiscal house in order, but we are not there yet.

In the wake of these efforts, getting control over our debt will require additional deficit reduction.

Our fiscal problems will self-correct if our government reduces our deficits and debt over the next ten years by at least an additional $2.4 trillion dollars in reforms, reforms that should also increase in their effectiveness beyond this ten-year window. In total, this would produce over $5 trillion in savings when including the policies we have already put in place. This represents the minimum amount of savings needed to put the debt on a downward path as a share of the economy to below 70%.

Ideally, lawmakers would aim for an even larger amount of savings. In today's terms, the President's own National Commission on Fiscal Responsibility and Reform would produce a total of between $6.5 and $7 trillion in savings over ten years – an even more aggressive target.

Some observers have said we only need an additional $1.5 trillion in savings over the next ten years in order to stabilize the debt as a share of the economy. While it is true that $1.5 trillion would likely stabilize our debt this decade, it would likely be insufficient to control the debt over the long-term, leaving the country open to serious risks, including:

- **No Room for Error** for future deficit-increasing policies or if economic projections are too rosy;
- **No Long-Term Stability** in the face of rising health care and retirement costs that become harder to contain later this decade and beyond, requiring a "running start" to control the debt and interest payments later on;
- **Slower Economic Growth** due to higher interest rates "crowding out" investment; and
- **No Fiscal Flexibility** in the case of natural disasters, security needs, or an economic downturn.

Putting debt on a downward path with another $2.4 trillion in new deficit reduction would address the risks. This may seem like a great deal of money, but when one considers that it is off a base of approximately $40 trillion dollars of spending over the next ten years, it is definitely manageable.

What policies can Congress pursue to reduce the debt and encourage economic growth

Most of the changes that are needed now, unlike the practical effect of continuing to reduce spending through the sequester, are changes to entitlement programs and tax

policy which can and should compound in their effectiveness as we move beyond this initial ten year window.

What is the deal we need? It should obviously start by an agreement to replace the sequester with targeted and effective changes to federal fiscal policy that gets a reduction in the deficit over the next ten years of at least $2.4 trillion dollars and that can be presumed to do significantly more than that in the following decades. It should be an agreement that at a minimum has a goal of stabilizing our debt to GDP ratio at 70 percent or less. Why wait for another fiscal speed bump to address these issues?

The President proposed a specific change, which would be a significant contributor to this type of responsible action, when he proposed changing the manner in which the Federal cost of living adjustment (COLA) is calculated to make it more accurate.

In their latest framework, Sen. Simpson and Erskine Bowles have put forward $600 billion as a credible and bipartisan target for health savings over ten years, which could be achieved through various options, including many outlined by the Committee for a Responsible Federal Budget, which I have attached to my testimony. It is a specific and doable list. Much of it is directed at making Medicare and Medicaid better programs by focusing on outcomes and value rather than utilization and repetition.

Of course, there is also the proposal for approximately $200 to $300 billion in entitlement savings that was reportedly agreed to between the President and the Speaker in the summer of 2011 and which was further discussed during the fiscal cliff negotiations. These are presumably well-vetted ideas that are essentially off the shelf ready for a "deal."

Take any permutation of these proposals and add in the CPI change proposed by the President, known as “chained CPI” and throw in a long-term adjustment in the eligibility age for Medicare and Social Security (which reflects the large increase in life expectancy that we have seen and will continue to see) and you have the spending side of a very strong package.

Comprehensive tax reform is also necessary. Although a significant majority of the reduction in our deficit must come from the spending side of the ledger, reforming the tax code to lower rates and broaden the tax base will be good both for economy and our fiscal health. Ironically, Senator Coats, the lead Senate Republican of this Committee has, along with Senator Wyden, proposed such an approach and it would be a good guide to developing a bipartisan, strong bill to fundamentally improve and reform our tax policy as a nation making us more competitive.

There are at least two other crucial points that the "deal" must include. First, it must be based off an agreement that fixes the size of the government as a percent of GDP. The federal government since the end of World War II through 2007 has been approximately 19.8 percent of GDP. In the last few years it has grown to over 23.5 percent and is still headed up. Some of this growth is inevitable due to the retirement of the baby boom

generation, which is doubling the number of retirees in our society. Agreeing to fix the size of the government to a percent of the GDP that is closer to its historical range is essential to driving long-term solutions to our debt problem. The National Committee on Fiscal Responsibility and Reform used the metric of 21.3 percent, which is realistic in light of the demographic shift. This metric also sets an appropriate relationship between spending restraint and revenues of about three to one in the out years.

Secondly, all entitlement changes that reduce projected spending need to be locked in with a procedural provision that keeps later Congresses from arbitrarily rescinding them. This can be done by making attempts to reverse such changes subject to a 67 vote point of order in the Senate.

The opportunity for the "deal" is sitting there. It is not rocket science or, for that matter, even model rocket science. It is very doable and all the policy options are well debated, vetted, and known. It should be simply done so that a predictable fiscal crisis can be muted and our nation can move on as a better and stronger place for ourselves and our children.

Attachment of Sen. Judd Gregg
Health Savings Options
Source: The Committee for a Responsible Federal Budget
http://crfb.org/document/report-health-care-and-revenue-savings-options

Health Care Savings Options	Potential 2013-2022 Savings
Expand Current Income-Related Premiums	**$10 - $70 billion**
Freeze Income-Related Thresholds for Part B and Part D	$10 billion
Increase Income-Related Premiums by 15%	$25 billion
Reduce Threshold for 35% Premium from $85,000 to $50,000	$25 billion
Impose Part A Premium on Higher Earners Making Above $250,000	$10 billion
Increase Premium Base Rates	**$75 - $330 billion**
Increase Medicare Part B Base Rate to 35 Percent of Program Costs	$250 billion
Increase Medicare Part D Base Rate to 35 Percent of Program Costs	$80 billion
Increase Premiums by 5 Points Across-the-Board (incl. means-tested)	$190 billion
Increase New Beneficiary Premiums by 5 Points Across-the-Board	$75 billion
Modify Existing Cost-Sharing for Current and/or Future Beneficiaries	**$10 - $100 billion**
Increase Part B Deductible by $75 (for 2012 it is $140) by 2020	$10 billion
Impose a 10% Home Health Copayment	$40 billion
Impose Cost-Sharing for Skilled Nursing Facilities	$20 billion
Impose Copayments for Clinical Laboratories	$25 billion
Overhaul Medicare Cost-Sharing System	**$30 - $65 billion**
Establish Unified Deductible of $550, 20% Uniform Coinsurance, and $5,500 Out of Pocket Limit	$30 billion
Impose a 5% Coinsurance Above the Initial Out-of-Pocket Limit	$25 billion
Give IPAB authority to Adjust Coinsurance rates	n/a
Combine Cost-Sharing Overhaul with Medigap Restrictions	$10 billion
Restrict Medigap Coverage	**$10 - $100 billion**
Ban Medigap Plans from Covering First-Dollar Costs (first $550) and Limit Coverage to 50% of Remaining Cost-Sharing	$55 billion
Apply Above Medigap Restrictions to TRICARE for Life	$35 billion
Apply Above Medigap Restrictions to Employer Plans	Unknown
Replace FEHBP Wraparound Coverage for Medicare with Premium Subsidy	$10 billion
Impose 15% Premium Surcharge for Certain Medigap Plans	$15 billion
Levy 5% Surtax on all Medigap Plans	$15 billion
Increase Medicare Age	**Up to $150 billion**
Increase Medicare Age by 2 Months Per Year Until It Reaches 67	$150 billion
Increase Medicare Age by 1 Month Per Year Until It Reaches 67	$75 billion
Establish Medicare Buy-in at Age 65 or Age 62	-$1 billion
Once Medicare Age Reaches 67, Index to Longevity	Future Savings
Make Changes to Medicare Advantage	**Up to $30 billion**
Recover Erroneous Payments Made to Medicare Advantage	$2 billion
Repeal Quality Bonus Demonstration	$6 billion
Accelerate Phase-in of All Benchmarks and Coding Intensity Adjustments	$10 billion
Prohibit Medicare Advantage Plans from Exceeding 110% of FFS Costs	$10 billion
Adjust Timing of Medicare Advantage Payments	$2 billion
Reform Graduate Medical Education Payments	**$5 - $70 billion**
Consolidate GME and IME Payments Into a Grant and Grow at CPI-1%	$70 billion
Limit GME Payments to National Average Salary and Reduce IME	$55 billion

Health Care Savings Options	Potential 2013-2022 Savings
Payments Adjustments from 5.5 to 2.2 Percent	
Enact More Modest Adjustments to GME and IME	$5 to $20 billion
Require Private Insurers Pay $2 per Enrollee by 2014 to Contribute to GME	$4 billion
Reduce Payments for Bad Debts	**$23 - $35 billion**
Reduce Bad Debts Reimbursements from 65% to 25% of Costs	$23 billion
Phase Out Bad Debts Payments	$35 billion
Reform Rural Hospital Payments	**Up to $30 billion**
Cut All Special Payments to Rural Hospitals in Half	$30 billion
Reduce Payments to Critical Access Hospitals (CAH) from 101% to 100% of Reasonable Costs	$1 billion
Prohibit CAH Designation for Facilities within 10 Miles of a Hospital	$1 billion
Reform Post-Acute Care Payments	**Up to $55 billion**
Reduce Skilled Nursing Facility (SNF) Payment Updates by About 1.1%	$12 billion
Reduce Skilled Nursing Home Health Payment Updates by About 1.1%	$25 billion
Equalize Certain Payments to SNFs and Inpatient Rehabilitation Facilities	$1 billion
Reduce Readmissions to Skilled Nursing Facilities	$2 billion
Institute Value Based Purchasing for Home Health and SNFs	$4 billion
Reduce IRF and Long Term Care Hospital Payment Updates by 1.1%	$8 billion
Return to the 75% Rule for IRFs	$1 billion
Institute Premium Support/Defined Support/Competitive Bidding	**Dialable**
Switch Medicare to a Premium Support/Defined Support/Competitive Bidding Plan Without a Cap *(Savings Depend on Subsidy Benchmark)*	Unknown
Switch Medicare to a Premium Support/Defined Support/Competitive Bidding Plan w/ a Cap on Subsidy Growth Rate	Dialable
Switch Federal Employees Health Benefits Program to a Premium Support System with a Cap	$10 - $40 billion
Reform or Replace Sustainable Growth Rate *(Estimates Relative to a 10-year Freeze of Physician Payments)*	**Dialable**
Index Physician Payments to Medicare Economic Index	-$90 billion
Reset SGR Target at 2011 Spending Levels	$15 billion
Reduce Payments by 1% in 2014, Require CMS to Develop New Payment Formula Enforced w/ Rebased SGR in 2015 (Fiscal Commission Recommendation)	$35 billion
Freeze Payment Rates for Primary Care Physicians and Reduce Other Rates by 16.5 Percent (MedPAC Recommendation)	$80 billion
Enact Medical Malpractice Reform	**Up to $70 billion**
Implement 3-Year Statute of Limitations, a Fair-Share Rule, Collateral Source Rules, and Limits on Lawyer Contingency Fees	$15 billion
Impose Caps on Noneconomic Damages (at $250,000) and Punitive Damages (at the greater of $250k or twice the economic damages)	$50 billion
Institute Evidence-Based Practice Guidelines and Safe Harbor Protections	$5 billion
Reform the Medicaid Payment Formula	**Dialable**
Establish Per Capita Cap on Medicaid Growth	Dialable
Block Grant Medicaid and Set a Fixed Growth Rate	Dialable
Allow up to 10 States to Submit Medicaid Waivers to CMS, under an Expedited Waiver Approval Process	Unknown
Reduce Federal Medical Assistance Perentage (FMAP) Rates Across-the-Board	Dialable
Move to a “Blended Rate” for Medicaid and CHIP	Dialable
Reduce Floor on FMAP Matching Rates	Dialable (~$300b max)

Health Care Savings Options	Potential 2013-2022 Savings
Enact Targeted Medicaid Changes	**Up to $100 billion**
Reduce Medicaid Provider Tax Threshold	$10 - $65 billion
Reduce Duplicative Administrative Payments to States	$3 billion
Equalize Federal Matching Rates for Administrative Function At 50%	$25 billion
Allow States to Increase Medicaid Cost-Sharing	Unknown
Reduce Medicaid DME Payments to Medicare Levels	$3 billion
Rebase Medicaid Disproportionate Share Hospital (DSH) Payments for FY2022 and on Permanent Basis	$4 billion
Require Drug Rebates in Medicare	**$50 to $135**
Require Rebates for Brand Name Drugs for Dual Eligibles	$75 billion
Require Rebates for Brand Name Drugs for Other Low Income Subsidy (LIS) Beneficiaries	$45 billion
Require Rebates for Generic Drugs For Dual and LIS Beneficiaries	$25 billion
Reduce Federal Spending on Prescription Drugs	**Up to $85B**
Prohibit “Pay for Delay” Agreements	$5 billion
Encourage Faster Introduction of “Biosimilar” Drugs from 12 to 7 Years	$3 billion
Reduce Part B Drug Payments from Average Sales Price (ASP)+6% to ASP+3%	$3 billion
Establish Rebate for Part B Drugs Administered in Physicians’ Office	$15 billion
Adjust Medicaid Inflation Rebate	$20 billion
Allow Drug Re-importation	$20 billion
Change Cost-Sharing in Medicare Part D LIS to Encourage Use of Generics	$20 billion
Reduce/Reform Select PPACA Provisions	**Dialable**
Repeal Frontier State Adjustments	$2 billion
Exclude Part D 50% Discount from Out-of-Pocket (OOP) Cost Calculation	$85 billion
Eliminate Cap on Subsidy Recapture	$45 billion
Repeal Prevention and Public Health Fund	$10 billion
Repeal Individual Mandate	$335 billion
Institute a Public Option	$100 billion
Require Health Insurance Exchanges to Offer Tiered Insurance Plans	$10 billion
Reduce PPACA Subsidies	Dialable
Enact Payment Reforms	**Up to $95 billion**
Aggressively Expand Penalties for Avoidable Complications	Up to $23 billion
Aggressively Expand Penalties for Avoidable Hospital Readmissions	Up to $29 billion
Expand Competitive Bidding to All Durable Medical Equipment	$10 billion
Expand Competitive Bidding to Medical Devices and Lab Services	$25 billion
Expand Payment Bundling and Other Pilot Programs	$10 billion
Other Provider Payment Reductions	**Up to $45 billion**
Recoup Hospital Coding Intensity Adjustments	$3 billion
Pay Hospital Outpatient Evaluation and Management (E&M) Visits at Physician Fee Schedule Rate	$10 to $20 billion
Modify Payments and Require Prior Authorization for Advanced Imaging	$2 billion
Reduce Payments to Clinical Labs by 5%	$5 billion
Reduce Cap on Rental for Oxygen Concentrators from 36 to 13 Months	$10 billion
Reduce Medicare Payments to End-Stage Renal Disease Facilities	$4 billion