REMARKS OF AFL-CIO PRESIDENT RICHARD L. TRUMKA
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ON FISCAL RESPONSIBILITY AND REFORM
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Mr. Chairman and Members of the Commission, I know my time is short, so I will limit my testimony to eight key points:

**First, stabilizing the national debt is a means to an end, not an end in itself.**

The goal of our national economic policy should be sustainable, broadly shared prosperity. To achieve that goal, there is no question that we need to stabilize the national debt as a share of our economy over the long term. But stabilizing the debt is simply a means to achieve our goal of sustainable, broadly shared prosperity, and we should reject approaches to debt stabilization that take us away from that goal.

Which approaches would help us achieve sustainable, broadly shared prosperity? I can think of a few: providing the economic stimulus necessary to erase our 10.4 million jobs deficit and avoid a double dip recession; investing in the 21st century infrastructure necessary to support stronger economic growth in the long term; further reducing excess health care cost growth; asking Wall Street and the small minority of Americans who benefited most from the economic policies of the past 30 years to pay their fair share for rebuilding the economy; and avoiding austerity measures that increase economic inequality, which played a key role in precipitating the current economic crisis.

**Second, let's be honest about what the problem is.**

We need to be clear that President Obama is not to blame for getting us into this mess. Two weeks before he took office, the Congressional Budget Office (CBO) projected a budget deficit of $1.4 trillion for 2009—and annual deficits averaging well over $1 trillion for the coming decade.[1]

We should be honest about what's causing deficits over the next ten years. According to the Center on Budget and Policy Priorities, "The tax cuts enacted under President George W. Bush, the wars in Afghanistan and Iraq, and the economic downturn together explain virtually the entire deficit over the next ten years." And "without the economic downturn and the fiscal policies of the previous administration, the budget would be roughly in balance over the next decade."[2]

Although more than half of the 2009 deficit is due to the recession,[3] Council of Economic Advisers Chair Christina Romer points out that "in the absence of [Bush administration policies that we failed to pay for], we could have had an economic downturn as severe as

[1] http://www.cbo.gov/ftpdocs/99xx/doc9957/01-07-Outlook.pdf
[2] http://www.cbpp.org/files/12-16-09bud.pdf, p. 1.
[3] http://epi.3cdn.net/396ffab9a9598406c3_5lm6bh2cu.pdf, p.5.

the current one and responded to it as aggressively as we have, all while keeping the budget roughly balanced over the next ten years [2010-2019]."[4]

We should also be honest about what's causing projected deficits over the long term. We do not face a crisis of entitlement spending generally, caused by the retirement of the Baby Boomers. In the long term, we face a crisis of public and private health care costs growing faster than GDP, especially after 2035. Social Security has its own source of dedicated funding and is not responsible for our unsustainable long-term debt, and spending on other entitlements is projected to fall as a share of the economy over the long term.

**Third, premature withdrawal of economic stimulus threatens to throw the global economy into a double dip recession, or worse.**

Already we can see how exaggerated fears and misinformation about deficits are leading to premature withdrawal of the economic stimulus that so far has prevented another Great Depression.

The Recovery Act was necessary because of a massive shortfall of aggregate demand, which resulted from high levels of unemployment and the loss of $12 trillion in wealth from the collapse of the real estate and stock market bubbles.

The Recovery Act did exactly what it was supposed to do. It increased the number of people employed by up to 2.8 million in the first quarter of 2010, increased the number of full-time jobs by up to 4.1 million, and increased real GDP by up to 4.2%.[5] But it wasn't big enough to make up for the massive shortfall of aggregate demand.[6]

Without a significant reduction in the trade deficit, only economic stimulus in the form of deficit spending can make up for the remaining shortfall of aggregate demand until private sector demand regains its footing.

But instead, we are heading in the opposite direction. We are prematurely withdrawing economic stimulus, allowing the Recovery Act to phase out and standing by passively as state and local governments plan budget cuts that will cost us 900,000 jobs.[7]

Last month's jobs report sends a strong signal that private sector job growth remains exceedingly weak and may fall further as the stimulus provided by the Recovery Act tapers off this year.

By withdrawing economic stimulus, we run the risk not only of prolonging the jobs crisis for several more years, but also of bringing about a "double dip" recession—or even what Nobel Laureate Paul Krugman calls "a third Depression."[8]

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[4] http://www.americanprogress.org/events/2009/10/av/romer_remarks.pdf, p.2.
[5] http://www.cbo.gov/ftpdocs/115xx/doc11525/05-25-ARRA.pdf
[6] *See* http://www.whitehouse.gov/sites/default/files/rss_viewer/back_to_a_better_normal.pdf, pp. 2-3, 6-8.
[7] http://www.cbpp.org/files/11-11-09stim.pdf

This is a monumental blunder of global economic policy that bears an uncomfortable similarity to mistakes made by the U.S. in 1937, when premature fiscal contraction deepened and prolonged the Great Depression, and by Japan in the 1990s, when premature fiscal contraction led to a lost decade of economic stagnation.

There is no good economic policy reason that requires fiscal contraction at this time—neither concerns about inflation (which is practically non-existent), nor about long-term interest rates (which are extremely low by historical standards), nor about the crowding out of private investment (because so much labor and capital is unemployed), nor about the long-term debt (on which short-term stimulus has a small impact).

In other words, we can do something about the jobs crisis if we choose to. But we do have to choose—between providing more stimulus, on the one hand; or causing more joblessness, more wage cuts, more poverty, more inequality, more foreclosures, more waste of human potential, and more suffering, on the other.

**Fourth, stronger economic growth, job growth, and wage growth are needed to stabilize the debt.**

Just as the economic crisis itself bears much of the blame for projected deficits over the next ten years, a double dip recession—or several more years of meager job growth—would have a similarly harmful impact on future deficits.

According to Paul Krugman, "Both textbook economics and experience say that slashing spending when you're still suffering from high unemployment is a really bad idea. Not only does it deepen the slump, but it does little to improve the budget outlook, because much of what governments save by spending less they lose as a weaker economy depresses tax receipts."[9]

To a great extent, the size of the deficit depends on employment and growth. When employment and growth are weak, tax revenues are low and social assistance expenditures are high. When employment and growth are strong, the reverse is true.

Moreover, as Christina Romer has pointed out, failure to bring down unemployment quickly enough in the short term can result in permanently higher rates of unemployment, which would reduce federal tax revenues and increase federal expenditures.[10] In other words, failure to provide additional stimulus in the short term threatens our fiscal sustainability in the medium and long term.

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[8] http://www.nytimes.com/2010/06/28/opinion/28krugman.html?ref=opinion/
[9] http://www.nytimes.com/2010/05/31/opinion/31krugman.html
[10] http://www.whitehouse.gov/sites/default/files/rss_viewer/back_to_a_better_normal.pdf, p. 11.

These are some of the reasons why President Obama said last weekend that "our fiscal health tomorrow will rest in no small measure on our ability to create jobs and growth today."[11]

And these are some of the reasons why Larry Summers said recently that "spurring growth, if we can achieve it, is by far the best way to improve our fiscal position" because "it is not possible to imagine sound budgets in the absence of economic growth and solid economic performance"; and therefore "it would be penny-wise and pound-foolish not to take advantage of our capacity to encourage near-term job creation."[12]

Strong economic growth is equally important in the long term. Long-term deficit projections are based on assumptions about U.S. economic growth. If we achieve higher than expected growth, then projected deficits will not loom quite so large and stabilizing the debt will be a less daunting challenge.

In short, we must have a job-centered approach to stabilizing the national debt, which would bring us closer to our goal of sustainable, broadly shared prosperity.

**Fifth, Wall Street should pay to build a 21st century infrastructure that will lead to long-term economic growth.**

To achieve higher levels of economic growth, we have no choice but to abandon the failed economic policies of the past.

For decades the U.S. has pursued an economic growth strategy based on low wages and debt-fueled consumption that was financed by asset bubbles (first stocks, then real estate). We no longer have the option of perpetuating this obsolete strategy, whose failures have been exposed by the economic crisis.

We must identify new sources of economic growth for the future. One thing economists can agree on is that a modern, well-developed infrastructure is key to productivity growth in the private sector, to U.S. competitiveness in the global economy, and therefore to long-term economic growth.

Yet today we face a $2.2 trillion deficit in 20th century infrastructure that is crumbling and in disrepair,[13] and a broad array of 21st century infrastructure—especially in transportation, communications, and clean energy—that is waiting to be built. Failure to invest in rebuilding our infrastructure for the 21st century will result in lower rates of economic growth—and therefore lower tax revenues.

*Washington Post* columnist Steven Pearlstein agrees that this is the ideal time to "invest heavily in public infrastructure that has been badly neglected over the past 30 years. I'm

[11] http://www.whitehouse.gov/the-press-office/remarks-president-obama-g-20-press-conference-toronto-canada
[12] http://www.whitehouse.gov/administration/eop/nec/speeches/fiscal-policy-economic-strategy.
[13] http://www.infrastructurereportcard.org/

referring not only to roads and bridges but also to airports and air traffic control systems, urban transit, high-speed rail, schools and university facilities, national laboratories, national parks, 'smart' electric grids, broadband networks, green generating plants, and health information networks. Properly chosen, these projects can have huge long-run economic payoffs while tangibly improving the lives of all Americans. They're the kind of government spending today's voters can get excited about while also leaving a valuable legacy for future generations -- along with the debt that was used to finance them. And if they wind up creating some jobs at a time when millions of people are unemployed, so much the better…It's time to settle up and get on with the more exciting challenge of shaping our long-term economic future."[14]

Of course, rebuilding our infrastructure for the 21st century will require higher levels of public investment. The example of the postwar boom—when an economic strategy of broadly shared prosperity with strong unions and shrinking inequality paid off enormous dividends—shows us the way forward. High levels of public investment fueled robust GDP and job growth in the postwar period that reduced the debt-to-GDP ratio from over 100% after the war to less than 30% in the 1970s.[15]

After the jobs crisis is behind us and economic stimulus is no longer needed, higher levels of public investment in infrastructure will need to be paid for. This will require new sources of federal tax revenue. Federal revenues are now at their lowest share of GDP (14.4%) since 1950,[16] and effective tax rates applicable to high-income taxpayers (earning over $250,000 in 2009 dollars) reached their lowest level in at least half a century in 2008.[17]

The question we now have to answer is who should pay for the urgent task of rebuilding our economy for the 21st century—the small minority of Americans who benefited from the economic policies of the past 30 years, or the vast majority of Americans who have seen little reward for their hard work.

We believe it is only fitting to ask Wall Street to pay to rebuild the economy it helped destroy. One way to do that would be through a Financial Speculation Tax (FST)—a tiny 0.05% tax on transactions of stocks, options, futures, credit default swaps, and other derivative instruments. The $100 to $300 billion in additional tax revenue *per year*[18] that this tax would generate could be used to fund higher levels of public investment, and the tax itself would curb unproductive speculation that is harmful to the economy.

It would also be fitting to ask the wealthiest Americans who benefited most from the failed economic policies of the past 30 years to pay their fair share for rebuilding the 21st

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[14] http://www.washingtonpost.com/wp-dyn/content/article/2010/06/10/AR2010061004971.html
[15] http://www.gpoaccess.gov/usbudget/fy11/sheets/hist07z1.xls
[16] http://www.gpoaccess.gov/usbudget/fy11/pdf/budget.pdf
[17] http://www.whitehouse.gov/sites/default/files/microsites/economic-report-president.pdf, p. 154.
[18] *See* H.R. 4191, which would impose a tax of 2 to 25 basis points on certain financial transactions, with large exemptions. A broad global coalition of labor unions is supporting a tax of 5 basis points on a broader range of financial transactions, which has been estimated to generate revenue equal to 1% to 2% of global GDP ($100 to $300 billion in the U.S.). *See* http://www.steuer-gegen-armut.org/fileadmin/Bildgalerie/Kampagnen-Seite/Unterstuetzung_Wissenschaft/Schulmeister_EU_und_IWF.pdf

century economy and stabilizing the national debt. For example, a surtax of 1%-5.4% on earnings over $350,000 would raise close to $600 billion over 10 years.[19] Other proposals to make the tax code more progressive enjoy broad public support.

**Sixth, efforts to stabilize the national debt should not increase income inequality.**

The alarming growth of economic inequality was a contributing factor to the economic crisis. Faced with stagnating wages, many workers responded by incurring more and more personal debt, often based on their home equity. At the same time, the shift of income to top earners contributed to excessive speculation and asset bubbles.

While a jobs-centered approach to debt stabilization would help reverse income inequality and bring us closer to sustainable, broadly shared prosperity, several approaches now under discussion in the debate over deficit reduction would take us in the opposite direction.

These approaches include prolonged unemployment, which would permanently cripple the earnings potential of millions of workers, exert downward pressure on workers' wages, and condemn millions of children to poverty unnecessarily; cuts to Social Security benefits; and cuts to Medicare benefits.

**Seventh, we must reduce health care costs even further—without cutting benefits or compromising the quality of care.**

Before health reform was enacted, it was widely recognized that long-term deficits were driven by health care cost growth in excess of GDP growth. The economist Henry J. Aaron wrote, "over the next four decades, growth of health care expenditures accounts for more than all" of the increase in [CBO's] projected long-term deficits."[20]

According to Christina Romer, "Some of this is the result of the aging of the population. But the far greater source is the fact that health care costs, both public and private, are rising much faster than GDP."[21]

Health reform is expected to reduce excess health care cost growth, but not eliminate it entirely. Additional reforms will be necessary.

Reducing excess cost growth can and should be accomplished without cutting benefits. Approaches that should be considered include (1) Medicare drug price negotiation; (2) easing restrictions on imports of prescription drugs; (3) expanding proven Medicare payment and delivery reforms; and (4) offering the choice of a public health insurance plan option that would offer premiums 10% below private insurance[22] and would reportedly reduce the federal deficit by $110 billion over 10 years.

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[19] http://www.cbo.gov/ftpdocs/104xx/doc10464/hr3200.pdf
[20] Henry J. Aaron, "How to Think About the U.S. Budget Challenge" (April 2010).
[21] http://www.americanprogress.org/events/2009/10/av/romer_remarks.pdf, p.3.
[22] http://www.cbo.gov/ftpdocs/104xx/doc10430/House_Tri-Committee-Rangel.pdf, p.5

So we face a choice between reducing health care cost growth in ways that cut benefits for working people and compromise the quality of their care; or in ways that challenge the pharmaceutical companies, the insurance companies, and other powerful economic interests. Only the latter approach is consistent with sustainable, broadly shared prosperity.

**Eighth, Social Security benefits are not the problem and must not be cut.**

Social Security has its own dedicated source of funding and is not responsible for our long-term debt problem. The Social Security trust fund is projected to grow from $2.5 trillion in 2009 to $3.8 trillion in 2020, and its surpluses are invested in government bonds that have to be repaid just like any other government bonds. Social Security has no borrowing authority and cannot pay benefits if its trust funds are empty.

Creating the false impression that Social Security is a principal contributor to the growth of budget deficits, or lumping Social Security together with Medicare as part of a general "entitlements crisis"—is a sleight-of-hand designed to build public support for the unpopular Wall Street agenda of cutting Social Security benefits and/or privatizing the program. We cannot allow deficit reduction to be used as an excuse for either.

It is especially inappropriate to cut benefits for near retirees who have suffered the most from the recent loss of their retirement savings in the collapse of the stock market and real estate bubbles.

In fact, Social Security should be strengthened to compensate for the decline of traditional pensions and for the stock market losses of retirement savings plans. Social Security benefits are about one third lower than the average of 30 OECD countries.

We need to remember that Social Security functions as a powerful counter-cyclical stabilizer during recessions. Every month, millions of Social Security checks are quickly cashed to pay for goods and services, flowing through communities and fueling the economy.

The modest 75-year shortfall in Social Security's finances can be easily addressed and does not require benefit cuts (such as reducing adjustments for inflation or reducing starting benefits) or raising the retirement age. One proposal to bolster Social Security's finances that would be consistent with sustainable, broadly shared prosperity is raising the cap on taxable wages to 90% of earnings, or lifting the cap altogether.

**Conclusion**

In the short term, we have a jobs crisis—not a debt crisis. The best way to improve our fiscal situation is through stronger job growth. However, given the massive shortfall of aggregate demand, additional deficit spending is necessary in the short term to bring

down unemployment and avert a double dip recession, which would only make deficits worse.

After the jobs crisis is behind us, we will need more tax revenues to pay for the higher levels of public investment in 21st century infrastructure that are necessary to create good jobs, ensure long-term economic growth, and improve our global competitiveness. Additional health reforms will also be necessary to further reduce excess health care cost growth.

Stabilizing the national debt over the long term can be a means of achieving sustainable, broadly shared prosperity. But exaggerated fears of deficits and the debt should not be used as a pretext to increase inequality and thereby repeat the mistakes of the past that brought us to the precipice of global depression.