

Originally Processed With FOIA(s):

FOIA Number:

S

FOIA MARKER

This is not a textual record. This is used as an administrative marker by the George Bush Presidential Library Staff.

Record Group/Collection: George H.W. Bush Presidential Records
Collection/Office of Origin: Speechwriting, White House Office of
Series: Snow, Tony, Files
Subseries: Subject File, 1988-1993

OA/ID Number: 13894
Folder ID Number: 13894-003

Folder Title:
[Economy-Foreign/Domestic, 1989-1990]

Stack:	Row:	Section:	Shelf:	Position:
G	18	29	2	2



Memo From the Public Affairs Council

March 27, 1989

To: Clark Ervin
From: Ray Hoewing
President, Public Affairs Council

Notes

The Presidents's speech should:

- Challenge business - make CEO'S uncomfortable (that is, have a hard "edge" -- a not "smoke-and-mirrors" tone).
- Confront the undeniable -- business commitment to its communities has lagged in recent years for understandable, but no longer sufficient, reasons (competitive pressures, etc.).
- Seek business involvement not because it is in the public interest (though that too) but mainly because it is in business' self-interest.
- Make clear the Bush program will go beyond publicity, awards, "P.R."
- Suggest that the emphasis will not only be to stimulate more business involvement but to provide models/yardsticks/case studies of effective involvement.
- Note that -- despite many instances of laudable business activity -- many business firms have yet to become engaged.


Some other suggestions/pointers/speech lines:

- Short-run profitability cannot be the only criterion for business in a society where cities are rampant with drugs, a public school system often fails to educate and hundreds of thousands are homeless.
- The speech must go beyond exhortation. (For example: "Next month I will be assembling a group of chief executive officers ..." "Because this Administration is giving top priority to winning

the war against drugs and in restoring our public education system to its previous standards of excellence, I have appointed two task forces of business people to spearhead business efforts to address these critical issues").

- ° Business must apply hard-headed business principles to its social involvement -- for example, researching needs, establishing objectives, measuring results. Mere "activity", no matter how well intentioned, is not sufficient.
- ° Business must become more actively and intelligently involved, not because we wish it would, but because it will not survive as viable, profitable enterprises over the long haul in a society that is failing.
- ° We must learn what business is doing that is truly making a difference and then find ways to help replicate widely.
- ° A few examples of business efforts which have made a difference (and which have been clearly documented) should be considered for mentioning.

Perceptions and realities to keep in mind:

- ° Remember that most serious and knowledgeable people in business (at both CEO and "program manager" level) view Reagan PSI as essentially a public relations effort doing little harm but also not much good.
 - ° Therefore, the President should convey that the program he is undertaking will be qualitatively and substantively different than Reagan PSI efforts.
 - ° A real risk or danger: leaving the impression that the President views private sector programs as the way to "off load" the responsibilities for social programs (thus replaying the near-fatal impressions created by Reagan's people in 1981-82).
 - ° One key word is "partnership" (but speak to this point: many business people have concluded that government means by partnership, "Business, you put up the money. Government will define and control the agenda and the program.").
 - ° Beware of excessive poor mouthing. While business supports fiscal integrity, it wants to know that the Federal Government is not some pitiable, penniless giant but rather is committed to finding/diverting additional government resources when they are indisputably required.
- 

- ° CEOs, particularly, will be looking for evidence that the President understands and accepts that in a democracy government is accountable for social progress and business cannot and must not pre-empt decision-making which properly belongs to political leadership.
- ° Acknowledge in no uncertain terms that under the most optimistic scenario about social problems the public sector is by far and away the "heavy" compared to the private sector (excellent summary statistics and exposition of this point have come recently from Brian O'Connell of Independent Sector).

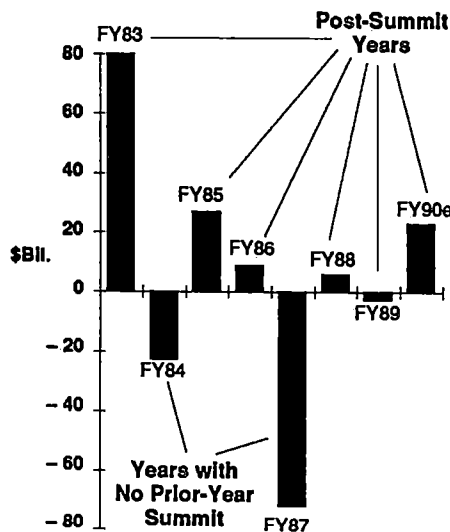
Tax Features

New Paper Traces History of Budget Summits in the '80s

Pattern of Deficit Reduction Shows Negotiations Ineffective

A new Tax Foundation analysis of budget summits during the 1980s entitled *A Decade of Budget Summitry* leaves little room for opti-

Change in Deficit: Post-Summit Years vs. Years with No Prior-Year Summit



^e First six months comparison of FY1989 and FY1990. Source: Tax Foundation.

mism that the current talks between the President and Congress will lead to deficit reduction. It points out that the FY1991 budget summit is the fifth time in nine years the White House and Congress have conducted special negotiations for this purpose, but the budget deficit has averaged well over \$160 billion each year during this period.

In the first six months of the current fiscal year, the deficit exceeded \$150 billion in spite of a full-year target of \$100 billion. In light of these results, summits convened to lower deficits may have done more harm than good.

See *Budget Summit* on page 5

Budget Process Reform: Two Views

Start from Scratch with a Legislative Overhaul



Cong. Christopher Cox (R-CA)

The nation's budget process has broken down to the point that most Americans, if they understood it, would regard it as a national joke. But it is no laughing matter.

As a freshman congressman, I was struck right away by the utter incomprehensibility of the budget process. Virtually no member of Congress — let alone the public — even reads the huge spending bills we adopt. Moreover, the typical year-end, catch-all spending bill is too long, too complex, and too tardy to expect the President even to read it before he must sign it into law.

On my first day in Congress, then Speaker



Congressman Marty Russo (D-IL)

Honesty Is the Best Budget Policy

When I talk about the budget process, I do so as a member of the Budget Committee who cannot wait to finish serving his last year on it. The budget process is so flawed that it has become a fraud. It is a sham, and one of the most important reasons we have the fiscal woes we do today is that the Budget Committee, along with the Administration and the rest of Congress, has been sliding by the problems for the last nine years.

I hope that as a result of the current budget summit, if nothing else is done, the summitters will be honest about the problem and honest about the solution. I for one do not

See *Russo* on page 2, col. 3



Tax Foundation

IN THIS ISSUE

New Analysis of Budget Summits	1
"Front Burner"	1
Tax & Budget Conference	3
President's Message	5
Pittsburgh & Washington Briefings on Budget Issues	6
New Research Fellow	6

Cox from page 1

Jim Wright declared that he was going to violate the law. This may shock most Americans, but in fact it is routine business in Washington. You see, Speaker Wright promised to pass all of that year's spending bills by August. In fact the law requires final action on these bills by June 15th.

Ordinarily it might seem brazen for a newly elected congressman to attempt to refashion what the system has been producing for a long time. But the frustration with the way the budget process has disintegrated is growing to the point that now a fresh approach may be just what is needed.

For that reason, I will soon be introducing a total rewrite of the 1974 Congressional Budget Act. My proposal calls for Congress to enact, on or before May 1, a simplified budget that would fit on one page. This binding "budget law," once passed by Congress and signed by the President, would set legal ceilings on spending in 19 major categories. These are legal limits, not "guidelines"; Congress would not be free to violate them or ignore them when it seemed convenient.

"As a freshman congressman, I was struck right away by the utter incomprehensibility of the budget process. Virtually no member of Congress — let alone the public — even reads the huge spending bills we adopt."

Until that budget is in place, it would be out of order for the House or Senate to consider any spending legislation in subcommittee, committee or on the floor. Once the budget is adopted, Congress could authorize expenditures by majority vote, provided we stayed within the ceilings. To break one of the

Christopher Cox, a Republican from California's 40th District, began service in 1989 and is Co-Chairman of the House Republican Research Committee's Budget Reform Task Force.

ceilings, it would take a two-thirds vote. But even then, the President could use enhanced rescission authority —

"My proposal calls for Congress to enact, on or before May 1, a simplified budget that would fit on one page. This binding 'budget law,' once passed by Congress and signed by the President, would set legal ceilings on spending in 19 major categories. These are legal limits, not 'guidelines'; Congress would not be free to violate them or ignore them when it seemed convenient."

"line item reduction" if you will — to bring these super majority-approved budget busters back down to the totals originally agreed upon by the Congress.

Finally, if the Congress and the President fail to do anything at all, an automatic continuing resolution would fund the government at last year's levels — thereby insuring we don't face the dilemma of shutting down the government or signing a massive, last-minute, catch-all spending bill. The prospect of no change whatever in last year's spending would also provide an enormous incentive for both Republicans and Democrats to get to work on a real budget.

The Gramm-Rudman-Hollings targets were aimed at addressing our gargantuan annual deficits, and they have helped. But they do not go to the heart of the problem, which is an undisciplined, runaway budget process.

It is time to harness this wild animal. My bill will be ready for submission this session. Soon we will discover whether Congress is serious about its responsibilities to the taxpayer, to our economy, and to future generations of Americans.

Russo from page 1

favor any new taxes as a solution to the mounting deficits. I think we can handle them by dealing with the spending side of the ledger, with cuts in both military and non-defense spending.

I think the American public is prepared to make sacrifices if we will tell them once and for all exactly what the problem is and exactly how we intend to solve it. It ought to be a bold approach that will attack the problem over a five year period. The citizens understand that there is a serious problem. Of course, they are very cynical today because every time we need to meet a Gramm-Rudman target, we somehow manufacture a way by asset sales, payday shifts, and faulty assumptions. This is done by both the Administration and the Congress. After we do all that, we say we have met the target. Then as soon as we get into the next fiscal year, CBO comes out with a budget that says we didn't hit the target — the deficit is not really \$100 billion — it is really \$161 billion. We have been doing that now for the five years that I have been on the Budget Committee. So, either we change the process and get honest, or we ought to get rid of the budget process.

"I for one do not favor any new taxes as a solution to the mounting deficits."

I think the summit is a rare opportunity for the Congress to work with the President — if he is prepared to make the tough decisions necessary to deal with the massive problem. The problem has many components: The economic assumptions are \$22 billion off; Medicare and Medicaid costs are going up; there is a shortfall in FDIC premiums; and the cost of food stamps is going up. The Administration knew of these problems before it sent its budget to Congress. But the biggest hit we are going to take is the S&L bailout. That is anywhere between \$50 and \$100 billion this year alone. So if you take the

Rep. Marty Russo, a Democrat, has served the 3rd District of Illinois since 1975. He serves on the Ways and Means and Budget Committees, and is Deputy Majority Whip.

Budget Summit from page 1

Talk Is Expensive

Throughout the 1980s the White House and Congress have generally been locked in a budgetary stalemate, impeding any significant deficit reductions. The high-level budget talks held in 1982, 1984, 1985, 1987 and 1989 all fell far short of their stated goals.

Ironically, the fiscal years that were not preceded by budget summits actually resulted in the most real deficit reduction (see figure on page 1). For example, in FY1984, the deficit dropped \$23 billion when spending growth was held to 5.4 percent — half the rate of revenue growth for that same year. Again with no summit agreement in force, FY1987 spending grew only 1.4 percent and the budget deficit fell a record \$71.5 billion. Conversely, the fallout in fiscal years with negotiated deficit reductions was higher taxes and higher deficits.

Historical Overview

The analysis begins by showing how the well-intentioned negotiations of 1982 and 1984 went awry, concluding, "Any plan that promises to balance today's tax hike with tomorrow's spending cuts is unsound. Taxes once enacted into the code are collected, but long-term spending cuts demand constant discipline."

Congress vented its frustration with the deficit by passing the Gramm-Rudman-Hollings law in 1985, but a budget accord reached earlier in the year with the President fared no better than in 1982 and 1984. In fact, the deficit reached an all-time high of \$221 billion in 1986.

The October 19 stock market crash and the looming \$23 billion in automatic spending cuts under Gramm-Rudman-Hollings were the cue for high-level deficit reduction talks in 1987. After weeks of closed-door negotiations, the 1987 summit emerged with a plan to trim the deficit \$76 billion over the next two years. What resulted was a \$5.4 billion increase in the deficit in FY1988 and a FY1989 deficit \$11 billion over the summit target. Also, the Gramm-Rudman-Hollings deficit targets were rewritten, postponing the promise of a balanced budget from 1991 to 1993.

During the budgetary stalemate in 1989, the President and Congress were forced to contemplate across-the-board

PRESIDENT'S MESSAGE

Globalization of Economy Makes U.S. Tax Policy Seem Parochial

Muscovites must be getting used to the golden arches of McDonalds on Pushkin Square. Since opening on January 31 of this year, the Moscow McDonalds has done more business than any McDonalds in the world — the nearly 1,000 Soviet employees there are serving up nearly 50,000 meals a day. Canada's Olympia & York has unveiled plans to extend Moscow's international trade center, and Skanska, a Swedish developer, has joined with five Hungarian state agencies in Budapest's first joint venture office development.

The news is filled with such stories of burgeoning investment opportunities abroad: Eastern Europe, Mexico, the Pacific rim, and even the Soviet Union are opening up. In the past decade, the growth in world trade has far outstripped the growth rate in domestic demand for goods and services. So the watchwords are competitiveness and globalization — how will U.S. firms match up head to head with foreign-based companies in the world marketplace? Some pundits are pessimistic, citing high-tech manufacturing prowess in Japan and the proximity of West Germany to Eastern Europe as reasons that companies based there will prosper.

We at the Tax Foundation are urging policymakers in Washington to realize that U.S. tax policy is a critical component of competitiveness, one that can have a dramatic impact on the fortunes of U.S. firms. Tax Foundation members have made clear in a survey taken earlier this year that they want more research done on the taxation of U.S. firms doing business abroad. Consequently, the Tax Foundation's new senior research fellow Dr. Anthony Billings (see page 6) will initiate a multi-year project on the subject, exploring how various tax provisions help or hinder U.S. competitiveness.

We must remember that international competitiveness depends not only on the innovation of U.S. firms but also on their ability to operate abroad without punitive tax laws holding them back. As the record number of Big Macs selling at the Moscow McDonalds reveals, foreigners do want American products. It is up to us to make sure we don't allow an uncompetitive tax policy to prevent American enterprise from taking those products to foreign lands.

spending cuts mandated by Gramm-Rudman's "sequester." The President and Congress substituted budget summitry for the full sequester, however, and the result was \$6 billion in new taxes and one-time savings gimmicks designed to hit a \$99.4 billion FY1990 deficit target.

The Current Negotiations: Will History Repeat Itself?

In 1990, fears of a slowing economy and possibly \$100 billion in across-the-board spending cuts have sparked deficit negotiations between the White



Wayne Gable

House and Congress. Hopefully, these new talks will actually result in lower deficits. Only 10 of the last 62 budgets paid their own way without deficit spending, and in none of the last 21 years has the budget been balanced. Unfortunately, judging by recent budget summit history, a deficit reduction deal could be a bad deal for taxpayers.

Now Available

A new Issue Brief entitled *A Decade of Budget Summitry*, 4pp. \$10 + \$2 p/h.

from the economics of these proposals, McLure stressed the relative ease of their administration.

Bernard Shapiro outlined the major budgetary legislation of the 1980s. He described ERTA's \$750 billion tax cut over five years as "clearly too big... but the biggest problem was that it was uncoupled with a spending cut." The huge deficits that resulted have played a major role in budgetary and Presidential politics since then.



James Q. Riordan (L), co-chairman of the Tax Foundation and chief executive officer of Bekaert Corporation, talks with Larry Wilson, general tax counsel at Unocal Corporation.

And combined with the repeal of indexing, they have contributed to tax complexity as legislators look for small pockets of revenue in the code. Mr. Shapiro predicted that the budget summit in progress would bring a major tax bill of at least \$15 billion in new revenue.

Fred Goldberg asserted the view that much complexity resulted from perceived abuses of the code. He also sees complexity arising from a well-intentioned attempt to be equitable that ends up in a mire of rulings that are attempts to solve individuals' problems. He closed with a warning that although some may view repealing the corporate income tax as a good simplification, revenue issues are everpresent, deficits are real, and revenue-neutral proposals are the ones that get serious consideration.

Gramm-Rudman-Hollings

The theme of the second panel was "Gramm-Rudman-Hollings: Save It or Scrap It?" James C. Miller, III, Co-Chairman of the Tax Foundation, defended Gramm-Rudman on its record, pointing out that when it has been enforced, the deficit has been substantially reduced.

Congressman Bill Frenzel (R-MN) also spoke in its defense, but both he and Mr. Miller called the sequester a "meat-ax approach" to budgeting that should be avoided.

Henry Aaron, senior fellow at the Brookings Institution, argued against Gramm-Rudman as a mere procedural distraction from the central issue of what and whom should be taxed.

"Fiscal Policy in the 1990s" was the general theme for the luncheon speaker, the Honorable Jim Jones, Chairman of the American Stock Exchange. Mr. Jones reiterated his long-held belief that "the deficit and national debt are the overriding issue this country has to solve if we are going to have good economic conditions for decades and generations to come." In the investment area, he argued for a capital gains differential and would tie that reduction in the rate to a holding period of at least one year to promote longer term investing. Also, he would favor initiatives to even out the debt vs. equity bias in LBOs.

On the spending side, Mr. Jones is pushing investment in human capital — education and retraining. He sees a labor shortage coming and insists we must improve our labor pool. Aside from education, infrastructure improvements and research and development are at the top of his list of spending priorities.

State and Local Taxes

Gordon St. John Gilman, Tax Attorney, Texaco, Inc., moderated the state/local panel, and after pointing out some particular state-level problems he faces in his role as head of the Dallas Chapter of the Tax-Executives Institute, he introduced the panelists. They were Duane Parde, Director of the State Legislature and Private Sector Task Force at the American Legislative Exchange Council; Elliott Dubin, an analyst with the Advisory Council on Intergovernmental Relations; and Steven Gold, Director of the Center for the

Study of the States at the Rockefeller Institute.

These experts testified to increasing tax burden at the state level. With less federal assistance than in the 1950s and '60s, states have been raising reve-

"The deficit and national debt are the overriding issue this country has to solve if we are going to have good economic conditions for decades and generations to come."

***—Jim Jones, Chairman,
American Stock Exchange***

nue and may continue to do so at a rate higher than the increase in personal income.

The "No New Taxes" Pledge

Two politicians and two budget analysts discussed the current budget crunch and debated the need for new revenues. Marty Russo (D-IL) and Christopher Cox (R-CA) gave two Capitol Hill viewpoints while Norman Ture, President of the Institute for Research on the Economics of Taxation, and Robert Greenstein, Director of the Center for Budget and Policy Priorities, debated the relative importance of the deficit to the economy. The panel was moderated by Paul Gigot, editor, *Wall Street Journal*.



Congressman Bill Frenzel (R-MN) is flanked by Henry Aaron, senior fellow in economics at the Brookings Institution, (L) and James C. Miller III, co-chairman of the Tax Foundation and former director of the Office of Management and Budget.

worst case scenario, the deficit is \$186 billion higher than projected. If you take the best case scenario, it is \$86 billion off. It depends on how you calculate the numbers.

So the question is, what do we do about it? We just had a meeting with some of our summiteers. Some of us told them that they should be honest, tell us what the problem is, what we need to do, and how we need to do it. And don't come back with payday shifts and other budget gimmicks, the kind of games that have made people in this country cynical about what comes out of Washington.

The Chairman of the Ways and Means Committee has made it very clear that until he has an agreement with the President on what is needed from his committee, he is not going to offer anything and move it through the committee. So, unless and until the

"The summit is a rare opportunity for the Congress to work with the President — if he is prepared to make the tough decisions necessary to deal with the massive problem."

President decides he wants revenue as part of his solution and works it out ahead of time, I don't think we will see the Ways and Means Committee moving forward.

Personally, I think you can do it without taxes. It will require a severe hit in the Defense Department, and it will take some hits in the domestic side. For example, one of the things I would recommend we do is eliminate plans for the space station. We don't need to put people out in space when others can't find homes on earth. That can wait. This year we are giving the Defense Department \$295 billion in our budget. Last year they got \$296 billion. If you can believe David Stockman, there is about \$30 – \$40 billion of waste in the Defense Department. I will take David Stockman at his word. We need that kind of honesty now if we are to restore sanity to the budget process and prosperity to the nation.

Tax and Budget Conference Brings Government and Industry Leaders Together During Budget Summit

The Tax Foundation held a conference on tax and budget issues in cooperation with Citizens for a Sound Economy Foundation on May 23 in Washington, DC. Corporate executives, members of congressional and executive agency staffs, and of the business press heard presentations from experts in the fields of state taxation and tax complexity, as well as more general discussion of public finance from well-known politicians and economists.

Senator Phil Gramm (R-TX) began the conference by pointing out that the federal budget process was never intended to restrain federal spending and that the budget committee in the House was originally structured to prevent its becoming a source of power. The senator said the Gramm-Rudman-Hollings bill was "the only budget reform that was ever aimed at trying to have a real impact on the deficit." As to whether it has been effective, he pointed out several shortcomings and possible improve-

"The Gramm-Rudman-Hollings balanced budget bill was the only budget reform that was ever aimed at trying to have a real impact on the deficit."

—Senator Phil Gramm (R-TX)

ments, but cited three developments which prove that overall, the legislation has had a positive impact.

First, since the law went into effect, the deficit has been reduced in real terms. Second, for twenty years prior to its enactment, federal spending grew an average of 11 percent annually, compared to 3.8 percent after passage. Third and most important, federal government has begun to grow more slowly than the private sector.

The Burden of Tax Complexity

Lee Sheppard, contributing editor of *Tax Notes*, moderated the first panel



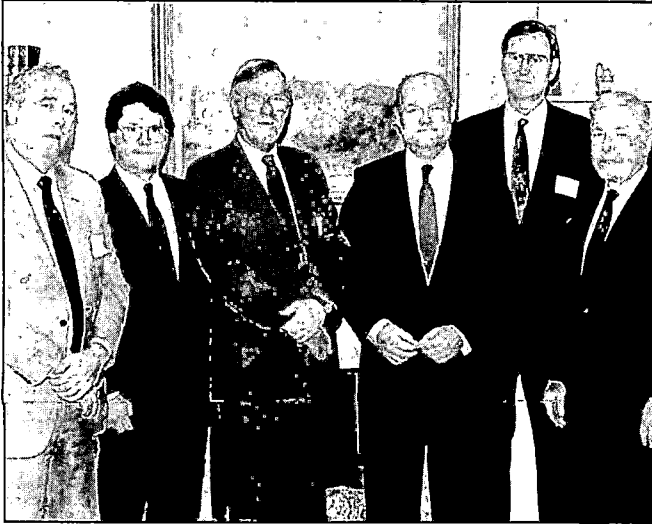
Senator Phil Gramm (R-TX), talks with James W. Nethercott (L), Senior Vice President, The Procter & Gamble Company, and a member of the Tax Foundation's Policy Council.

on the program. It focused on the complexity of tax compliance, featuring Glenn White, Director of Taxes at Dow Chemical; Charles McLure, senior fellow at the Hoover Institution; Bernard Shapiro, National Director of Tax Policy, Price Waterhouse; and Fred Goldberg, Commissioner of the IRS.

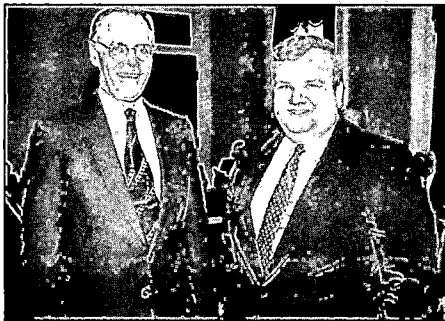
Glenn White started by citing a much-quoted study by the A.D. Little Company showing that in 1983, corporations in the U.S. spent 2.7 billion hours calculating tax liabilities, the normal work product of 1,350,000 people in one year. He decried the Tax Reform Act of 1986 for worsening the situation and gave anecdotal evidence of his own company's travails in trying to deal with the ever more complex code.

Charles McLure picked out a few areas that are sources of complexity — fringe benefits, low income provisions, and anti-shelter provisions like the alternative minimum tax — but pointed out that the only alternative to complexity in these areas is inaccuracy and distortion of economic decision-making. He outlined instead a more fundamental change in corporate taxation which, among many changes, would allow "immediate write-off of all purchases, whether for inventories, intermediate goods, or capital goods." Aside

Briefings in Pittsburgh and Washington Keep Members Attuned to Budget Issues



Senior Tax Foundation staff met Foundation members and other corporate leaders in Pittsburgh for a briefing on the current budget debate. From left to right: Richard Larry, President, Sarah Scaife Foundation; Wayne Gable, President, Tax Foundation; James W. Wirth, Senior Vice President & CFO, Aluminum Company of America; James C. Miller, III, Co-Chairman, Tax Foundation; Robert A. dePalma, Senior Vice President & CFO, Rockwell International; W. Bruce Thomas, Vice Chairman - Administration & CFO, USX Corporation.



Tax Foundation Co-Chairman James Q. Riordan (L) with Lawrence Lindsey, Special Assistant to the President for Domestic Policy Development, during a briefing at the Old Executive Office Building in Washington, DC.



Tax Foundation Vice President Dan Witt (L) exchanges a word with Michael Darby, Under Secretary for Economic Affairs at the Department of Commerce, before a presentation Mr. Darby made to the Tax Foundation's Program Committee.

Anthony Billings Joins Foundation Research Staff

Anthony Billings has joined the Foundation's staff as a senior research fellow. An associate professor of accounting at Wayne State University, Professor Billings' articles have appeared in the *Journal of Accountancy* and numerous other professional journals.

He has studied international tax problems for Dow Corning and 3M, and at the Tax Foundation he will be undertaking a major study of U.S. taxation of American firms doing business abroad.

Tax Features

Tax Features (ISSN 0883-1335) is published by the Tax Foundation which operates as a separate unit of Citizens for a Sound Economy Foundation. Original material is not copyrighted and may be reproduced. Please credit Tax Foundation.

Co-Chairman James Q. Riordan
Co-Chairman James C. Miller III
President Wayne Gable
Vice President Dan Witt
Director of Fiscal Affairs Paul Merski
Editor William Ahern

Tax Foundation
470 L'Enfant Plaza, S.W.
Suite 7112
Washington, D.C. 20024
202-863-5454

470 L'Enfant Plaza, S.W.
East Building, Suite 7112
Washington, DC 20024
202/863-5454

First Class
U.S. Postage
PAID
Washington, DC
Permit No. 2979

Mr. Dan McGroarty
Speechwriter
Office of Speechwriting
The White House
Washington, DC 20500



Citizens for a
Sound Economy
470 L'Enfant Plaza, SW
East Building #7112
Washington, DC 20024

(202) 488-8200
FAX: (202) 488-8282

THE CASE FOR A TAX LIMITATION/BALANCED BUDGET AMENDMENT

STATEMENT OF DR. JEROME ELLIG

DIRECTOR OF PUBLIC POLICY

CITIZENS FOR A SOUND ECONOMY

BEFORE THE

SUBCOMMITTEE ON THE CONSTITUTION

COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

JULY 27, 1989

On behalf of Citizens for a Sound Economy's 250,000 members and supporters, I would like to thank this subcommittee for the opportunity to share our views on the various balanced budget amendment proposals offered in the 101st Congress.

Citizens for a Sound Economy is a grassroots citizens' organization with members in every state and congressional district. Our members include Americans from all walks of life -- the family trying to borrow for that first house or a college education, the employee who needs financing for a car to get to work, the small entrepreneur seeking backing for a new idea that could improve the quality of life for millions of fellow citizens. Tens of thousands of these Americans send in small contributions to help keep our doors open, out of concern for the burden that massive federal deficits place upon themselves and their children.

We know the deficit statistics all too well. The federal government owes almost \$12,000 for every man, woman and child in America. Every \$150 billion deficit obligates the average taxpayer to pay more than \$150 annually in taxes just to meet the interest payments. Congress will soon find it necessary to raise the legal limit on the national debt to more than \$3 trillion, and that figure doesn't even include the unfunded liabilities of programs like Social Security and Medicare.

Citizens for a Sound Economy's members are extremely concerned about these trends. Let me just share with you a few of their comments.

Sadie Adamson of Fort Myers, Florida wrote to us earlier this year, "One rule all my life has been, 'live within your income.' I don't understand a group of supposedly intelligent congressmen doing otherwise with our national income." Betty Woodson of Memphis, Tennessee told us, "I am a housewife. I don't spend more money than I have...If we are only incurring debt on the next generation, we are the immoral generation."

Adah Smith of Athena, Michigan writes, "Above everything else, the budget deficit must be effectively reduced, brought under control, and legislation should be enacted to prevent such from ever happening again. No one ever borrowed themselves out of debt." Norma Rodriguez of Miami, Florida offers policymakers the following advice: "Stop playing with the people. A balanced budget amendment is mandatory. Don't pass the blame to the other guys."

During the past two years, we've received petitions, surveys, and letters from nearly 300,000 Americans who favor the tax limitation/balanced budget amendment. Some of you may have seen the 160,000 petitions that we displayed on the House side of the Capitol steps on July 19. Our members are neither economists nor politicians. They're just ordinary Americans trying to make ends meet.

And their views receive wide support across the country. Earlier this year, Citizens for a Sound Economy Foundation released the results of a nationwide poll on tax and budget issues conducted by the Roper Organization. Some of the results are summarized in an appendix to this testimony.

Approximately two-thirds of those polled said they favor a constitutional amendment which would mandate a balanced budget and limit taxes. This result mirrors those of many other polls, which have found that Americans favor a balanced budget amendment by margins of as much as to 6 to 1. But equally interesting were the Roper poll's results for various subsets of people.

The tax limitation/balanced budget amendment enjoys wide support among major demographic groups and across the political spectrum. It's an initiative that knows no gender gaps or generation gaps, enjoying the support of about two-thirds of respondents of both sexes and all age groups. Sixty-two percent of blacks favor a tax limitation/balanced budget amendment. A solid 67 percent of union members said they favor the amendment, with only 20 percent opposed. Sixty-four percent of working women expressed support for the amendment.

It's probably not surprising that 67 percent of those identifying themselves as conservatives and 65 percent of those identifying themselves as Republicans favor the tax limitation/balanced budget amendment. But the idea enjoys support across the political spectrum. Sixty-one percent of Democrats and 62 percent of independents said they want the Constitution amended to limit taxes and require a balanced federal budget. Sixty-three percent of moderates and 55 percent of liberals also endorsed the amendment. With such statistics, it's no surprise that the tax limitation/balanced budget amendment enjoys bipartisan support.

The American people clearly understand that we need a constitutional amendment to ensure that the budget is balanced. The reason is that in a representative democracy like the United States, a fundamental imbalance biases the political process in favor of those who seek more federal spending on specific programs and against the average citizen who has to pay the bill. As a result, lawmakers who want to balance the budget face an extremely difficult political challenge, even though their constituents want a balanced budget.

Every dollar the government spends goes into someone's pocket, and the beneficiaries of federal spending know who they are and how they benefit. Each spending program has its own well-organized constituency with very obvious and compelling reasons to lobby legislators for more spending on the particular program. The average taxpayer, on the other hand, does not gain very much from elimination or cutbacks of one particular program,

so he has little reason to spend time and effort fighting the special interests over each program. As a result, when it comes time for Congress to make spending decisions, members frequently hear plenty from advocates of specific programs but little from opponents.

Government borrowing compounds this problem. While the average taxpayer may have little incentive to lobby against the special interests, those who are hurt by government borrowing may not even know what the government is doing to them. For example, a family may know that high interest rates put a mortgage for that first home out of reach, but it may not realize the role that the \$150 billion federal deficit played in pushing up interest rates in the first place. Similarly, future generations will pay for debt that the government incurs now, but generations yet unborn certainly have no way of knowing that now -- or of influencing the federal government's spending decisions today.

Ultimately, continuing deficits will even limit the government's ability to satisfy special interests as interest payments on the national debt consume more and more of the federal budget. The government will pay about \$170 billion in interest on the national debt in 1989, double the amount it paid in 1982.

As a result of imbalances in the political process, lawmakers receive a skewed impression of what the public wants. Indeed, the real surprise is not that we have \$150 billion deficits, but rather that for most of its history, the United States managed to avoid chronic peacetime deficits.

The explanation is that for about 150 years, policymakers took it for granted that deficit spending was irresponsible -- indeed, even immoral. The federal government used deficits not to avoid paying for its day-to-day operations, but rather to spread out extremely large expenditures, such as the costs of fighting a war, over a period of years. Even after World War II and the Korean War, the federal budget returned to modest surpluses -- although, unlike the periods after previous wars, the government made little progress toward reducing the national debt. Even though there was no constitutional amendment requiring a balanced budget, policymakers felt obligated to avoid deficits.

But attitudes toward deficits started to change in the 1930s. Balanced budgets, which had been considered prudent economic policy, came under attack from, of all places, the economics profession itself. With the publication of John Maynard Keynes' General Theory of Employment, Interest, and Money, a majority economists eventually came to view deficits as a way to stimulate -- rather than ruin -- the economy. By the 1960s, the change in economists' thinking was pretty much

complete. The American people were told that their common sense concern about federal deficits was misplaced. "Keynesian" economics became a battering ram for special interests to break down the door of the public treasury.

Today, the balanced budget amendment's critics continue to use economic theory as an excuse to attack the amendment. Arguing that deficits can sometimes help the economy, they say that a balanced budget amendment is unwise economic policy because it would tie the government's hands during a recession.

In making such arguments, the critics ignore the fact that most versions of the amendment do not ban deficits outright; they merely require a three-fifths vote of Congress to approve any borrowing. But more importantly, the critics conveniently ignore the past 20 years of economic research and practical experience with unconstrained deficits.

We know from experience that huge deficits could not prevent recessions in the 1970s and 1980s. Moreover, there is no longer a consensus among economists that deficit spending is sensible economic policy. Indeed, many prominent economists now advocate a tax limitation/balanced budget amendment precisely because they understand that the political process makes policymakers more eager to adopt spending programs than to search for ways of paying for them. The absence of external fiscal restraint has allowed policymakers to triple the national debt in just eight years, from \$908 billion in 1980 to an estimated \$3.1 trillion in 1989.

James Buchanan, the 1986 Nobel laureate in economics and a member of Citizens for a Sound Economy's academic advisory board, commented several years ago, "Balanced budgets formerly dictated by moral standards were never explicitly mentioned in formal constitutional documents. Without such standards, however, balanced budget constraints must be explicitly chosen, imposed and enforced."

Similarly, Milton Friedman, the 1976 Nobel prizewinner, has consistently called for a tax limitation/balanced budget amendment. He and Rose Friedman have pointed out that the purpose of the amendment "is to correct the defect in our present structure under which democratically elected representatives vote larger expenditures than a majority of voters deem desirable."

The message from the American people is loud and clear; they want a balanced budget amendment with tax limitation. The economists who agree with the common sense of the American people have also made a convincing case. Citizens for a Sound Economy stands ready to assist this subcommittee in restoring fiscal sanity by making the tax limitation/balanced budget amendment a reality.

APPENDIX

Results from Citizens for a Sound Economy Foundation Roper Poll

Released: January 25, 1989Conducted: December 3-10, 1988Methodology: The Roper Organization conducted personal, in-home interviews among a nationally representative sample of 1,947 adults, age 18 and over.Question: Some people have suggested a Constitutional amendment that would both require a balanced budget and limit the amount of tax increases Congress could pass, except in times of national crises. Would you favor or oppose such an amendment to the Constitution?

<u>Group</u>	<u>%Yes</u>	<u>%No</u>
Total	62	20
<u>Gender</u>		
Male	62	23
Female	63	17
<u>Age</u>		
Age 18-29	63	22
Age 30-44	63	20
Age 45-59	63	20
Age 60+	61	18
<u>Political Affiliation</u>		
Democrats	61	22
Republicans	65	21
Independents	62	17
<u>Political Ideology</u>		
Conservatives	67	20
Moderates	63	16
Liberals	55	29
<u>Other Demographic</u>		
Blacks	62	22
Working Women	64	17
Union Members	67	20



EXECUTIVE OFFICE OF THE PRESIDENT

OFFICE OF MANAGEMENT AND BUDGET

WASHINGTON, D.C. 20503

THE DIRECTOR

EMBARGOED FOR RELEASE UPON DELIVERY
8:00 p.m. EDT; MAY 1, 1990

KEEPING AMERICA FIRST:
AMERICAN ROMANTICISM AND THE GLOBAL ECONOMY

THE SECOND ANNUAL ALBERT H. GORDON LECTURE
HARVARD UNIVERSITY

DELIVERED BY

RICHARD DARMAN
DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

Thank you very much. As always, it is a pleasure to return to Harvard. It is a special honor to follow the distinguished former Chairman of the Federal Reserve, Paul Volcker, and to present the second annual Gordon Lecture.

I should note at the outset: I realize my choice of topic has done little to suggest a coherent theme for this lecture series. Where Paul Volcker delved with delight into the workings of a floating target zone system for international monetary policy, a Director of OMB now comes along and proposes to talk about American Romanticism. I must beg your forgiveness: If you had a job with an annual cash shortage of 150 billion dollars and an inherited debt of roughly 3 trillion dollars, I suspect you, too, might be inclined toward occasional distractions. Be that as it may, I suggest we might all enjoy this Lecture more if I spare you a detailed examination of the Federal Budget's 190,000 individual accounts. I will touch on the Budget, and the Volcker lecture, in due course. But I propose to begin with a bit larger issue.

I. WHITHER THE AMERICAN ROMANCE

The Race Track and the Lorelei
(or America's Decline and the End of History)

In fond memory of my days in the Yard, I put the issue as a question that could be the title of a freshman Humanities course: Whither the American Romance?

For the moment, a large part of the answer seems to be coming from abroad. It is being played out by the recently-liberated nations of Panama and Nicaragua, and the newly-pluralistic parliaments of Eastern Europe. There, the romantic spirit is soaring. It is the same spirit as has shaped the American Romance: love of freedom, respect for individual rights, distrust of excessively-centralized authority, appreciation of markets, hope, optimism, a confident faith in the future, heroization of risk-taking and the pioneering spirit.

Yet, there is a curious irony: As the American Romantic spirit expands in foreign lands, it is oddly quiescent here at home -- especially among the intelligentsia. And while many Americans lament that the U.S. may be losing its primacy to pro-growth Japan, anti-growth sentiment is also becoming fashionable. Confidence in the American pioneering spirit seems mixed, at best. In some respects, we seem to be becoming a risk-o-phobic society -- just when many of our historic risks are seen to be paying off.

This has been an American Century. In World War I, Americans were not hesitant to exhibit their romantic enthusiasm. They were "making the world safe for democracy" -- as Americans would do again in World War II and in the subsequent battles to expand freedom, opportunity, and market-oriented progress.

Yet now, much of America is strangely subdued. Some of this is the correct prudence of mature statesmen. Some is a discrete politeness. But in general, as history seems to be moving America's way, America is less than fully conscious of its own continuing primacy. U.S. opinion-leaders seem less than fully confident of America's vital destiny, its unique capacity to move the world toward new frontiers in the 21st century.

If one asks where in America's cultural establishment is there visible representation of American Romanticism, one is hard-pressed to come up with an answer. The closest I have come is an exhibition now at the National Museum of American Art: the collected paintings of America's finest romanticist (and a native of nearby New Bedford), Albert Ryder.

But though Ryder's work is still alive, it dates from the nineteenth century. And one wonders: In this time of pluralism's heroic advance, where is the domestic celebration of the compelling power and virtue of the American Idea?

The cynicism and self-flagellation of the Vietnam and Watergate eras have passed. But the America-is-in-decline school is now intellectually fashionable. The fashion may have reached a peak with Paul Kennedy's recent best-seller, **The Rise and Fall of the Great Powers**. Yet it lingers with the likes of Mead's **Moral Splendor: The American Empire in Transition** (popularized in Harper's as "On the Road to Ruin") and Krugman's **The Age of Diminishing Expectations** (popularized in the *Washington Post* as "We're No. 3 -- So What?").

This defeatism remains current in the popular mind with the misguided conventional wisdom that "Japan is Number One." Indeed, a recent cover of The Economist provides a pathetic commentary on the erosion of America's once-supremely-confident self-concept. It features a decrepit, hobbled Uncle Sam with this reminder as a caption: "Yes, you are the superpower."

The only romantic American counterpoint of note is Fukayama's naive neo-Hegelian suggestion: that liberal Western ideology is now so evidently -- and inevitably -- triumphant that we are the fortunate witnesses to "the End of History."

One might try to fit these competing images of America's historical condition -- the defeatist and the naive -- within romantic frames. In doing so, one might recall two Ryder pictures. The America-in-decline school might be represented by "The Race Track," also known as "Death on a Pale Horse." In it, a solitary white horse runs the wrong way on a deserted racetrack, with a ghostly skeletal reaper as its grim rider. The end-of-History school might be represented by "The Lorelei" -- the golden-haired maiden whose seductive siren song would distract naive sailors from attention to the whirlpool ahead.

Unfortunately, these images are not exactly uplifting. Indeed, it would be rather depressing if, in fact, the choice were between an eerie race with death and a complacent drift toward the whirlpool.

But, of course, the choice is not so bleak. America's range of possibility -- like Ryder's range of imagery -- is more hopeful and encouraging than the limited choice between The Race Track and The Lorelei. The problem is that realistic and romantically powerful images of hope have not yet been satisfactorily framed to define the American future.

II. THE STRUGGLE FOR "GLOBAL MANAGEMENT"

Of Growth and Greenery (or Neo-Luddites: Making the World Safe for Green Vegetables)

The problem is also that there are romantically powerful counter-images -- advanced by some who are opposed to the American Romantic Spirit. I have in mind one recent example: the picture of a simple, bucolic, blue-green planet -- untainted by competitive industrial advance, unmarked by "artificial" boundaries of competing nation-states. This is an alluring romantic image. It has understandable general appeal -- and was seen everywhere on Earth Day. But the natural appeal of such a romantic symbol may lend itself to abuse if its operational significance is determined by anti-growth activists seeking to lead the mass of so-called "greens." Indeed, the currently fashionable green romance could turn rather blue if it is not advanced in a way that is consistent with the American Romance.

Let me be clear: I do not mean to criticize the majority of self-styled greens. Nor do I criticize most environmentalists. My wife and children are environmentalists. The President is an environmentalist. Republicans and Democrats are environmentalists. Jane Fonda and the National Association of Manufacturers, Magic Johnson and Danny DeVito, Candice Bergen and The Golden Girls, Bugs Bunny and the cast of Cheers are all environmentalists.

Increasingly, we are all environmentalists. And in many respects, that is an important advance. In the main, environmentalism is benign and well-intended. Indeed, it would be irrational and ultimately self-defeating not to promote the efficient use of resources; to address legitimate needs for clean air, clean water, and a healthy biosphere; and to respect reasonably balanced aesthetic interests in natural preservation.

There is a problem, however, in the very success of legitimate environmentalism. Because so many people are self-proclaimed "environmentalists," the label is no longer a meaningful defining characteristic. It is a green mask under which different faces of politico-economic ideology can hide. And now that East-West conflict is in decline, the green mask is one under which competing ideologies will continue their global struggle.

From this perspective, one might identify two distinguishable faces of environmentalism: pro-growth, market-oriented, and pluralistic environmentalism, on the one hand -- a face consistent with the American Romance; and, on the other hand, anti-growth, command-and-control, centralistic environmentalism. The environment can and should be protected within a pluralistic, market-and-growth-oriented framework. But environmental interests should not be used as a false pretext for abandoning that framework. It would be a regrettable irony if just as the values of the American Romance were to triumph in the East-West struggle, they were to be lost in what some environmentalists like to term the struggle for "global management."

Fortunately, this latter threat may well prove transitory. The practical and moral underpinnings of the more radical green "global management" regimes are unlikely to withstand unmasking:

- The "global" management perspective will prove at once too large and too small -- too large because free people will not be managed by a globally centralized regime in which the nation-state withers away; too small because pioneering people will not long be limited to traditional earthly bounds.
- The absolutist approach to environmental values will prove too rigid. Extremists will be met by demands for trade-offs. In efforts to protect existing species, humans will wish somehow to be counted along with turtles and owls (however attractive the latter). And, in a world of limited resources, proposed environmental investments for incremental human health benefits will have to compete. They will have to be justified in relation to the values of economic growth, and also in relation to competing claims for, say, health research, or maternal and child health care, or auto safety, or drug and alcohol abuse prevention.

-- Further, in the end, the radical, anti-growth green perspective will prove too static. The needy of the world will not be helped by, and will not settle for, a neo-Luddite attack on technological advance. More generally, the human spirit -- by definition -- will not be limited to an aspiration for "stasis." Americans did not fight and win the wars of the 20th century to make the world safe for green vegetables.

The Volcker Lecture Revisited
(or Managing Market-Oriented Pluralism)

There is, however, still a problem for those who would fight for more than green vegetables and "global management." For those who favor market-oriented growth, technological advance, pluralistic tolerance, and expanding opportunity -- along with responsible environmentalism -- the problem is this: the management of market-oriented pluralism is often too subtle and complex to capture the public imagination. It is often at a disadvantage in a simplistic competition among romantic images.

Consider, for example, the subject of last year's Gordon Lecture. Paul Volcker was right to focus attention on the "G-5" (Group of Five) and the "G-7" (Group of Seven). These informal institutional arrangements are fundamental to the global management of market-oriented pluralism. Building on the 1986 Tokyo Summit communique, they have a major role to play in setting targets and in advancing economic growth, development, and the quality of life. Their importance has increased with the rise of interdependence and the decline of likely superpower military conflict. They are an essential complement to, and link between, multilateral economic institutions and independent nation-states. Their reach is far beyond international monetary policy -- to virtually all elements of economic policy. And through their connection with the Summit of Industrialized Nations, their reach extends to virtually all of the major international politico-economic issues.

They are, essentially, an executive committee in the international management system for market-oriented democracies. Yet, they are largely unknown.

They are unknown partly because they have chosen to avoid the spotlight and partly because much of their work is technical (even arcane). But even if they wished to be more visible, they would have an inherent disadvantage in the intense competition for media attention. Because they are not dirigiste, they cannot command dramatic leaps forward. Like market-oriented systems generally, they must inspire more by actual performance than by rhetorical promise. In the end, their power to reshape the world for the better depends on their capacity to deliver, and the power of positive example.

The Importance of Being Firstest
(or Building the "City on a Hill")

Within this framework, the same rule applies to the United States. America's power to shape the world for the better depends on its continuing capacity to deliver, and the inspirational quality of its example. This is one reason (among the many) that America must remain "Number One" -- in both perception and reality.

In a world where symbols compete for popular appeal, America is itself a symbol. Its status and visibility -- its capacity to stir the imagination and deliver on its special promise -- have much to do with the relative appeal of market-oriented pluralism. The power of the American example is, thus, fundamental to the pace of human progress and the ultimate quality of human life.

From its very founding, America has served as a beacon of hope, the proverbial "city on a hill." Millions of immigrants have risked and sacrificed -- voted with their feet -- to reach this promised land. Millions and millions more have voted from afar with their hearts.

And America has been worthy of the hope invested in her:

- America has successfully assimilated more of the world's richly diverse races, colors, creeds, and heritages than any nation on earth.
- The United States has grown -- almost miraculously -- from close to nothing at its post-colonial birth; to the largest economy on earth in its first century; on to dominant superpower status in its second century. In the process, America has created unrivaled opportunity for upward mobility, while providing a firm humanitarian safety net for those who might be left behind.
- In spite of the conventional strains of growth, America has preserved what is perhaps the greatest inheritance of natural beauty on the planet.
- And although insulated by two large oceans and continental self-sufficiency, America has engaged directly in the distant struggles for freedom, and the building of international institutions to promote human advancement and healthy development within all nations.

This is an extraordinary record. Nonetheless, there is, among America-in-decline theorists, the sense that America's time has somehow passed; that Japan is (or is about to be) the new "Number One." Confidence in Japan's continuing rise toward the top is, of course, neither universal nor firm. In the face of Japan's recent market troubles, for example, Business Week's cover suddenly reversed its line and asked, "Japan: Can It Cope?" This overreaction to temporary setback was as misplaced as the previous overreactions to Japan's consistent advance.

But putting reactive fears and forecasts aside, it may be useful to pause for a few current facts. It is undeniable that Japan's post-War performance has been dramatically impressive. Still, these points are at least noteworthy as a matter of perspective:

- The U.S. economy is still the largest, by far. It is more than double the size of Japan's. And although the U.S. economy is more mature than some rapidly-growing countries, the U.S. share of total world production has been rising (slightly), not falling.
- Although Japan's productivity growth rate has been higher than America's, U.S. productivity still leads the world, and is roughly a third higher than Japan's.
- Although Japan and Germany are close, the U.S. is the largest exporter of high technology products, and the largest exporter overall.
- The Japanese advantage in real long-term interest rates has recently been eliminated.
- And after adjusting for relative purchasing power, American income per capita is number one, more than a third higher than Japan's.

The fact that Japan has been gaining, however, seems to have shaken America's self-confidence. To the extent that this stimulates a constructive competitive response -- and necessary domestic reinvigoration -- it can be useful. But self-confidence is fundamental to the American identity, just as a sense of special destiny is fundamental to America's self-concept. For America especially, if self-confidence is lost as primacy seems threatened, the loss could be a self-fulfilling cause of decline.

So, given the importance of American primacy -- the real and symbolic power of the American example -- the question of practical, ideological, even spiritual, interest is: How can we keep America Number One?

III. RENEWING THE AMERICAN SPIRIT

BEYOND ALICE'S RESTAURANT (or Budgeting for a Superpower)

Conventional wisdom suggests one place to start: reducing the U.S. fiscal deficit. There are both moral and practical reasons to attend to this:

- As a moral matter, the burden of debt being left to future generations is too high. Future generations are not here to represent themselves. And while the build-up of debt might be justified if it were financing investment in future growth and benefits, it is in fact being used for excessive current consumption.

-- As a practical matter, reducing the deficit is probably necessary to get interest rates satisfactorily down (in the context of continuing growth). And deficit-reduction is clearly desirable to reduce the risk of rates moving in the wrong direction. This is so partly because it is a view held by a strong faction within the Federal Reserve. It may also be true for market reasons. Japanese capital available for investment here may be contracting somewhat. European capital is looking more Eastward and inward. U.S. borrowing for the S&L mess is temporarily soaring. And there is, at some point, a limit to how much debt our capital markets can absorb on reasonable terms.

-- Further, as a political matter, deficit reduction may be necessary to allow the governmental system to get beyond its current stalemate, on to the host of policy reforms that are necessary for America's future.

For all these reasons, the conventional wisdom is correct: deficit reduction should be a high priority.

But that said, there is one bit of related conventional wisdom that needs to be put in better perspective: the notion that raising taxes would solve the deficit problem. This is much too simplistic a presumption to be useful. The problem with Federal budgeting extends far beyond the issue of revenue. Any serious approach to the problem must address at least six additional issues:

(1) The budget process must be reformed; and its fail-safe discipline must be strengthened. The current system simply cannot effectively control spending. Without reform, there can be no assurance that increased revenue would actually reduce the deficit. Indeed, in the current system, the likelihood is that it would not.

(2) The rate of growth in automatic spending programs must be slowed. Entitlements and other "uncontrollable" expenditures are taking over the Federal budget. They have grown from less than 25 percent in President Kennedy's day to about 50 percent now. When combined with interest expenditures, they threaten to consume almost two-thirds of the budget -- leaving less and less room for discretionary initiative. This trend cannot be sustained. Reform of both major and minor "mandatory" programs is essential.

(3) The pattern of federal expenditures must shift away from current consumption, toward investment in the future. This is related to the previous point. The growth of transfer payments must not be allowed to drive out necessary investment in infrastructure, research, and development.

(4) The growth of "hidden liabilities" -- now approaching 6 trillion dollars -- must be slowed and capped. The current budgeting system hardly gets at these at all. Credit subsidies are not properly accounted for. Risk-sharing is minimized. Exposure to loans, guarantees, potential insurance claims, and implicit obligations is largely unattended to. And the next round of avoidable S&L-like surprises is simply left to show when it will.

(5) To the extent that new revenues are to be generated, they must not hamper healthy economic growth; indeed, they should be designed to encourage it. That means, for example, an emphasis on incentives for growth-oriented investment, and on user fees rather than increases in income taxes.

(6) Finally, the Federal accounting system must be reformed to improve financial control and to encourage greater attention to the future. The current system is essentially a primitive cash budgeting system -- without satisfactory controls or audits; without accruals; without balance sheets; without a clear picture of assets, liabilities, returns on investment, or risks. It is arguably worse than the old city of New York's when New York went bankrupt. We have started to fix it. But basically, it is still the type of system one might associate with a 20-person restaurant, not with a superpower.

The Federal budget in fact is (itself) larger than the economies of all countries except the United States, Japan and the Soviet Union. Yet one would sense that something is seriously amiss if one were to hear me as I walk down the old hall toward my office in the morning. Knowing what I know, I can't help whistling the Arlo Guthrie song from just west of here (Stockbridge), in the '60s: "You can get anything you want, at Alice's Restaurant." This really should not be what comes to an OMB Director's mind as he walks to work.

When bipartisan negotiations on large-scale deficit reduction commence -- as necessarily they will -- one of my personal objectives will be to erase the image of the Federal budget as Alice's Restaurant!

That will require serious action on all six of the issues to which I have just alluded. The political system has fooled around for just about long enough. It's time to get beyond conventional posturing and conventional wisdom about the deficit -- time to get down to serious work.

Beyond the Risk-o-phobic Society
(or Ending the Fear of Flying)

That said, let's suppose for a minute that the deficit problem were soon responsibly addressed. Would that suffice to assure the extension of the American Romance for yet another American Century? Clearly not. Deficit reduction in and of itself -- even if it is done right -- is hardly a romantic inspiration.

There are, of course, additional issues on our economic agenda. Internationally, the U.S. can and should: open markets through the GATT and through bilateral negotiations; strengthen economic development through the IMF and the World Bank; assist emerging democracies in the process of transition; and help coordinate all this through the Groups of Five and Seven. Yet, though this is the stuff that one day may fulfill dreams, it is not -- in itself -- what dreams are made of.

If we are to continue to lead the world toward achievement of its full potential, its higher mission, we must renew our own self-confidence and our pioneering spirit. Given the inspirational importance of the American Example, we must somehow do more to restore the American Romantic Spirit -- at home.

Prudent risk-taking has been central to the American Romance. America was founded by risk-takers, expanded by risk-takers and led to the highest standard of living on earth by risk-takers. Now, we must renew the risk-taking capacities that historically have expanded so many frontiers. In the U.S.'s third century, we must counter the tendency to become a risk-o-phobic society.

There is a near-limitless amount of pioneering work to be done -- on technological frontiers, physical frontiers, political frontiers, and social frontiers. But we must move the pioneering spirit toward the 21st century.

-- In public policy-making generally, there must be more scientific and mathematical literacy, less "innumeracy." This would help dispel the misguided notion that we can or should eliminate all risks -- or that human welfare would be greater if we tried. The challenge, of course, is to manage risk more rationally, and to select the appropriate risks.

-- In regulatory policy and the burgeoning range of publicly-subsidized insurance policies, we must give greater attention to the relationship among risks, costs, and rewards. (This sounds like an old Kennedy School ad!) If we were to regulate houses with the same principles we now apply to our food and air, for example, we would all have to live in single-story homes -- for fear of falling down stairs.

And while we undoubtedly need insurance programs, do we really need to design them to produce the likes of the S&L fiasco -- or even, say, the Federal crop insurance program: where we subsidize the premiums, then guarantee the insurance companies against losses, and then pay both the insured and uninsured when disaster strikes? Somehow we must get our basic thinking about risk straight.

-- In social policy, we must allow ourselves -- encourage ourselves -- to be more innovative. Consider, for example, our approach to aging. The fear of medical adversity (and the support of a strong economy) have led the U.S. to the forefront of medical research. One reward is increasing lifespan. But as we continue this healthy advance, we will have to be more inventive in structuring ways for the rising population of older Americans to continue to work and contribute. To date, we've spent far more creative energy on preventing the downside of aging than on benefitting from the upside.

-- Or consider the other end of the life cycle: America's pre-college education system is an embarrassment. We have rightly committed to improve our standing internationally. But to meet our new goals, there will have to be a degree of innovation that approaches both technological revolution and cultural revolution in the American system of education. That cannot be achieved without a greater willingness to take risks.

-- In R&D generally, we must be willing to invest more for the future. Our basic research remains the strongest in the world. But in applied civilian R&D, both the public and private sectors have shown a tendency to underinvest. This must be countered -- with stronger tax incentives for private applications, and direct public investment in generic applications.

-- The recently-launched Hubble telescope might serve as a metaphor for a renewed spirit of basic exploration. But important for the understanding of the cosmos though it be, it is inadequate. A far better inspiration will be the manned missions to Mars and beyond -- to which President Bush committed America on the 20th anniversary of man's reaching the moon. These missions will involve more applied research. More importantly, they will symbolize directly what is at the heart of the American Romance: Man is meant to pioneer, to explore, to expand, to advance, to reach and exceed new frontiers.

In this land of the Wright brothers and The Right Stuff, we must get beyond the policy equivalent of the fear of flying.

Toilers on the Shining Sea
(or Advancing Realistic Romanticism)

Returning to Ryder's images: we don't have to look over our shoulder at an imaginary rider gaining on us in the race. And we should not be distracted by the allure of siren songs; there is serious navigation to be done.

At its best, American Romanticism is a realistic romanticism (if you'll pardon what may seem a contradiction in terms). One might think of it as more like one of the often-copied Ryder marines. The most famous of these, perhaps, is "Toilers of the Sea." In it, the sea is dark. The boat is less than secure. But the moon is a bright and shining light. And with it as a guide, one senses, the toilers will reach the distant horizon.

The distant horizon is where the American Romance is meant to take us. A budget may make some difference, like the state of provisions in a boat. But of larger interest must be: the light that serves as a guide, the Romantic dream, and the spirit that moves us to advance.

We will get the deficit down. But as we do, we must not lose sight of the larger picture. We must -- with confidence -- continue to foster the policies of growth, the risk-taking of pioneers in all walks of life, and the **Romantic Spirit** that has given the world the better **American Example**.

Thank you very much.