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Deficit panel leaders propose curbs on Social Security, major cuts in spending, tax breaks

By Lori Montgomery
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The chairmen of President Obama's bipartisan deficit commission on Wednesday offered an aggressive plan to rebalance the federal budget by curbing increases in Social Security benefits, slashing spending at the Pentagon and other agencies, and wiping out more than $100 billion a year in popular tax breaks for individuals and businesses.

The blueprint drafted by former Clinton White House chief of staff Erskine Bowles and former senator Alan K. Simpson (R-Wyo.) would slice more than $3.8 trillion from deficits over the next decade, reversing a rapid run-up in the national debt that many fear has the country headed for crisis.

To meet that goal, Bowles and Simpson are proposing to slay a herd of sacred cows, including the tax deduction for mortgage interest claimed by many homeowners, the tax-free treatment of employer-provided health insurance and the practice of letting retirees claim Social Security benefits starting at age 62. The blueprint would raise the early retirement age to 64 and the standard retirement age to 69 for today's toddlers.

During a briefing for reporters, Bowles and Simpson stressed that the plan is theirs alone and acknowledged that it is unlikely to win support from a majority of the commission's 18 members, many of whom seemed startled Wednesday by its breadth and scope. Bowles called it "a starting point" as the panel attempts to forge an agreement by Dec. 1.

Obama, speaking Thursday at a news conference in Seoul where he is attending the G-20 conference, cautioned that "before anybody starts shooting down proposals, I think we need to listen, we need to gather up all the facts."

"If people are, in fact, concerned about spending, debt, deficits and the future of our country, then they're going to need to be armed with the information about the kinds of choices that are going to be involved, and we can't just engage in political rhetoric," the president said.

"I set up this commission precisely because I'm prepared to make some tough decisions," Obama said, adding that "I'm going to need Congress to work with me."

Balanced-budget advocates praised the seriousness of the effort, saying it has the potential to reframe the debate over taxes and spending that dominated this month's congressional elections, regardless of how many commission members ultimately support it.

"A White House commission has put out a credible plan to eliminate the deficit and debt. This has changed the rules of the game and, for the first time, things are serious," said Maya MacGuineas, president of the bipartisan Committee for a Responsible Federal Budget, who hailed the blueprint as "a breakthrough."

"After this," she said, "the debate simply cannot go back to silly games where people pretend that eliminating earmarks will solve the problem."

Still, the reaction was harsh in some quarters, particularly among liberals who have vowed to protect retirees from any reduction in benefits. House Speaker Nancy Pelosi (D-Calif.) called the plan "simply unacceptable."

Speaker-in-waiting John A. Boehner (R-Ohio) declined to comment, saying he would discuss the plan with his three representatives on the panel. But Republican anti-tax activist Grover Norquist was not happy and warned that Republicans who support the proposal would be breaking their pledge not to raise taxes.

A five-step plan

Obama created the commission this year, directing it to balance the budget - not counting interest on the debt - by 2015. He also requested a long-term plan to rein in the debt projected to spiral in coming decades as the baby boom generation retires and begins laying claim to Social Security and Medicare.

The Bowles-Simpson blueprint lays out a five-step plan that would exceed Obama's targets, if adopted. It would stabilize borrowing within the next three years, balance the budget by 2040 and bring the debt more in line with historical norms.

Step one would be a sharp reduction in discretionary spending that would slice more than $200 billion a year from budgets for the Pentagon and other federal agencies in 2015 and beyond. Strict spending caps would be enforced by new procedural rules and automatic across-the-board cuts.

Step two would be tax reform. The plan would squeeze $100 billion a year out of the tax code through a comprehensive strategy that would eliminate all the expensive and popular deductions known as tax expenditures. Special rates for capital gains and dividends would be gone, and the inheritance tax would reappear at a rate of 45 percent for estates worth more than $3.5 million for individuals and $7 million for couples.

Not all of that cash would be dedicated to deficit reduction. Some of it would pay for an overhaul of the tax code that would lower rates for most taxpayers and eliminate the unpopular alternative minimum tax. The six current tax brackets would be replaced by three brackets with rates of 8 percent, 14 percent and 23 percent. The corporate tax rate, currently one of the highest in the industrial world at 35 percent, would be reduced to 26 percent.

Step three is targeting the rising cost of health care, one of the primary drivers of future deficits. The Bowles-Simpson blueprint would leave in place the vast expansion of health-care coverage enacted this year, rejecting GOP calls to repeal "Obamacare."

But it would strengthen the cost-cutting mechanisms in the law that seek to squeeze savings from Medicare. And it would permanently protect doctors from a sharp scheduled cut in Medicare payments in exchange for other payment reforms and cost-sharing agreements. The plan also would offer doctors new protection from malpractice lawsuits.

Entitlement programs would not go untouched. Step four calls for cutting farm subsidies by $3 billion a year, reducing benefits for government retirees from both the civil service and the military, docking student-loan subsidies and using a new, stingier measure of inflation to calculate increases for programs government-wide.

Social Security reforms

Step five is an overhaul of Social Security, though Bowles and Simpson took pains to make clear that any savings would be dedicated to the solvency of the program - not to reducing deficits in the government's general fund. The retirement age would go up, while benefits for the wealthiest 50 percent of retirees would go down from currently projected levels.

The plan proposes a hardship exemption for those unable to work beyond age 62. And it would institute other reforms aimed at ensuring that the oldest and the poorest retirees receive adequate support.

In addition to reducing benefits, the plan proposes to ensure Social Security's solvency by raising the payroll taxes that finance the program. The rate would be unchanged, but the amount of income subject to the tax would gradually rise from $106,800 this year to about $190,000 in 2020.

"We have harpooned every whale in the ocean - and some minnows," Simpson told reporters, joking that he and Bowles will "be on the witness-protection list when this is over."

Members of the commission, including a dozen sitting members of Congress, emerged from a morning briefing in a Capitol Hill hearing room praising the effort but voicing deep reservations about the details.

Spending cuts outweigh revenue increases by about three to one, a ratio Sen. Richard J. Durbin (Ill.), the No. 2 Democrat in the Senate, called lopsided. And Rep. Jan Schakowsky (D-Ill.) flatly rejected cutting Social Security benefits as "not at all something I can live with."

Schakowsky also said she wants to see an analysis showing how the changes would affect various income groups. In other words, she said, "Who pays?"

Republicans were equally leery of the proposal. Asked whether he could support it, Sen. Judd Gregg (N.H.), the senior Republican on the Senate Budget Committee, said no. "This is the starting point. It shows the size of the problem, which is massive," Gregg said. "This is the draft for discussion purposes to get us all thinking."

Staff writer Scott Wilson in Seoul contributed to this report.

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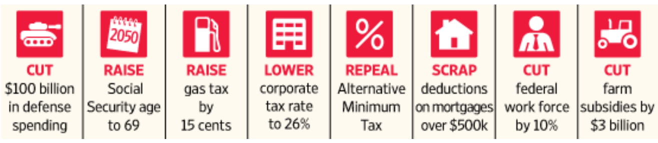
Deficit Panel's Leaders Push Cuts

Proposal to Save $3.8 Trillion Targets Medicare, Pentagon, Middle-Class Tax Breaks

By JOHN D. MCKINNON, COREY BOLES And MARTIN VAUGHAN



WASHINGTON—The leaders of a White House commission laid out a sweeping proposal to cut the federal budget deficit by hundreds of billions a year by targeting sacrosanct areas of U.S. tax and spending policy, such as Social Security benefits, middle-class tax breaks and defense spending.

The preliminary plan in its current form would end or cap a wide range of breaks relied on by the middle class—including the deduction for home-mortgage interest. It would tax capital gains and dividends at the higher rates now levied on wage income. To compensate, one version of the plan would dramatically lower and simplify individual rates, to 9%, 15% and 24%.

For businesses, the controversial plan would significantly lower the corporate tax rate—from a current top rate of 35% to as low as 26%—but also eliminate a number of deductions. It would make permanent the research and development tax credit.

Overall, the plan would hold down the growth of the federal debt by roughly $3.8 trillion by 2020, or about half of the $7.7 trillion by which the debt would have otherwise grown by that year, according to commission staff. The current national debt is about $13.7 trillion.

The budget deficit, or the amount by which federal expenditures exceed revenues each year, was about $1.3 trillion for fiscal year 2010, which ended on Sept. 30.

The interim report by the panel's co-chairmen stands as an opening bid in what will likely be a heated debate over the future of spending and taxes, issues that exploded in the midterm elections. Many of the plan's more provocative elements are intended as starting points for negotiation, not final recommendations.

The question is whether members of the commission can hone the draft into something on which they can agree, or whether they and their supporters will splinter. The plan's unveiling Wednesday provoked denunciations from some quarters, particularly from organized labor and liberal lawmakers, but also from conservative taxpayer advocates.

"We have harpooned every whale in the ocean, and some of the minnows," said co-chairman Alan Simpson, a retired Wyoming Republican senator. "No one has ever done that before." The panel of 18 lawmakers, business and leaders and others was formed by President Barack Obama; it was led by Mr. Simpson and co-chair Erskine Bowles, a White House chief of staff to former President Bill Clinton.

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On Social Security, the plan would gradually raise the retirement age to 68 around 2050 and 69 by 2075. It would combine various cuts to benefits with an increase in taxes on wealthier people's incomes. It would also seek to rein in federal spending on health care beyond what's called for in the recently passed health-care overhaul. This would be achieved by introducing further changes, including reform of medical-malpractice law, and by seeking to slow the growth of the Medicare program.

The plan would make significant cuts on spending over which Congress has direct control, beyond entitlements such as Medicare. It identifies $410 billion in discretionary spending cuts by 2015. It proposes cutting the federal work force 10%, at a savings of $13.2 billion by 2015.

Congressional earmarks—provisions inserted into legislation for lawmakers' pet projects—would be banned permanently, saving $16 billion.

In the bond markets, which have much riding on the outcome of the deficit debate, investors cautioned that the ideas are preliminary and touch many political third rails.

With gridlock likely after the midterm elections split control of Congress between the two parties, enacting major changes designed to significantly cut the deficit "would take some pretty Herculean efforts I think down in Washington, D.C.," said Kevin Flanagan, chief fixed-income strategist at Morgan Stanley Smith Barney.

The plan's authors hope this first draft will improve the chances of any final version, said commission aides, by making it look milder by comparison. At a minimum, the plan's surprise release gives President Obama a chance to appear serious about deficit cutting should he adopt its recommendations.

The recommendations aren't binding; the proposal needs to garner the votes of 14 of the 18 members to trigger votes in the House and Senate. But the final version, due Dec. 1, likely would be a starting point for any deficit-reduction plan Congress and the White House put together.

"In the end, the president is going to have to decide whether to incorporate some of this into t he 2012 budget," said David Walker, a former U.S. comptroller general and an advocate for deficit reduction. "He's going to have to lead, because if the president doesn't lead on this, it goes nowhere fast."

Mr. Obama avoided any comment on the specifics, as did Congressional leaders. Both said they'd wait for a final product.

Lawmaker reaction was mixed, suggesting any final plan will be weaker than the one released Wednesday. Sen. Judd Gregg (R., N.H.), the top Republican on the Budget Committee and a panel member, called it "a genuine product that deserves very serious attention."

But liberal panel members were less enthusiastic. Sen. Richard Durbin (D., Ill.) said he wouldn't vote for it, saying that "there are things in there that I hate like the devil hates holy water."

Associated Press

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Erskine Bowles, co-chairman of the deficit commission, outlined proposals Wednesday.

Some important interest groups were sharply critical, particularly over curbs on entitlement spending. The plans authors "just told working Americans to 'Drop Dead,'" said AFL-CIO president Richard Trumka. "Especially in these tough economic times, it is unconscionable to be proposing cuts to the critical economic lifelines for working people, Social Security and Medicare."

The conservative Americans for Tax Reform also blasted the plan. "It confirms what everyone has known—this commission is merely an excuse to raise net taxes on the American people," the group said in a written statement. Supporting the plan would violate the group's no-new-taxes pledge, which many Republicans and some Democrats in Congress have signed, it warned.

Sen. Gregg said that overall, federal spending takes a bigger hit in the plan than taxpayers do. The plan's goal is to reduce federal spending and federal revenues to 21% of gross domestic product. Federal revenues currently are projected to be about 19% of GDP in 2015, and outlays about 23%.

It would seek to achieve the pullbacks through a mix of spending cuts and increasing tax revenues—about 75% in spending reductions and about 25% from the tax side.

Bloomberg News

Erskine Bowles, right, and Alan Simpson, co-chairmen of the deficit commission.

If the plan was adopted in its entirety, it would reduce the deficit to 2.2% of gross domestic product by 2015, exceeding the target set for the panel by the White House of lowering the deficit to 3% of GDP.

The budget deficit equaled 8.9% of GDP in the fiscal year ended Sept. 30. Despite the raft of spending cuts and changes to the tax code, it would still take until 2037 to balance the budget entirely.

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