NATIONAL GOVERNORS ASSOCIATION

SUMMER MEETING

Friday, July 9, 2010

ACHIEVING A SUSTAINABLE HEALTHCARE SYSTEM

GRAND BALLROOM

SHERATON BOSTON

39 Dalton Street

Boston, Massachusetts 02199

PARTICIPANTS:

GOVERNOR JAMES H. DOUGLAS, VT, CHAIR

GOVERNOR JOE MANCHIN, III, WV, VICE CHAIR

GUESTS:

SAM PALMISANO, CEO, IBM CORPORATION

DR. DAVID CUTLER, HARVARD UNIVERSITY

P R O C E E D I N G S

(11:37 a.m.)

CHAIRMAN DOUGLAS: We've got a busy morning, so I'd like to ask everyone to please be seated So we can get through our opening plenary session on time and give adequate opportunity to our special guests to make their presentations and lead us in an important discussion about healthcare reforms.

So, I'd ask my colleagues and everyone else to please find a seat so we can get our session under way.

Well, governors and guests, good morning and welcome to the 102nd Annual Meeting of the National Governors Association. We'll begin with the Color Guard. So, I would ask everyone to please turn off your cell phones, and please rise at this time for the presentation of the colors by the 54th Regiment Ceremonial Unit, the Massachusetts Army National Guard. And then please remain standing for the Pledge of Allegiance, that will be led by Operation Iraqi Freedom veteran Marine Sergeant, Liz Thompson.

MARINE SERGEANT THOMPSON: I pledge allegiance to the flag, of the United States of America, and to the republic for which it stands, one nation under God, indivisible, with liberty and justice for all.

CHAIRMAN DOUGLAS: Let’s thank our color guard and Sergeant Thompson, and all those who serve our great country.

Well, please be seated and welcome again to our annual meeting. First, I would ask for a motion to adopt the rules of procedure for our annual meeting.

GOVERNOR MANCHIN: So moved.

CHAIRMAN DOUGLAS: Governor Manchin moves.

GOVERNOR [Deval] PATRICK: Second.

CHAIRMAN DOUGLAS: Governor Patrick seconds. Any discussion? Not. All in favor of adopting the rules of procedure say aye, opposed no. The ayes have it. We’ve adopted the rules.

One of which is, that any governor who wishes to submit a new policy or resolution for adoption at the meeting will need a three-fourths vote to suspend the rules. And it must be submitted to David Quam of our NGA staff no later than 5:00 p.m. tomorrow.

I want to appoint the members of the nominating committee for next year's executive committee and officers of the association. Governor [Gary] Herbert, Governor [Jack] Markell, Governor [Steven] Beshear, Governor [Mike] Rounds, and the chair of the committee, Governor [Mike] Beebe.

We have a number of distinguished guests who have joined us for our NGA Annual Meeting from outside of our nation. For a number of years, we've had the privilege of having representatives from the Canadian Parliament. And we're honored and delighted to have them with us again today. Will our Canadian guests please rise. Thank you very much for being with us again.

Members of Parliament and also

Counsel General for New England Neil Leblanc is here, as well, and we welcome him.

We've got a delegation of Arab ambassadors organized by the National U.S. Arab Chamber of Commerce. I had the privilege of meeting some of them last evening, as you did, I'm sure. I met the ambassadors from Morocco, Bahrain, and Iraq, and there may be others who've joined us. Would our Arab guests please rise. Thank you for being with us today.

And finally, for the past 11 years, NGA has been working with a group of governors of the 36 democratically elected chief executives in Nigeria to form a forum similar to ours for the exchange of ideas. And we're delighted to have played a role in that success. They perhaps helpfully didn't call it the NGA, but instead call it the Nigerian Governors Forum, or NGF. And it's a privilege to have them with us, as well. Would our Nigerian guests please rise. Welcome.

Thank you all for being with us

this year. I want to thank our hosts for this annual meeting. As I have noted on several occasions, it’s no easy task to host a meeting of this magnitude. And I want to thank, on behalf of all of our colleagues, Governor Patrick and his wife, Diane, his great staff, the Massachusetts Host Committee for an outstanding job. And hosting the nation’s governors in this historic city is a great privilege for all of us. Deval, come on up.

GOVERNOR PATRICK: Thank you, Jim, and I- it gives me great pleasure and honor to welcome all of my colleagues, my fellow governors and your spouses, and families, and staff, all of our guests, the members of the diplomatic core, guests from around the country and around the world to this summer’s NGA meeting here in Boston.

We have done a lot of good work with you and with the NGA staff to prepare for you, and to make sure that the program under Jim and Joe’s leadership is rich and substantive. And that the time outside of our meeting time is fun.

There's a lot to like about Boston and the Commonwealth. And we invite you to take advantage of it consistent with your responsibilities inside during the plenary sessions and the--I know, I know who you are.

And I invite you as I have on more than one occasion please to use--take advantage of the many restaurants and shops, and other attractions, historic and cultural, that we are famous for and rich in, here in the Commonwealth. We're looking forward to a terrific series of conversations, both those in the plenary sessions and our private conversations, which are always so great and welcome. Let us know if there is anything at all that you need. Great to be with you. Thank you, Jim.

CHAIRMAN DOUGLAS: Well, thank you again, Deval, for your willingness to host this annual meeting. It's going to be a real success, I'm confident. And we appreciate your hospitality.

Well, at our opening session, along with hearing our distinguished speakers on the topic of achieving a sustainable healthcare system, we're going to recognize our distinguished service award winners, and our 15- and 20-year corporate fellows.

I'm excited again at this meeting, to chat briefly about the challenges and opportunities that we have in our nation's healthcare system. It's been an active year, to say the least, in health policy. And we all need to continue to tackle this critical issue for our states.

Over the past year, we've made real progress in moving the R_x for Health Reform agenda forward. Our goal, as an association, was to give each governor the tools that you need to begin to implement aspects of federal health reform, while continuing to pursue your own state-based delivery system reform efforts.

In front of you at your place, is a report that we're releasing today, as a capstone for my year-long initiative. It's a report that reviews the evidence available and highlights state approaches to delivery system reforms, including quality improvement, care coordination, primary care and prevention, and payment reform. It's a thorough and comprehensive review of the options available to each state to move toward a more efficient system and improved health outcomes.

The initiative activities wouldn't be possible without the great support of the governors on the task force. I want to thank Governors Manchin, [Haley] Barbour, [Mitch] Daniels, [John] Lynch and [Ted] Kulongoski for their input and support. And also our initiative funders, without whom it would not have been a success.

Well, as we look forward, the federal healthcare reform law stands poised to make substantial increases in the number of people who have health insurance. These changes, though, will increase the vital need to contain costs and improve system performance. I think we have a great opportunity and a critical need to drive system improvement efforts as federal reforms are implemented. We need to tailor federal reform implementation and system improvements in ways that focus on containing costs and improve the quality of care.

To be successful, these reforms must build on states’ experience in coordination, planning, oversight and innovation. And while states face significant challenges in implementing federal reforms, especially in the current budget situation, we have the experience and insights to push forward if given the appropriate flexibility.

So, I hope you’ll continue to build on the information and guidance we’ve provided over the past year. NGA will continue to offer opportunities for information sharing and advice, as states move forward. And to help us to continue the dialogue on the future of healthcare in our country and the possibilities for achieving a sustainable system, we have two well-respected and very knowledgeable speakers on the topic this morning.

They both have significant expertise with the effects of the healthcare system on our country and the best ways to accelerate improvement. While they come from different perspectives, my guess is you'll hear some similar themes and some new ideas for progress in this important area.

I'd first like to introduce Sam Palmisano, the chairman, president, and CEO of IBM. IBM is the largest corporate employer in Vermont. And I've had the pleasure of working with the company, with Sam, with members of his team many times.

The company is a key supporter of our Blueprint for Health Program, which is changing the way we provide and pay for healthcare in Vermont. As someone who's watched

IBM over the years, I know that this is exactly the kind of forward looking project that Sam would champion.

He was appointed chairman in 2002, and best known for leading one of the most ambitious transformations in the company's 99 year history. Under his leadership IBM has made tough calls to get out of legacy businesses that the company, itself, had invented, and to enter new ones, leading to future growth and innovation. He did this, not by the quick and flashy path of M & A, but through the far more difficult, but more lasting path of re-invention from within. While running a state and corporation are different endeavors, I think we can all relate to how hard this is to do.

Another difficult task anyone in leadership struggles with, especially these days, is being able to adapt to an ever changing economy. Four years ago, Sam authored a forward looking piece in *Foreign Affairs*, identifying the emerging model, the globally integrated enterprise.

IBM has become a premier example of this new form, becoming far more efficient and effective across all of its 400,00 employees in the 170 markets where it does business. The results speak for themselves. IBM has delivered record performance for the past six years.

Today, we'll hear about Sam's latest vision of how our world is working now, how it can work better. Especially in the complicated area of healthcare. I'm delighted that he is able to be a part of our program. Let's all welcome Sam Palmisano.

MR. PALMISANO: Thank you governor. That was a very flattering introduction. It's quite humbling and--and for me to be here. And good morning--good afternoon, I should say, to everyone. It really is an honor for me to speak to you.

You know, we come together in an

interesting consequential moment, as you all know. And I think you would agree that the states are at the epicenter of all of this. If we believe the *New York Times Magazine* cover story a couple of weeks ago, we are now the country of the broken states of America. And I'll talk a little bit about that.

But without question, governors and CEOs must be laser focused on their term issues. I mean, we all understand it. We face a severe fiscal crisis. Everyone understands that we confront a historic moment. Nothing more needs to be said.

But I think the question is what do we do about it. And that answer, to me, depends on your understanding of the present moment in time and how we got here. Because if you think about it as a cyclical economic slump, which happens in a capital based democratic society all the time, you ride out the storm. Hunker down, cut costs across the board, spread the pain, rest for a couple of years and you get through it.

If you believe the crisis was not cyclical, but caused by gross imbalances in our system, then you might drive a reform agenda. More regulation and oversight, rebalance of who pays and who benefits.

But if you believe that this is a turning point, not only in the state of the United States, but in the context of what’s happening across the world, then you would take a different approach.

I happen to be of the latter perspective. I believe that what’s at stake isn’t just the next year’s budget, which is certainly very, very important. We all live by budgets. Like you, I set them, and we have to accomplish those goals.

But America’s long-term global competitiveness is at stake. This period will create winners and losers. And I believe the winners in the new era that lies on the other side of the present crisis will not be those who played duck and cover, those who concentrate on repairing the current system. It's going to be those who look to the future. I believe this because I see what's happening all over the world, especially in the emerging economies. I see it in the trajectory of global economic growth; I see it in all the market data; and I see it firsthand. I just got back from Africa, the Middle East. Before that, I was in China. And you see it. And you see it throughout the world.

In fact, last month we were in Shanghai. IBM convened a forum with 100 civic and business leaders from 40 countries from around the world. The large concentration of our guests were from China. All the mayors, all the mayors of China, were told by the central government to attend a Smarter City Conference. It was also the Shanghai Expo.

But we've also had 100 of these conferences around the world. We did Berlin. Chancellor Merkel was with us there.

We've done New York City; we've done Boston. We've done a bunch of cities across the U.S. But let me tell you, I mean, when you look at the ambition, the vision, the innovation that's driving China and the other emerging markets, it is breathtaking.

The investments that built out of infrastructure, the modernization of entire societies and economies, expanding electrical grids, wireless capacity, transportation, motor management and more; it is attracting businesses, people, and capital flows and is creating a formidable force in the world. It is no longer the low-cost manufacturing capital of the world. And if you assume that it is, that's a mistake.

Now, I know this is not news to you. But I would like you to think about it from a personal standpoint. What your peers and all of those nations are doing, what those leaders of those provinces, municipalities, cities, states, whatever jurisdictional definition you select, what are they thinking about. And this came from a conversation that we had over there. What is the agenda? What choices are being made today? And as I said to the mayors that day, what is your value proposition, why will people live in your city, invest in your city, and stay there?

Now, that is the reality. Your counterparts are making decisions with an eye toward the global marketplace. They're leapfrogging over legacy systems and legacy approaches. They're not just repairing what is broken--and yes, there's a lot to be done. But they're preparing for what is coming. If we want to remain competitive, we must do the same.

Now, I understand, believe me. This is very, very easy to say. And as in some of the meetings I've had with the administration, and my colleagues in the corporate sector, so it's easy for Sam to have this point of view, he had two record years, we haven't. But nonetheless, I mean, so let's put all that aside. I got it; it's harder to do than to talk about. But we are in the business, governors and CEOs, of more doing, more doing than talking, as you all know.

The economic downturn may make any of us sound foolish or wishful, or this is crazy to talk about innovation and invention moving forward. But I also believe that the opportunity is there, because I see it, and I see it in a lot of the initiatives that many of you are working on.

And the American states can use this crisis to take transformational steps, to make your states and our society, as we would say, smarter. And that I believe you governors are absolutely critical to make this happen. You have more impact on America's future standing, I think, than any leaders in the federal government or local governments. And that . . . let me tell you why. Because you sit where all these things come together. You operate the systems that make things work for our people, or for our businesses. That’s where they all intersect. In your cities and your state is where it all happens.

And, as I say, you’re in the position of transforming all of that, because you have to govern. And if you use the term that we use in business and use as a CEO, you have to operate the company. You just can’t give speeches about compelling vision. I mean, you’ve got to run the place. You’ve got to make it come together. You’ve got to make ends meet. The plumbing has to be connected.

So, the subtext to me of the *Times Magazine* cover story, is that the states are really where the action is. And therefore, where the greatest opportunity is to facilitate much of this change.

To capture this moment, though, we need to look at our companies, our organizations, our states in some new ways. And we need to see them, not as isolated entities, but as part of a broader system.

Now, at IBM, we know a little bit about systems. And I’m not really talking about computer systems. I mean economic, logistical, societal systems and how the world operates. If you go back to the work we’ve been doing for a century, for businesses and institutions, we designed and built most of the social security systems of the world; the central banking systems of the world; in fact, we’re doing Russia’s central banking system at this point in time. Retail; transportation; space, Apollo 13.

So, in doing so, we’ve learned a lot about what’s required to do a system that is well-functioning, resilient, and reliable.

Now, first I’m going to define a system. I want you to think about this in the context of healthcare. And then I’ll . . . I’ll bridge it for you. First, there must be clarity of the system’s purpose or goal; a vision of its end-state, put a man on the moon. Second, its element must actually be -- its elements must actually be connected. Third, it must be continually able to know the status of itself and its critical components. And finally, the system must be able to adapt as conditions change, often in real time.

Now, viewed against these four simple characteristics, every well-functioning system looks about the same. An ATM system looks much like a public safety system, or the Apollo mission that sent the astronauts to the moon and brought them back safely, even though they called Houston with a little bit of a problem. But nonetheless, the system as a system point of view, they're very, very similar. And they're very analogous.

It becomes clear why other systems are in crisis, like the one we're focusing on today, the American healthcare system. In truth, when it comes to healthcare in America, we need to put the word system in quotation marks. It is not a "system"; it is a collection of cottage industries coincidentally running into each other from day to day. In theory, I mean I think everyone would agree on the purpose. If we said the purpose of a healthcare system is to provide patient care in a high quality affordable way for all of our constituents, your citizens, my employees, I think there's instantaneous agreement. We can argue about how much time we spend talking about that, but I think we could agree on the system's purpose. It's about the quality of care for our constituencies. Simple--it's simple.

Patient time, treatment, experience should be the design point. And a systems design point matters. Because that's what you optimize around. You optimize around that design point. In this spirit of economics, we all have to pay. You'll hear later, I'm a very big payer in the healthcare system. But you need to envision the end-state, because that's where you do your design is in the end-state. Governor Douglas mentioned the Blueprint

For Health in Vermont. I won't take you through the details, there's a thing called the Patient Center Medical Home. And we were proud to be a participant in that. It's free to everyone; its goals are clear. It has had the great benefit of reducing visits to the emergency rooms and hospitals. Therefore, people are healthier, costs are down and IBM, as the largest employer, is happy to participate. Because at the end of the day, we want a healthy workforce, and we want our costs to go down. I mean, it makes a heck of a lot of sense.

So, we're happy to be participating in those kinds of partnerships. And as I said, the services are free to all of the patients in the system. But a key to mention of patients in our healthcare is really wellness and prevention. And I'll repeat that, because it seems like many days we forget. It's all about wellness and prevention.

Within IBM, we've also substantially reshaped our healthcare programs.

We provide healthcare coverage for 450,000 employees and retires and their family members in the United States. We're one of the few companies that still provides retiree healthcare, at a cost of more than 1.3 billion annually. At one time we found this attractive, until we were defined as being Cadillacs.

In 2004, we pioneered a wellness incentive for employees. IBM has several wellness rebate programs available to U.S. workforce and the retirees. They're focused on what you'd expect, exercise, eating, weight loss, smoking, healthcare risk, children's health, et cetera, et cetera. As a result, IBM employees have become healthier, our costs are rising slower than other costs in corporations or in the public sector. And oh, by the way, we saved about $190 million, because people are healthier; they use the system less.

Do I have to worry about this? We're fine, OK, I mean, you know. There's enough security around, so I guess we're OK.

I mean--just getting through the parking lot was, I mean, you know, it’s easier to get to a Giants game, governor, than to get into the . . . of course, unless we’re playing the New England Patriots.

Nonetheless, but I think the problem is no matter how much efficiency and we improve the care in the system, as a company, as a community, or as a state, it will always be limited because it’s not interconnected. Because a system is interconnected end to end.

In many areas of life, this kind of connectivity is so basic, we simply take it for granted. Consider banking, we take it for granted that we can transfer funds and make payments among institutions. Retail, we take it for granted that you can use the same payment and billing system whether you’re in a store or a Web site, or anywhere else in the world, you can use the payment system. And the reason for that is the interfaces and the standards are defined, and they’re common, and they're open. And the information flows.

And when I talk about information flow, I'm not talking about bits over wire, or in the air now with wireless, it's basically about the processes and the protocols that allow all this information to flow freely and be shared. I mean, clearly healthcare in America, you would agree, today fails the test of a well-functioning system.

Third, many of the components of the healthcare system are not instrumented. I mean, they may be instrumented, but then they're differently instrumented. From the insurer to the doctor to the employer, it's impossible to know with confidence what the current status is. Whatever it happens to be; it could be a medical procedure; it could be a payment in the system. You just don't know with confidence the accuracy of that information.

Yeah, of course, as you know, it's a colossal waste of time and money. But it also introduces consistencies in quality and multiple opportunities for error. If you ever see somebody who comes out of surgery and they have a magic marker on the- wherever it is; they mark the leg--a friend of mine, they marked his leg. I said that’s very sophisticated. They take a big magic marker and mark, so they don’t do the procedure on the wrong leg. I mean, it’s, you know, you can’t make it up. You just can’t make it up, right.

When it comes to the fourth characteristic of a well-functioning system, it’s adaptability. Now, I know you’re asking yourselves this one. Is the healthcare system in your state spanning providers, researchers, governments, payers, patients, and communities; is this ready, this ecosystem ready for what is coming? Because demand is only going to increase. Population growth, an aging rate of baby boomers, and urbanization continuing to march on; there will be far more physical and digital capacity needed than we have. Put it all together and it’s not hard to see why we find ourselves in the current crisis regarding healthcare costs. And it hits the states the hardest of all, as you well know.

Healthcare costs are expected to explode by 70 percent; 70 percent in the next decade, outpacing any form of GDP assumption one could rationally make. So, if you agree on the need for and the lack of a true healthcare system, you know, how do we get there, how do we get to that point in time?

A little bit of a statement on why a computer guy is talking about this stuff, IBM works with the top 10 U.S. hospitals in the United States; the top 20 healthcare insurance companies; the top 30 pharmaceutical companies; and 18 of the top 20 biotechs. We have similar relationships in all of Western Europe, Canada, Singapore, China, India, Australia, and I could walk you through Latin America.

So, we have a point of view, needless to say. We have validated a lot --

what’s required and what I would call a smarter healthcare system; and I’m nearly surprised when I say this, it’s not about a computer chip. It’s not about a device, or a server, or a router. It’s not even about the electronic medical record which everybody wants to define as nirvana. That’s not enough. It’s important, but not enough. It’s about the data. And in this planet, it’s becoming increasingly more instrumented, interconnected. We’re capturing data in unprecedented volumes. In just three years, the IP traffic is expected to be more than one-half of a zettabyte. That’s one followed by 21 zeros. That’s a lot of stuff.

We’re receiving these enormous streams in real time. They’re coming in multiple forms, from rich format text, to rich media, embedded sensors, e-tags, to cell phones and cameras. We’re capturing it from just every kind of system or event imaginable. Supply chains; traffic flows; weather patterns;

water systems; poultry from the farm to the shelf. Billions of individuals using social media networking every day. So, the most important point about this is not how much data that there is, the important point is what the data can tell us.

To capture that, you need to dive deeper. You need to move from big data to smarter data. And that's why analytics are so key. Analytics are really quite honestly, they're just mathematical algorithms. Yes, some are quite significant and they detect patterns; patterns in care; patterns in testing and healthcare; patterns of fraud in the Medicare, Medicaid system. It's detecting patterns. It's the context of the data. You need to see what it relates to, and you need to see it in real time, so you can make the necessary adjustments. And you do so not after the fact.

As IBM's Dr. Paul Grundy, who does a lot of this work for us, said, healthcare

IT is going to be . . . do for the doctors’ minds what the X-ray did for their vision. It going to change how they look at things. And thanks to advance analytics, where we once inferred, we now know where we once interpolated or extrapolated, we can determine. That’s the promise of a smarter planet, a smarter healthcare system. Instead of doing 15 random tests, you do the analysis and do maybe two of the right tests.

So, let’s talk about smarter healthcare and let me give you some of examples. I’d like to do this by example versus droning on from a systems perspective.

So, let’s talk about Governor Rendell’s Pennsylvania, and a very close client of IBM, University of Pittsburgh Medical Center. They’ve improved the quality of care, the delivery of care; they’ve reduced costs by $104 million. They’ve taken up capacity 200 percent. So, very innovative approach. An end-to-end view of the system, and the community, ancillary care units in their area, and connected it; and it works extremely well.

You see in Governor Perdue’s North Carolina, where the University of North Carolina and healthcare is using analytics to improve the quality of patient care, support research, and manage diabetic patients. Records of every patient can be quickly examined for blood pressure, risk of chronic illness, or drugs that have been administered.

You see it in Governor Patrick’s Massachusetts, where the University of Massachusetts is building internal and external health information exchanges that will centralize patient and provider registries and connect the physician community, providing faster, safer, more comprehensive care at a reduced cost.

You see it--I can give you tons and tons of examples around here, here and around the world. You also see it in what a lot of the business is doing. For instance, at IBM, we’re working with major primary care societies, the American Association of Medical Colleges (AAMC), the AMA, and many Fortune 500 companies to promote the concept of a medical home. It is aimed at helping doctors think about themselves as a business, about continuous quality improvement, about efficiency in the office. And in demonstration projects with the American Association of Family Practitioners, they found that practices adopting a medical home approach took income up 14 percent, visits to the emergency room were down 50 percent. Forty percent reduction in hospitalizations for individuals with chronic diseases such as asthma. And as you know, one of the biggest costs of the system is people randomly going to the ER versus receiving primary care. So, tons of examples for this.

But it’s not just in healthcare. Since governors, you have to deal with all of these things. I’ll spend a second on a couple of other examples of where I think many things are becoming smarter in your states and in your cities. Government services, something you have to do obviously every day, like we all do. Governor Schwarzenegger's California, where Alameda County Social Services is using advanced analytics, real-time reporting dashboards enabling caseworkers to find the immediate status of any child, as well as staff member, support service, and program association with that child. So, instead of taking weeks, it takes minutes and it saved $11 million.

We talk about smarter transportation in Washington, DC. The Washington, DC, Metropolitan Area Transportation Authority is managing and maintaining all of its assets, including more than 12,000 bus stops, train stations, 106 miles of track, 1,144 rail cars, and 1,500 buses, plus escalators and elevators, all parts of their transportation system--267,000; they're managing 180,000 change orders and repairing the system before it breaks.

Another example of smart transportation: We're doing this system in Singapore to get people to use alternative transportation versus cars. And it connects everything and then taxis, buses, light rail, etcetera. So, that if you know that you get off light rail that the bus will be there. And they're accurate to within 30 seconds. So, by the use of analytics.

Monitoring traffic flows, congestion, all those sorts of things . . . but you can predict the way to get to where you need to be in a timely manner.

So, it's also true in public safety. In Governor Paterson's New York, where in New York City's real time crime center where we worked with Police Commissioner Kelley and Mayor Bloomberg, there's millions of pieces of information uncovered--previously unknown data relationships--leading to a 20 percent drop in crime. And as you know, New York has now been classified as one of the safest large cities in the world.

Let’s talk about smart educational systems. Governor Riley’s Alabama, where the largest school district, Mobile County Public Schools, is using analytics to track students’ performance and identifying when they’re at risk and adjusting the curriculum, so that they can improve in a real-time way. So, we can prepare the skills that are required for the 21st century.

I mean, the list goes on and on and on. So, there are lots of forward thinking leaders that are seizing upon new capabilities that are available and that are quite ingenious. And yeah, they’re building coalitions and partnerships to get a lot of this done.

And by the way, smarter systems can help with the nation’s economic recovery. There was a recent study published by the Information Technology and Innovation Foundation, that found for every $1.25 billion put into smarter transportation, it creates 35,000 jobs. For the

$10 billion put into the smart electrical grids in the country, it will generate 239,000 jobs per year. For investments of $10 billion over a one-year period, for broadband, especially to rural areas could create or retain 500,000 jobs, which would help economic development in the areas that don't have the same advantages as major metropolitan areas do from a logistical perspective.

Yes, these are challenging times, but I would again make the argument that whether it's healthcare or elsewhere, yes, we need to invest with an eye to the future. Now, it may be surprising for you to hear from a mid-sized company in the IT industry that this really isn't about technology, because this stuff is readily available. I mean it is just readily available. It is about leadership. And I'd like to close by seeking your help in four areas.

The first: we must establish data standards for healthcare and also other systems. But let's focus on healthcare. This is long overdue. You can't have things connected if the information can't flow. You can't have the knowledge of the patient between primary care, and the clinics, and the hospitals, if the information doesn't flow. It has to be standard. The standards have to be established. It's time to stop arguing about it. I've been in all of those meetings. You know, it's 99.7 percent accurate. We can deal with the three-tenths of a percent as an exception.

But of course, the purists will argue on and on and on, and therefore nothing ever gets done. We need these things to be interconnected, and the information has to flow if the system is actually going to work.

For example, as you know, the Obama administration has pledged $34 billion to incent healthcare providers who digitize healthcare records, with a goal of 90 percent of the doctors and 70 percent of the hospitals having EMR systems. But if these aren’t based on standards, and they’re all isolated islands in a municipality, or in a state, maybe in a region, maybe not necessarily for the country, we will have wasted the money--wasted the money.

So, I mean, it’s not about giving doctors iPhones, so they can call their patients. It’s about actually dealing with the systemic problems of the system, which is the accuracy of the information, the flow of the data, so you can take the redundancy of procedure out of the system. Therefore, you take the cost down and the insurance goes down that we’re all users and payers of.

So, on this question of open standards, you need to take an active voice. You just have to request it. It can be done. And don’t--when they tell you it can’t be done--remember 99.7 percent of the information can be standardized. We’re talking about three-tenths of a percent. That’s more accuracy than most anything we do in business or in government.

Second, we need to build smarter systems by design. In anything as complex and dynamic as the 21st-century American state, the qualities of a well-functioning system, you can’t bolt it on afterwards. Many of you are working on redesigning state government. It has to be inherent in the design. Remember, the purpose, the vision, the end-state; it has to be defined in the initial design. It’s too complicated to go add it on later or make it up in an appropriation bill, using your kind of terminology.

And as you do so, you have the opportunity to deal with the key criteria associated with this, which is interconnectivity, analytics, and security in many of your own state operations. A systems based approach, leveraging analytics can have immediate payback--yes, one year immediate payback. There are lots of examples where we’ve helped states in financial losses associated with fraud or compliance issues, usually in taxes. New York state's governor, as you know, I get lots of notices from that system, which I don't live in--New York state. My house is in Connecticut, by the way, since you're here today. But they're convinced I have an apartment in New York because of my own system. So, I can't yell about it. Medicaid, and on, and on, and on.

Third, a smarter state will enable and require far more collaboration. I'm not just talking about the familiar idea of the kind of this private vs. public sector thing, you know, right. We all get together for about 15 seconds and we all run off based on our own self-interest. It's really shoulder to shoulder, working together to solve these problems, i.e., Vermont.

Working together--in the crime center in New York, or North Carolina. I can give you lots of examples. Shoulder to shoulder, work together, our interests are truly aligned when it comes to these types of challenges we all face. And yes, we all have particular responsibilities to our partners, our regulators, our shareholders, et cetera, et cetera, in today’s world. And if a family’s responsibilities is different, then we need to take a system view for them to be transformational. And that will require change.

Finally, where we need your help is on policy and ethics. I mean, there’s increasing pressure on all of us with the empowerment of individual citizens or employees, expectations of sustainable living. We’re entering a very different world as leaders, as we all come together on these guidelines that are being established. And there’s a lot of challenges from a societal and ethical point of view. And a great example is you think about cameras. Yes, crime goes down, first responders have more information. They can get there quicker with more accuracy. People’s lives are saved. Phenomenal benefit. But of course, there are real questions like what are you going to do with all of that data? Who will have it? And what will they do with it? And do I trust them? Very, very real questions.

Similarly in regard to healthcare; clearly, everybody understands if you could digitize--like the UPC code when you buy chewing gum--the medical record, you could check out quickly. I mean, the thing could flow electronically and you get rid of all the paper in the system. Clearly, everybody understands it, but then the questions are one in the same: What about the privacy of information? What about chronic disease? What’s the impact to me as an individual? My insurance premiums: Will I be dropped? Who will be covered? You know, a lot of this is addressed in the new bill, but nonetheless, these are very real societal questions that need to be addressed.

Security is another one. We talk about building smart grids, and smart rail, and smart sewers, and smart buildings. But do we want the security of a web page or a smart phone for your electrical grid or nuclear facility, as you interconnect all these things? I don’t think so. But people are taking that kind of risk. They’re also . . . these are all very, very serious issues, and they require serious work from all state quarters and society. And we need to build support of constituencies--yes, constituencies. We have to come together, we have to work on policy frameworks that address these very, very real concerns or we’re not going to be able to progress in many of these areas.

But let me conclude with a note of optimism. I really do think that the smarter state is not some grand futuristic vision. I don’t believe that. I think it’s very, very pragmatic. Nor do I believe that making IBM a smarter globally integrated enterprise is all about vision without any operational execution. It’s very, very, real. I think the examples say it’s very real. There are more being deployed than the ones I've referenced here today. By governments here, by states here, and all over the world. You see it every day.

So, the smarter state is, I think, very practical, and it's refreshing because it's not ideological. I mean, I understand debates are going to go on. There's going to be debates around healthcare, and energy, and security, and climate change. And it's necessary in a democratic society. But wherever the debate comes out, you still need these types of systems. You still need these smarter systems to address these kinds of problems. They have to be more transparent, more efficient, more accessible, more resilient, more innovative. All those kinds of things. Regardless of where the public policy debate comes down, it has to be done.

So, to get there, I believe that we in this room, and our peers across the public and private sectors, must take a leadership role. And to me that's the good news. And it's the good news, because we don't have to wait. We're not dependent on anything other than ourselves. We don't need the federal government. We can do this ourselves. We don't need anyone else.

Someone is going to do it, by the way. Someone is going to turn healthcare into a true system. And we're working with very smart people that know this field, that have individuals who have billions of dollars of backing, that are going to go in and fix the problem, because they don't want the implications of not fixing the problem.

Someone is going to put in place, the key building blocks for smarter education, to prepare our kids for the future jobs, not prepare our kids for jobs that aren't going to exist when they're in their 30s and 40s. Someone is going to institute standards that allow for cross systems interaction or connectivity. So, silos and state governments can share, or municipal governments can share with state governments, state governments with . . . someone will do all that. Someone is going to unleash the scale, and the expertise, and creativity of the local American communities. Someone is going to build the capacity to identify the key patterns of all this data and knowledge. This will happen.

Someone is going to drive incredible progress for their region across this country. And when they do that, they're going to unlock economic growth and profit. And my suggestion, in a very humble way, is that someone is you, because you're in the middle of it. You have to solve these problems.

So, in a way, whether you wanted it or not, congratulations, you won the election! But I think the precondition for change is there. I mean, you know, you don't have to sell any of these points I'm making to your constituencies or your citizens--the need. I think you need to be transparent and candid with the way, not the need.

I think that's where things break

down, is in the way, not the need. They get the need. And I would argue, and a lot of the work that we've done here and elsewhere around the world, when it's articulated properly like Stockholm congestion, tolling went up, but when they saw the benefits, the congestion went down and pollution went down, they bought in. So, when you're transparent and you show them the result, they buy in and they support it.

So, despite the litany of challenges we face, I'm confident that the states across America will do what leaders do, and that is lead. We're going to go build a bunch of smarter states and cities. We're going to make societal progress, and this is going to be a great place to continue to have a wonderful future. Thank you for your time.

CHAIRMAN DOUGLAS: Well, thanks so much, Mr. Palmisano. We really appreciate your perspective, your time today. We have a lot to learn from the experience of IBM and other major employers that are working to hold down healthcare costs. And we're grateful to have your thoughts at this NGA meeting.

Our next speaker is a health economist with a great deal of experience in the delivery of healthcare cross the country. Dr. David Cutler is the Otto Eckstein Professor of Applied Economics in the Department of Economics and Kennedy School of Government at Harvard University. Professor Cutler was the senior healthcare advisor to Senator Obama's Presidential campaign; served on the Council of Economic Advisors, and the National Economic Council during the Clinton Administration.

Professor Cutler has held positions with the National Institutes for Health and the National Academy of Sciences. He's now a research associate at the National Bureau of Economic Research, and a member of the Institute of Medicine. Professor Cutler is the author of *Your Money or Your Life, Strong Medicine for America's Healthcare System*.

Let's have a great NGA welcome for

Dr. David Cutler.

DR. CUTLER: Thank you so much for the introduction. Thank you to my own wonderful governor and to everyone for having me here. It’s a great privilege and an honor to be here.

I suspect given the health reform debate over the past year or 18 months, you feel a bit like a friend once told me he felt. Where he said if you took all the healthcare economists in the world and you lined them up end to end, that would be a good thing.

So, I will try not to play the usual healthcare economist and tell you what must be done. But rather to give you a sense about what might be done, and a few thoughts about how to make it happen in a productive way. And I will follow along some of what Sam Palmisano was telling you in terms of how to make a system work and how to get it to drive towards better results.

So, let me say there are several challenges that are going to come out of healthcare reform. And one of the things about them is, of course, they all happen at the state level. And I don’t know very many things for sure, but one thing I know for sure is that if we are going to make the healthcare system work; that is, work for people as individuals; work for state governments; work for the federal government; work for us as a country; it’s going to be because the nation’s governors make it work. And there’s no group that is more important in making reform work than that. There’s . . . there’ll be huge issues of regulating insurance. Most of the states here have some . . . have some familiarity with that. Covering people under Medicaid and under exchanges, a number of states here have begun that process.

Perhaps most important in healthcare reform is what I think of as improving the value of care, which is making care be both higher quality and less expensive at the same time. And that, I think is going to be the goal, because without that, nothing else will work.

If we can't figure out how to deliver better care cheaper than all of the commitments that we have made, we'll turn out not to be able to keep. And those commitments that we made long ago to Medicare and Medicaid we won't be able to keep either. So, that's the bad news, or the good news.

The better news is that what we know is there's an enormous amount of wasted resources. That is, we're starting from a place where we really can make enormous progress. Our best guess is that state government spending on healthcare is probably about $70 billion a year above where it needs to be. That is, from a situation where healthcare is roughly one-third of the budget, we're probably wasting about a-third of that, or maybe about 10 percent of state government spending.

And I don't mean waste in the fraud and abuse sense, I mean waste in the sense that the system is not working, and it’s generating outcomes that are inferior, that are higher cost and lower quality. And that therefore, the savings from doing things right would be on the order of within a couple of decades, say $200 to $250 billion a year. That’s the potential for what we should be able to realize.

Now, in other industries, of course, the solution is move things overseas. So, maybe the clinic has moved to China and people can just go there. We need some kind of better solution here. I don’t know if China will be the answer. Maybe China wouldn’t be the right place for two decades from now. But we clearly need some better answer.

And what I want to suggest to you are a few of those answers. And in particular, tell you that I believe that you have the tools at hand to really push the system in the right way.

Those tools are one, the

collaboration that you can foster, as in the Commonwealth of Massachusetts as we’ve done over the past few years in healthcare, using the tools to collaborate between the public and the private sectors.

Second is changing the way the system operates by changing the information and the rules under which the money flows, and therefore in which the system operates. I’ll expand on each of these.

And then third is encouraging innovation, the right kind of innovation that says we’re going to figure out how to do better, cheaper. Not how to do more in a disorganized way. So, those are the points that I want to leave you with.

Let me start off by talking a little bit about where is that $70 billion , that is what is happening that we’re wasting so much money. Part of it is administrative expense.

It turns out the most common

occupation in healthcare, the most common thing that people do, not being doctors, not being nurses, but doing clerical work. Actually I know at Duke University Hospital in North Carolina, Duke University is 900 hospital beds, and 1,300 billing clerks. I feel if I'm admitted there, I should get one and-a-half billing clerks in bed with me.

What are they doing? They're both in insurance and provider groups. They're figuring out how to bill; they're figuring out how to deny bills; they're figuring out how to get them resubmitted; they're figuring out how to get approval for what one needs to get approval. All sorts of things like that. Huge amounts of administrative waste that go on.

I'll tell you how I think we can drive it out, how you can lead the effort to drive it out. Inadequate prevention, people show up in hospitals when they don't need to; when we could care for them better on an outpatient basis. It's not that people like going into hospitals, it’s just that that’s the default activity. People going into nursing homes when they ought to be able to stay out. People not getting the care they need. When they do get care, it’s often too costly. Things happen, repeat episodes. Anyone who’s managed anyone with a chronic illness will know about the tests that are repeated or the services that are redone, because they’re not available the first time.

Medical errors, just to give you one example of this. As a country, we spend about $30 billion dollars fixing medical errors every year. And all of that money, if you think about it, we could use for much better things.

So, what is the common denominator, and I think this really goes at what Sam was saying as well. The common denominator is lack of any organization, or lack of any way of making the system work. You have people who are healthy, who sometimes get sick. And then often time need various medical services. The services that they need are all completely disorganized. They go to a primary care physician, who sometimes, but not regularly talks to a specialist physician. They'll go into a hospital, they'll leave the hospital.

One in five Medicare beneficiaries who go into a hospital come back in the hospital within 30 days. And a very large share of those people never saw a doctor or a nurse between hospitalizations. Huge failures to keep track of people. The cost of that is probably about $10 to $15 billion that we don't need to have. All because people aren't thinking the way that a system does. There's no organization to the healthcare system.

And if there's one theme to both what Sam was saying and what I believe about the future of healthcare is, we won't get it better until it's better organized; until there's some central organization. And I don't mean government controlled organization, I mean something that says our job is to take care of patients, do it in the right way, and do it in a way that works for them.

And if you actually look, not at healthcare, think not about healthcare, but think about every other industry in the economy. Every firm that you admire, from Walmart or Amazon to IBM, whatever it is, and you say, what is it that they do that makes them successful? It's kind of like every happy family is happy in the same way. What is it that leads to success? There are really three things.

Number one is getting the information right. Name an industry that ever got better without knowing what it was doing. In healthcare, we don't know what we're doing. If you want to find out which doctor is better than which other doctor at doing surgery--almost no way to find out. With the exception of a couple of states, Governor Paterson's New York, Governor Rendell's Pennsylvania, Governor Patrick's Massachusetts, you can do it for very scattered situations. But--but not as a whole.

Get the information right. That’s what every big firm does. They know who is doing things; why they’re doing it; how much it’s costing; what the best way to do it is. How do we do it better? How do we make it work?

Number two, make the compensation work out. Make doing the right thing be the profitable thing. If you ask any doctor now, what is it that . . . what incentives do they operate under? It’s do more, get paid more. Do it fancy, get paid even more. So, of course that’s what we get. We get more and more things often times without any documentation that it’s medically appropriate to get. And what we then do is we get in these fights, where someone tries to say no, and the doctor says, but this is what I need to do. And it’s all because we don’t give them the right information; we don’t give them the right incentives.

When you tell doctors, look, we want to help you do the right thing, help to take care of people before they get sick so that they don’t need very expensive care, what they say is alleluia, thank you so much, I would love to do that. And they wind up doing that.

The best healthcare systems--not around the world--the best healthcare systems in the U.S., the Kaisers in California; the Health Partners in Minneapolis; the Geisingers in Pennsylvania; the Group Health Cooperatives in Washington state; the best healthcare systems integrate, coordinate, pay their doctors a better way, and they get savings that are in the millions of dollars a year from doing do. Why? Because they figured out how to make the money and the information flow.

And the third thing they do is they empower workers and often consumers to figure out how to do things better. These are not top down management; this is liberating innovation. If you wander around any hospital--all of you wander around hospitals all the time; I like to do it as well--if you wander around hospitals and you say to the nurses, are there ways you can make the system be better? They'll tell you of course, they'll give you 25 answers for how to do it. If you say why don't you do it, they'll say because no one's ever asked me.

So, you take the most dedicated workforce in any industry anywhere, and you stick them in a little box, and you say do a job. By the way, a third of what a nurse does in a typical day, a third of what she does is documentation. Very frequently taking things from a computer and writing them on paper. Usually we think about going the other way. Often times it's converting things back.

So, we take the most productive workforce, the most dedicated workforce, and we stick them in halls, and we say don't think innovatively; don't make system changes, but just do stuff. And the result turns out to be a huge waste.

So, how do you solve this. Let me tell you what steps I would encourage. Number one, push on the administrative costs. I believe that in U.S. healthcare system as a whole, the administrative waste is probably about $250 to $300 billion a year. And that we should be able to cut that in half within the next five years. We should be able to save the country $100 to $150 billion a year just by streamlining the administrative system.

How are we going to do that? A lot of that is going to come from getting people together and making it work. You talk to any provider group, they'll say it's so complicated, they need hundreds of people in their billing systems just to submit bills. Insurers will tell you the same thing.

When we had the debate over the past year, we didn't agree on very much. One thing that everybody agreed upon, left and right, Democrat and Republican, provider groups, doctor groups, insurers groups, what everyone agreed on is that now is the time to tackle this issue. That if we get together, and it’s going to happen at a state and local level, if you get together and say look, we’re going to cut this out, I’m committed, we’re going to cut this out, now, we’re going to figure out how to make it work. OK, let’s figure out where the doctors are putting resources in; where the hospitals are putting resources in.

One of the hospitals here in Massachusetts is spending $200 million to put in a new billing system that they think will get their bills submitted and paid quicker.

Figure out how do we avoid those kinds of expenses. That’s something very concrete that can happen at the public sector level. It will be an enormously valuable thing for everyone in the system to get rid of that. So, that’s the first thing I would do, is I would push on that quite strongly.

Second thing, you can't do better unless you have the right information. And the information is going to be key here. You have the capacity to do this. You have the capacity to assemble all the data. Remember, in most of your big cities, you've probably only got five insurers. And across your state, maybe you've got really 10. You've got Medicare, which you can now get the data for, or soon will; Medicaid; maybe three or four private insurers in any big city. So, you've got a fairly small group of folks now. You can get that and you can learn what's working. Who's doing more and who is doing less. We know how to do . . . we know how to analyze things like that.

What's the best way how to care for people. The way that I like to think about this question is we have about a million people in the United States who analyze which stock prices go up, which go down. On Tuesday, do they go up if they've fallen on Monday and so on. And we have next to nobody who analyzes medical data and says how do we determine what's the best thing for that particular patient, and which way of treating them is better.

The federal government has done some of that with its comparative effectiveness money. We're going to need a whole lot more. Some of that can happen at the state level, by getting together and saying we're going to learn about this. Those folks who are doing a substandard job we'll help them get better, but they've got to come along the way, too. They've got to tell us how we can help them get better.

There's the money from the federal stimulus funds for health IT, the $30 to $35 billion that's out there, that'll be available this fall. I would encourage--if I were in your position--I would encourage all the providers to be applying for that; get that money; make sure, as Sam was saying, that you can move the information around, because you're never going to get better if you don't know what you’re doing. So, that’s the second thing I would do.

The third thing I would do is make the money follow the value. We have things that are very uncoordinated because that’s the way we pay for it. We tell doctors, see a patient in your office and treat them, and you get paid for that. And that’s what works out well. In reality, what people care about is not who sees them where, but is the patient as a whole doing well. And what has come out in the past year and-a-half, and again, I want to avoid the contentious fights over healthcare reform which we just had, and nobody wants to rehash. But the areas where there were agreement was that we ought to think about ways where we can fix the payment system, so that doctors say treating people well is the right thing to do.

How do you do that? You move away from paying for each service. You say find a way to take care of this person who needs it. Find a way to do that, and we’ll make it worth your while. Take your dual eligible populations for a second, who are probably the most expensive people in the healthcare world. Dual eligible folks. If I were giving advice what to do, one thing I would say is go to the provider group, say whoever can manage these people well will save us money. We'll share that savings with you. The cost is what $20 thousand a person now? Find a way to do it for $15 thousand, save the $5 thousand, we'll give you half of that. Figure out how to make it be in their interest to help you save the money. We're going to monitor the quality of care; we're going to monitor what you do; we're going to make sure that you're not skimping on them. But find a way to do it better. That's what really can happen. We know in the best healthcare system that's what they do. They think about the patients in that way, how do we do better by them.

You can make there be payments as a whole, that is to tell folks we're not going to pay you for individual things, but care for this patient as a whole. You can do measures of performance-based payment that--different things will be appropriate in different regions of the country, and different parts of the state.

The key is going to be to start the process of payment reform. Who can start it best? I think the best answer is the people in this room can start it the most. Why? You have a lot of folks who are already integrally involved with what’s going on at the state level. You have the Medicaid beneficiaries; you have state employees, who are an enormous purchasing group in a lot of states. They are the single biggest group of people buying insurance as state employees. You have the chip population. Pretty soon, you’re going to have the exchange populations as well in many states. So, you’ve got an enormous share.

The private insurers are actually quite willing and eager to work with the public sector to make this happen. If you ask the private insurers why they haven't innovated in payments or in information, they'll say because there was no government there to work with. Partly they were complaining correctly about the federal government; partly they were hoping that there would come a time that there would be reform and they could also work with state governments as well.

So, the private insurers, most of the ones that I know of are quite eager to start to work with state governments. And Medicare, by virtue of the new legislation is now able to do this. And I would push on them, on the federal agencies to make this happen, where Medicare can work with the private sector, with what's going on in state government to make these sort of systematic changes in payment that are then, with the information, going to filter through. Remember, go back to what Amazon, go back to what Southwest Airlines, go back to what IBM, what all those folks do is they get the right information and they get the right incentives. And that's what this is about, getting the right information, getting the right incentives, and then telling people go ahead, and go to it.

Fourth thing I would do is I would be quite open to new organizations helping out. This fall, the federal government will release standards for what are called accountable care organizations. Organizations that are able to bundle large numbers of Medicare beneficiaries, care for them, take care for them better, take part of the savings as profits and leave some for the federal government.

Physicians will be able to set up medical homes, something that Sam was talking about in Vermont and other areas. Then maybe even private ownership here in Boston. Cerberus, which is a private firm, is partnering with Caritas Christi, which is the largest hospital system in Michigan. Blackstone, which is the largest private equity firm in the country is buying Detroit Medical Center. A lot of this innovation can be about how do you bring principles to healthcare that we've thought about outside, how do you actually run something well? How do you take care of a very complicated relationship?

And I want to give you one other way, one other example of how to think about this. I've shown you, and I can give you list of all the people who are billionaires out of healthcare, everyone who is a billionaire in healthcare. In the Forbes 400 list of richest Americans, everyone who is a billionaire in healthcare, with only one or two exceptions, everyone on this list made their money by inventing something you do to people. You stick something in them. They make devices; they make drugs. You stick it to them.

Let me show you a different list, the list of people who made money off retailing. There are six Walmarts; two Home Depots; a few other home improvements; a few Gaps; a Best Buy.

Some of these you have to be from states other than Massachusetts to have visited. And the rest of American industry, not a single person on this list, not a single person makes a product you use. Every single person on this list made their money by changing the way that you buy things. So, that it’s higher quality and cheaper.

In healthcare, you made your money by inventing something you do to someone. Everywhere else you make money by figuring out how to make the system work better. If we get it right, our best guess is that the waste in healthcare, at the country as a whole, is about $700 billion a year. So, you could completely overwhelm that list with people who can figure out how to better coordinate care; streamline medical practices; overhaul the administrative procedures; ensure people get the right care; manage the information flows. That’s what we’re waiting to do.

The reason why it hasn’t happened

is because we’ve stifled it, because we haven’t invested in the information. And we haven’t got the payment or another system set up right.

I think if we do this right, if you can find a way to do this right, what we will do is we will unlock a healthcare revolution over the next decade that will completely transform the way that we see healthcare. Just as illuminating uninsured people will completely transform the way that people think about the relationship with healthcare and about society as a whole.

I want to quickly note one other thing, which is tackling the obesity issue. Sam mentioned what IBM was doing. What we do know is that if you make fattening food be more expensive, people use less of it. And there are a variety of ways. I don’t want to spend too much time on them here, because I wanted to deal more with the things that were probably most immediately affecting you.

But the ways that think of dealing

with that, either at the level of taxes or at the level of workplace kind of wellness programs, that I think belong on people's agenda.

I keep in mind the words of the famous philosopher Jerry Garcia: "Somebody has to do something, and it's just incredibly pathetic that it has to be us."

So, what is it that we have to do. I think what we have to do is we have to unlock savings. We have to start with the easy money, which is the administrative expenses. And then, we have to set up a learning, innovative dynamic system. And the way that I think about it is, I'll just give you the bottom line. The way that I think about it is that our job over the next five, to 10, to 15 years is to set up a process where the healthcare system is completely reborn. And if the healthcare system looks the same in 10 years as it does now, then we will have failed at our efforts. And if it looks different in the way that everything that is responsive to what people want is happening, then we have a chance of making this be the most productive thing we have done in the economy in the past 30 years.

And I will stop there. Thank you so much for having me.

CHAIRMAN DOUGLAS: Well, thank you, Dr. Cutler very much. We appreciate the information and guidance you've presented to us. As many of my colleagues know, this afternoon, the Health and Human Services Committee will focus on childhood nutrition and obesity. That is an important objective in any reform effort.

We got a lot of thoughts from Mr. Palmisano and Dr. Cutler. We've got the new report that NGA has presented. And obviously healthcare reform implementation is going to consume a lot of our time and attention for a number of years to come.

So, let's again thank Mr. Palmisano

and Dr. Cutler for joining us this morning.

My next order of business is one we always look forward to at NGA’s Annual Meeting, and that’s the presentation of awards for distinguished service to state government and the arts. This awards program is now in its 34th year, and offers governors the unique opportunity to recognize the most valuable civil servants and private citizens in their states.

Each of these distinguished honorees has made noble and important contributions to state government and public service. On behalf of all of the governors, I’m honored to congratulate these extraordinary individuals for their commitment to improving their communities, their states, and indeed our country.

I want to thank the governors who submitted nominations for the program. I want to thank the selection committee that was chaired by Betsy Bishop, the president of the

Vermont Chamber of Commerce, who's with us today. Thank you, Betsy, for your leadership.

These awards will be presented in the state official, private citizen and arts categories. And as I announce each winner, I would invite you to come forward, along with your governor, if he or she is here. And I'd then ask the appropriate governor to make a few appropriate remarks honoring the award winner from that state.

We'll begin with the state official category. Our first honoree is Katherine Miller, the Secretary of the New Mexico Department of Finance and Administration. Unfortunately, Governor Richardson is not with us today, but he has talked in his nomination about the exceptional ability of Secretary Miller to find effective solutions to problems in state government. She was instrumental in the implementation of New Mexico's Colonias Initiative, which brought together millions of dollars for critical infrastructure needs along the border region.

The secretary has also streamlined countless state systems, including the reorganization and consolidation of the troubled Legacy Accounting system in New Mexico state government. Her efforts have improved the state's ability to comply with laws, both at the state and federal level, and resulted in the largest reserve balances in the state's history.

In the governor's words, Katherine Miller has been creative and diplomatic in crafting solutions that address competing objectives and has always kept the interests of the people of New Mexico paramount.

Congratulations, Secretary Katherine Miller.

Our next winner is Dr. David Gifford, the Director of the Department of Health for the state of Rhode Island. I'd like to call upon Governor Carcieri to come forward and make some comments.

GOVERNOR [Don] CARCIERI: Thank you very

much, Jim. And it is my great pleasure this afternoon, because I think Dr. Gifford epitomizes a lot of the discussion we've already had and we're going to have later this afternoon.

I appointed David as the director of the Department of Health. And in his time he has demonstrated extraordinary leadership in my judgment, and commitment in using very innovative thinking to achieve good public health outcomes.

He is equally committed, his mantra, we call it, is continuous quality improvement and something he constantly preaches. He was almost single-handedly steering the development of our state wellness, program. We call it Get Fit Rhode Island, which was a catalyst for our state. I think some of you heard me say this in the past, was the first well state in the nation, awarded by WELCOA.

A consistent and strong advocate for immunizations, David has led the Department of Health in achieving some of the highest childhood immunization rates in the nation for over a decade. And we all dealt with, many of us in the Northeast in particular, the H1N1 flu pandemic last year. And through David's leadership, we resulted in having the highest H1N1 flu vaccination rates in the nation; highest for the overall population; for children; and for high risk groups. He had organized 693 school-based vaccination clinics, which we think were a key to achieving this. Which alleviated the burden, therefore, on local pediatricians. And resulted in almost 85 percent of Rhode Island children being vaccinated during that time.

A champion of electronic medical records and e-prescribing, what we've been talking about this morning, and he serves as the state's chief health information technology coordinator.

So, David it gives me great pleasure to present you with the NGA

Distinguished Service Award in recognition of your extraordinary leadership, commitment to public health, innovative thinking and dedication to the well-being of our citizens. Thank you.

CHAIRMAN DOUGLAS: Well, Don, don’t go far, because now we’re going to shift to the private citizen category. And our first award winner is from Rhode Island. Dr. Warren Simmons. So, Governor Carcieri, come on back.

GOVERNOR CARCIERI: You’re going to think this is Groundhog Day before the afternoon is over. But we are very, very pleased because Rhode Island is fortunate to be home to one of the nation’s most respected experts in education reform. Dr. Warren Simmons was the Director of the Annenberg Institute of School Reform at Brown University, has had an impact, a huge impact on untold thousands of children, both in our own state, as well as many of your states, because Annenberg works across the nation.

Committed to improving conditions and outcomes for schooling in America, especially in urban communities, to address the declining performance of many of Rhode Island's urban schools, two years ago I appointed him to lead an urban education task force. And his leadership and experience were instrumental in gathering and developing best practices, and beginning immediate implementation of the task force recommendations, many of which are incorporated in our Race to the Top application.

Thanks to his leadership, Rhode Island is moving ahead more aggressively, to improve early literacy, support expanded learning time, create level pathways for learning for at-risk students, work on the development of a statewide educator evaluation system, and collaborate across districts and schools.

Warren, I'm honored to present you with an NGA Distinguished Service award in recognition of your dedication to the improvement of education, your commitment to reforming urban education for the children of Rhode Island, and the impact your work has had on school districts throughout our nation. Thank you, Warren.

CHAIRMAN DOUGLAS: Our next award winners in the private citizen category are Joe Rogers and Bob Hatcher, the co-chairs of the Commission for a New Georgia. Neither Governor Perdue nor Mr. Rogers could be with us, but Mr. Hatcher is here and he will accept the award.

Joe Rogers and Bob Hatcher have led the Governor's Commission for a New Georgia since 2003, through which they've convened top business executives to identify focus areas and form task forces to address pressing issues in state government. The Commission has addressed a wide range of issues, including procurement, leadership development, customer service, tourism, and state health benefits.

Eighty-five percent of the

Commission’s 130 policy recommendations have been implemented. And their streamlining effects have saved hundreds of millions of dollars in contracts; and led to faster, friendlier, and easier service from state government.

In Governor Perdue’s words, Joe Rogers and Bob Hatcher are a tandem team of leadership that has and will continue to pay huge dividends to the state of Georgia.

Congratulations to Mr. Rogers and Mr. Hatcher.

Next, we’ll recognize the winners in the arts category. From Wisconsin is Willie Ney. Governor Doyle could not be with us today, so I’ll present this award on his behalf. Willie Ney is the founder and executive director of the Office of Multi-Cultural Arts Initiatives at the University of Wisconsin in Madison, and the first wave spoken word and urban arts community.

His one-of-a-kind program gives

students the opportunity to pursue their creative endeavors with faculty, staff, and nationally known spoken word and hip-hop artists, while earning their degrees.

Mr. Ney’s students have performed around the world and promoted a message of social activism and personal growth through uncensored spoken word. He has used his influence to make education more accessible for countless students. And has been nationally recognized for his work.

Governor Doyle said Willie is truly an advocate for education and the arts. He works tirelessly to share the value of his program and its importance. Congratulations, Mr. Ney.

A final award winner in the arts category is Barnaby Evans from Rhode Island. Remember the Chairman of the Committee is from Vermont, so I’m . . . Governor Carcieri.

GOVERNOR CARCIERI: Listen, nothing’s rigged. All right. I’m proud, we’re a small state with a lot of big contributors.

Let me just say if any of you . . . I'd invite you to come to Providence in the spring, summer, and fall, because you're in for a treat when you do.

On designated nights throughout the year, the three rivers that come together through downtown Providence are lit with flickering reflections of small bonfires that blaze just above the water's surface as music from around the world plays.

Tens of thousands of attendees watch and meander along the river banks, dance in local outdoor venues, watch local artists entertain and enjoy a spirit of community. This is a feast of the senses called WaterFire, the art installation project created by Barnaby Evans.

The impact of WaterFire on our state and capital city has been enormous. Since its inception, the WaterFire has attracted I estimate at over 10 million visitors to

Providence and to the state. The average attendance on a night is 40,000 people that just come, walk, listen, as these fires blaze away.

And WaterFire has generated over $45 million in new local spending each year, and inspired the work of numerous artists. And each event showcases the arts on a wide scale, exposing the public to numerous performance artists, visual arts, musical entertainment as I said, from around the globe, and it's all free of charge. So, I am very proud and thrilled, because WaterFire has become known around the nation and actually around the world. And it's the effort of Barnaby Evans, who was the creator of this.

So, I'm proud and privileged to present you, Barnaby, with the NGA's Distinguished Service award to celebrate the breathtaking installation you've created with WaterFire, and recognizing you for your shining bright light in the beautiful city of Providence. Congratulations.

CHAIRMAN DOUGLAS: Well, congratulations to all of our award winners. And thanks again to the governors for submitting nominations. We hope you’ll continue to do so, to recognize outstanding public servants and private individuals in our states who’ve made real contributions.

At each annual meeting, we take a moment to not only thank all of our corporate fellows for their collective support, but to also recognize those companies that have maintained a sustained commitment to governors and the work of our Center for Best Practices.

Founded in 1988, the NGA Corporate Fellows Program promotes the exchange of information between the private sector and Governors on emerging trends and factors affecting both business and state government.

Corporate fellow share their unique experiences, perspectives, and expertise with Governors through the NGA Center for Best Practices, the nation’s only research and development firm that directly serves the governors of America.

Through their support, corporate fellow companies demonstrate a commitment to improving cooperation and understanding between state government and industry, and to developing bipartisan collaborative responses and solutions to issues affecting our country.

The Corporate Fellows program is comprised of over 100 of America's top companies. Firms that through their involvement with NGA are demonstrating their commitment to bipartisanship and good public policy.

Today we honor and recognize the following companies: When I call your name, please come up to the podium to receive your award and have a photograph as well.

For 20 years of membership in the Corporate Fellows program the General Electric Company, T.J. Bolger.

Prudential Financial, Lee Wood.

The Dow Chemical Company, Steve Hazelwood. Steve, how are you? Good to see you.

For 15 years of membership in the Corporate Fellows program, AstraZeneca Pharmaceuticals, Paul Pereira. Paul.

Another 15 year corporate fellow, ACS Xerox Company is unable to be with us, but we appreciate their support as well.

Well, on behalf of all of these governors, let’s once again thank these companies, all of our corporate fellows for their commitment to good public policy and involvement in this unique public/private partnership. Thank you all.

And with that, our opening plenary session stands adjourned. Thank you all.

(Proceedings concluded at 1:06 p.m.)

COMMONWEALTH OF MASSACHUSETTS

I, PAULINE L. BAILEY, PROFESSIONAL COURT REPORTER, do hereby certify that the foregoing is a true and accurate transcription of my stenographic notes, to the best of my knowledge and ability.

WITNESS MY HAND, this 14th day of July, 2010.

Pauline L. Bailey

NATIONAL GOVERNORS ASSOCIATION

2010 ANNUAL MEETING

Saturday, July 10, 2010

REDESIGNING STATE GOVERNMENT

Sheraton Boston

Grand Ballroom

39 Dalton Street

Boston, Massachusetts 02199

PARTICIPANTS:

GOVERNOR JAMES H. DOUGLAS
of VERMONT, CHAIR

GUEST:

ALAN MURRAY, DEPUTY MANAGING EDITOR
and EXECUTIVE EDITOR, ONLINE, *THE WALL STREET JOURNAL*

P R O C E E D I N G S

(1:14 p.m.)

CHAIRMAN DOUGLAS: This is a very important topic for NGA and for our fates this afternoon as we have a facilitated discussion on the future of our state's fiscal situation, the economic challenges we are facing, and the creative, innovative ideas that governors are putting in place to move our states forward.

Could everyone please find a seat so we can get underway. I want to welcome everyone and thank my colleagues for their participation this afternoon. The goal of this discussion is to talk about how governors across America are redesigning state government in their respective states. How we are coordinating agencies. How we are making purchasing more efficient. How we are redesigning prisons. How we are finding better outputs while saving money at the same time.

We may get into how states are redesigning the higher education system for example, elementary and secondary education. We have a lot to learn from each other in these challenging times, and I look forward to hearing what is happening in the various states.

We also need to think not only about what we are doing immediately to address the fiscal challenges, but how we are positioning our states for success in the future. It is going to be important, I think, that we think about the long-term and restructure, redesign state government so that our successors and our future generations can have more sustainable state government in their states.

We are honored to have Alan Murray with us who is the deputy managing editor and online executive editor of *The Wall Street Journal*. He has become a trusted source of economic policy information throughout a long and distinguished career.

He has been with the *Journal* since 1983. His longevity is a testament to the tremendous contributions he has made to his readers. He was bureau chief in Washington for a while and won an impressive total of three Pulitzer prizes during that time in addition to a number of other accolades.

He is a frequent contributor to CNBC where he has co-hosted the “Capital Report.” He is the author of three bestselling books. His career has taken him all over the world, literally. We are delighted that he can be with us in Boston today. Let's all welcome Alan Murray.

MR. MURRAY: Thank you for having me here in Boston. Thank you Governor [Deval] Patrick. Thank you Governor [Jan] Brewer for inviting me to your party in Boston. It's been an interesting arrival.

I want to start by offering my condolences to all of you because all of you have picked a very unfortunate time to be governors. It is the worst fiscal crisis that we have seen since the Great Depression, as all of you know better than I do.

It looks like it is going to be very prolonged. You may be seeing some pickup in revenues, but whatever you are seeing coming in in revenues is going to be taken out probably by the federal government at the same time. Job growth, judging from the latest numbers at least nationwide, is very, very slow. It doesn't look like it's going to pick up for a long time. Of course, on top of that you have a health-care funding crisis layered on top of it.

So, I'm sorry that Governor [Joe] Manchin isn't here, but it is easy to see why a governor might want to become a senator. I mean it's a pretty good deal, right? There is no real responsibility. You do get to talk a lot, a lot of really nice perks. You certainly don't have a budget constraint that you have to worry about. So, I am surprised there aren't more of you thinking about it.

I appreciate the fact that you all have a very, very tough job. I feel like Governor Douglas has given me a very easy job here today because my job is essentially to get this shy, introverted group of people to talk.

So, we are going to talk a little bit about the decisions you've already made in dealing with the crisis. Then we want to look forward and think about how the decisions you have made, the decisions you should've made or the decisions that you may make in the future or your successors may make in the future that set the states up for the kinds of conditions that they are going to be facing five years and 10 years down the road.

I think we are getting a pretty good idea of what that world may look like in some ways anyway.

So, let's start with education, because we all know that education is the future. We all know that education is critical to creating sustainable jobs to long-term growth.

A simple question, how many of those of you who are sitting here right now have made it through this crisis without having to cut education spending at all? I'm talking K-12 and higher education. Governor [Dave] Heineman, you had a somewhat better economic situation than some of your fellow governors. What's the secret?

MR. HEINEMAN: The secret is we prioritized education. They didn't get as much as they wanted, but we continued to give, particularly K-12 funding has increased significantly. Higher education has maybe only gone up about 2 percent but compared to 10 percent reductions that other states have taken, it's a challenge.

How did we get there? I had shared a little bit as you and I were talking beforehand. If you look over the last three or four years what we did, we modernized our economic incentive programs. We lowered taxes. We began to control our spending. About three years ago slowed the growth. We haven't had a cut. And the end result is we have a fairly fortunate opportunity.

Our unemployment rate is 4.9 percent. I am still trying to catch up to Governor [Mike] Rounds over there. But the fact of the matter is we have diversified our economy. That was the other key element. But again, we just said education and jobs go hand-in-hand. Give our kids the best education we can and create jobs in the state to keep them there.

MR. MURRAY: I think it's a fair bet, I won't even ask because I know the answer that everybody has seen around the state who prioritizes education. Well prioritize education. Governor [David] Paterson, you have prioritized education, but you have been pushing for bigger cuts in education than the state legislature wants to give you. Why is that?

MR. PATERSON: The budget in New York state was originally projected for 2009 and 2010 at $5 billion. It quadrupled in nine months, which is to our view the largest escalation of a budget deficit experienced by a state in the history of the United States.

So what happened in both of the years that I have been governor is that you had $3 to $4 billion outyear budget deficits. And in those periods of time, you really can't cut education in the middle of the school year.

For the five years prior to when I became governor, education spending had increased by 47 percent over that period of time. So, there just came a point where our resources were so depleted having cut $21 billion in that period of time that inevitably we hit even the sacred area of education.

This year we actually wound up cutting $1.4 billion on top of it because we wanted to protect ourselves from an outyear gap where we wouldn't be touching education.

There's a little bit of a competition between education advocates and the health-care advocates. We have cut health care $5.25 billion since I've been governor. Over the two and a half years I have been governor, we have cut $43 billion from the state's economy. Combined with California, it's over $100 billion dollars just by those two states alone.

MR. MURRAY: We will get to health care in just a minute. I am sure all of you face the same problem. Education is a huge chunk of your budget. Education is a high priority but you have to deal with the fiscal realities. Who else wants to take this on?

GOVERNOR [Martin] O'MALLEY: In our state, we embarked about six years ago on a more equitable funding of public education. So, when we came in, part of the disjunct there that they had locked into this increase for education, which is a valuable and good thing, but there was no revenue stream attached to it to support it.

So early on, we had to address the $1.7 billion deficit that was left behind by our predecessor. We called a special session. We did a number of difficult things including raising the 42nd lowest sales tax in the country by a penny.

But for the last two years *Education Week* magazine has named our schools the best public schools in America, and thanks to Congress and President Obama, we are able to make record investments this year even with the cost containment things. And not being able to do as much as we might hope to, it's nonetheless been an investment that I believe is paying off.

We've never had higher achievement levels for our kids. And it's actually something that I do believe that the people of our state believe is tied to our economy. It is part of the reason why we've had three months in a row of positive job growth ahead of other states. And it's our future.

MR. MURRAY: So, you raised taxes, not a lot. But you raised taxes in part to pay for education?

GOVERNOR O'MALLEY: Right.

MR. MURRAY: And you are one of the people in this room who wants to stand for re-election?

GOVERNOR O'MALLEY: Sure am.

MR. MURRAY: And you're comfortable with that?

GOVERNOR O'MALLEY: Well, we all embrace our own vulnerability or we wouldn't be sitting around this table. We all work for the chief.

MR. MURRAY: The same question about taxes. How many of you have made it through the last two years dealing with your fiscal situations without having to raise taxes? Let's not play semantics here. Let's take a broad definition of taxes.

Show of hands if you made it through?

Now I see Governor [Dave] Freudenthal. I see you're raising your hand, but my understanding was you were proposing a tax on wind farms?

GOVERNOR FREUDENTHAL: We did, and then they got an offset in tax reduction. It had more to do with reallocation of revenues than net increase in revenues. And to the extent it is going to increase revenues is probably four years out. It is more of public policy statement with allocations to local governments than it was with regard to tax policy.

MR. MURRAY: We can get back to environmental issues in a minute. But is taxing windmills the right way towards our energy future?

GOVERNOR FREUDENTHAL: If you're committed to the notion that you want a level playing field, fully diversified energy portfolio, then yes, it is because in the sense that in our state all of the other forms of energy are fairly heavily taxed. Wind will be the least heavily taxed of anybody in the region.

The taxes, as I said, don't kick in for a while. So, we'll see what really happens.

MR. MURRAY: Governor [Chet] Culver, I saw your hand going up on no tax increases. I don't think I saw your hand going up on no education cuts. So, part of what you managed with no tax increases was to cut education, I assume?

GOVERNOR CULVER: Yes. We had to do a 10 percent across-the-board cut last fall. But we also, as a result of that, have a $500 million surplus, AAA bond rating, and we are one of the fastest growing economies in the country.

MR. MURRAY: It was the right trade-off as far you're concerned?

GOVERNOR CULVER: It was the right trade-off. Now we were able to backfill 5 percent of that 10 percent cut to education in part because we made the tough decision, and our economy is picking up a lot of steam right now.

MR. MURRAY: Who else wants in on this?

CHAIRMAN DOUGLAS: We reduced taxes this year. We cut taxes on capital gains in the state and we have not reduced our education spending either. We have made other tough choices.

MR. MURRAY: You increased spending for the university, right?

CHAIRMAN DOUGLAS: We increased higher education spending because we are among the lowest in the nation on a per capita basis for higher ed. So, it has always been a priority for me.

The K-12 education, we are near the top in the nation. We have a declining student enrollment, and frankly that is an area where we probably could trim somewhat. But since budgets are set at the local level, it hasn't happened.

MR. MURRAY: Where does the money come from?

CHAIRMAN DOUGLAS: From property taxes. According to the NEA, we have the second highest property tax burden in America. That's a real problem for people who are struggling to get by.

MR. MURRAY: Yes.

GOVERNOR O'MALLEY: May I piggyback on Governor Douglas? One of the things that we were able to do these last few years--I think I mentioned the 42nd lowest sales tax--we also were able to

reduce income taxes for 85 percent of Marylanders who earn less than $150 thousand and we are the only state to go four years in a row without a penny's increase to college tuition.

We've also had to cut $5.6 billion out of our operations because of this priority.

MR. MURRAY: That's the thing. If I read the report right, part of the way you did that was by dipping into your capital funds, right?

GOVERNOR O'MALLEY: No.

MR. MURRAY: No game playing, no bargaining for the future?

GOVERNOR O'MALLEY: No. As a matter of fact we actually diversified our transportation funding. We have not dipped into capital. We along with Governor Culver, are one of eight that still has a AAA bond rating.

So, we did this with tough choices and huge cuts, $5.6 billion. We are the first administration to submit a budget with state spending lower than it was four years previous.

MR. MURRAY: Because Governor

[Mike] Rounds, there are a lot of states that are either borrowing from pension funds, dipping into rainy day funds, doing things that might help for one year, but aren't going to help if this downturn is going to be as extended as the NGA thinks and some other people think.

GOVERNOR ROUNDS: You are correct. In South Dakota we have a requirement that we basically can't borrow money. So, we have to balance our budget.

We've got the same amount in our reserve accounts right now as we did in 2003. We've maintained our status as having the lowest taxes collected per capita of any state in the nation.

It's not easy to do it and in some cases there is an offshoot. This year we took about $9 million away from higher education. Part of that is going to be offset because they can also raise tuition.

So, this year tuition in South Dakota

for our state-supported schools will go up about 4.6 percent.

MR. MURRAY: Yes, sir, Governor [John] Baldacci?

GOVERNOR BALDACCI: In the last two years we didn't raise taxes to balance the budget, but we did have to change the administration of education because we were pouring more money into it. We had to consolidate school administrative districts.

We went from 152 and the goal is to 80. Tap in local school boards and districts has been a political contest of wills, but it was taken to a public referendum that the public supported 60 to 40, but we hope will pay dividends over time. But we don't have a printing press and we had to be more efficient with their resources. So, we took on that challenge. It is still a work in progress.

GOVERNOR PATRICK: Alan?

MR. MURRAY: Yes.

GOVERNOR PATRICK: I was just going to say that probably most of us that are in the midst of the worst recession and worst economy in living memory have taken a blended approach.

MR. MURRAY: You did everything.

GOVERNOR PATRICK: We did a little of everything. We cut $4.5 billion out of the budget. We reduced the number of positions by nearly 3000. We got concessions from public employee unions.

MR. MURRAY: Not all of them. There are a few people still out there.

GOVERNOR PATRICK: Who work for the state. Yes, they are not happy because they were cut too.

MR. MURRAY: You've made everyone angry.

GOVERNOR PATRICK: We've had to. It's about shared sacrifice, frankly. We have raised our sales tax from five to 6.25 percent, still low but it is a big jump in the minds of our people here in the Commonwealth.

We had a big rainy day fund, and we've drawn down on that because it's been raining. The stimulus funds have also helped. So, that blended approach and like some of my colleagues here, we've had our high bond rating reaffirmed by all of the

independent agencies because of that blended approach.

I wanted to suggest another part of this story, which I think is incredibly important. One of the things that a crisis presents is opportunity. So, thinking about big questions about what it is we want government to do and not do--and not.

One of the smartest ways to do that has at least in Massachusetts enabled us to move some reforms that I think under normal circumstances would be hard to do. One example is in transportation that we'll get to.

MR. MURRAY: Before that, what have you decided not to do?

GOVERNOR PATRICK: I'll tell you first of all just in terms of reforms--One thing we decided not to do is continue to be the only state in the nation that used police details on every single construction site.

I respect the police and I respect their concerns for public safety. I have concerns

for public safety. But we now use civilian flaggers at state construction sites where public safety doesn't require a uniformed officer. I think that was the right thing to do.

I also think that when we took six different transportation agencies and collapsed them into one and made the focus on the traveler instead of on the bureaucracy and saved more than a quarter billion dollars that was the right thing to do. But it made a lot of people mad because change is like that.

But I think there are examples of that probably everybody has been seizing on, right? Things that we know are right to do that would be harder to do if the circumstances were different.

MR. MURRAY: And we definitely want to spend some time this afternoon talking about that.

Governor [Chris] Gregoire, I want to get you in on this because I gather you've had a situation not unlike Governor Patrick. You've had to do a little bit of everything. You said you weren't going to raise taxes, raise revenues. You've had to do a

little bit of that. Can you talk about your experience?

GOVERNOR GREGOIRE: Well, we've had to cover a $12 billion shortfall in the last three years. It's a $32 billion budget. So, it's been a challenge. So, we did a little bit of everything.

The first with $9 billion we raised no taxes. Second year, this last year, with just over $2.8 billion we did raise some discretionary taxes to the tune of about $600 million.

But we have used our rainy day fund because we considered it pouring down rain. We have swept accounts that had more money than what they ever needed to do what they had to do. We have raised college tuition.

With K-12 an interesting aspect for us is we are constitutionally protected. So, you can't cut it. I didn't raise my hand because the people passed two initiatives with no funding associated with it. One teacher pay and two class-size. So, those were suspended. That's why I didn't raise my hand. Again, that is by virtue of

initiatives with unfunded demands on the state. The rest is constitutionally protected.

In our higher education institution, we found that we have some of the lowest tuition in the country of comparative universities. So, we cut them, but authorized them to raise their tuition to make up for the cuts.

So, I can't think of anything we haven't done to include closing down institutions, shutting down a third of our boards and commissions, collapsing environmental agencies.

MR. MURRAY: Health care?

GOVERNOR GREGOIRE: We have cut health care, yes. In fact, I have to put out an all-cuts budget in December this last year. It was going to take a huge toll on health care, and that's what drove everyone to raise some revenues.

MR. MURRAY: Health care, I'm sure is a tricky one for all of you. It is hard to describe it as a rainy day problem. If it is a rainy day problem, we are in for Noah's flood because it's not going away anytime soon.

We got a little bit of help from the federal government. Some of you are asking for more help from the federal government. Is that the right way to deal with the health care problem? Who thinks it is? Governor [Pat] Quinn? I mean they don't have the money.

GOVERNOR QUINN: I think health care is a fundamental right. I think everybody is in and nobody should be left out.

I walked across our state from the Mississippi River all the way to Lake Michigan on behalf of decent health care for everyone. I don't think you take a holiday from decent health, particularly public health.

The best way to have a productive economy is to have healthy educated workers. I think it's a large part of our economy.

So, the federal government and the state government have a partnership in Medicaid. We need more help from Washington to protect against job cuts and health-care cuts. That is why almost all of the governors are for enhancing the Medicaid match

for a couple of more years. If we don't do that we are following Herbert Hoover economics. And Herbert Hoover economics doesn't put America or Illinois back to work.

MR. MURRAY: Do all of you agree with that, more money from the federal government even though it doesn't have the money to send to you? Yes, sir.

GOVERNOR FREUDENTHAL: I don't agree with that. It's going to take a modification of the expectations of the public of what government does. So far this discussion has been about how have we scraped and adjusted to maintain the capacity to meet the public's expectations about funding.

Now you put the other option on the table, which is: states go to the federal government to find money to meet the expectations whether it's health care, roads or anything else. So, what we have as states in effect is we are dealing with a historical pattern that each state developed with regard to what it was going to fund and how it was going to fund it, whether it was going to fund it from

debt or from federal funds.

So, to me . . . it seems to me that we are avoiding the basic question which is: each of us has to figure out some way to pare back the public expectation of what government is going to pay for or we continue to sort of sweep funds, go to the federal government, go somewhere.

MR. MURRAY: So, what do you do then? We already have 40 million plus people that don't have health care insurance. Who are you going to tell you no longer get Medicaid?

GOVERNOR FREUDENTHAL: I think where you are going to end up is you are going to have to trim back what Medicaid provides to a more basic set of services.

MR. MURRAY: And make people pay more themselves?

GOVERNOR FREUDENTHAL: Make people pay more themselves. It's all of that stuff that your Momma told you about someday you've got to be responsible for yourself.

We are not in any danger of doing that

in this society.

MR. MURRAY: Did you know my Momma?

GOVERNOR FREUDENTHAL: I thought she was a delight. It seems to me that this whole discussion, and I've been through a lot of these redesigning government discussions, they all come down to how do we deal with the supply side of services.

We never talk about how are you going to deal with the demand side. That is the public expectation. We assume that the expectation is there because of our obligation to meet it. I don't think you can survive.

MR. MURRAY: Governor Quinn you say health care is a right, but how much the individual pays for his or her health-care coverage is certainly a flexible figure.

GOVERNOR QUINN: I think we'd save a lot of money for the American taxpayer by having a more efficient system with less monkey business by big insurance companies and HMOs. That is why I have supported the President's health-care reform.

Our state had more health insurance rescissions than California. What is a rescission? Some little girl at eight years old gets braces. It isn't on the form that she applies her insurance. Then when she gets pregnant years later the insurance company knocks her off the rolls.

The federal government has passed a law to protect against this kind of insurance abuse. I think it is important to protect the health care of people who work and live from paycheck to paycheck.

MR. MURRAY: There are projections that show if you leave this in the federal government's hands without major changes in cost growth, you are looking a few decades down the road the federal government going from 20 percent of GDP to 30 percent of GDP. Maybe that's inevitable. Maybe that is something you're all comfortable with.

But I guess the question I have: Is there anything that you can do as governors dealing with just one state to fundamentally change the health-care cost equation? Who thinks you can?

GOVERNOR [Jack] MARKELL: I think there are

things we can do. I also think this is probably the single most complicated public policy issue we face. It is as important as education and transportation as the other issues are, and I think health care is the most complicated.

Certainly, we can focus on wellness and prevention, incredibly important. We can focus on the administrative costs, which people generally recognize or expect to be somewhere between 25 to 30 percent.

But at the end of the day it does seem to me that until we figure out some kind of replacement for the fee-for-service model where the entire health-care system is compensated based on providing more procedures, more visits and the like as opposed to being compensated . . .

MR. MURRAY: Can you do that at the same level?

GOVERNOR MARKELL: I don't know.

And I think it is something--we've had conversations. I think it is certainly something we have got to at least try to figure out. There have been places which have piloted and have had some success. We've

got it figured on Vermont being one. We've got to figure out how we scale it up.

CHAIRMAN DOUGLAS: We have had success, Alan. We reduced our Medicaid costs by about a quarter of a billion dollars over the last five years. And for my colleagues from larger states that's a lot of money for us.

We've done it by asking the federal government successfully for a super waiver to give us flexibility in how we administer the Medicaid program.

My complaint about Medicaid historically is that it's not a health-care program. It's a sick-care program. It just pays for things after the fact.

But we've got permission to use these dollars for preventative care to make incentive payments to physicians who provide high-quality care. As a result, we are seeing some real savings. So, it can be done.

The federal government has to give us more flexibility. And in addition to our request for

a couple of extra quarters of enhanced Medicaid match, we've also asked for a relaxation of the so-called maintenance of effort so that states can have flexibility to design the programs in a way that works for them.

MR. MURRAY: Which is more important to you, the money or the flexibility?

CHAIRMAN DOUGLAS: Well, we always say give us one or the other. This is a short-term request, two quarters for additional Medicaid support during that time we are recovering from the Great Recession.

MR. MURRAY: It's money now and flexibility later?

CHAIRMAN DOUGLAS: Correct.

MR. MURRAY: Governor Herbert?

GOVERNOR [Gary] HERBERT: Thank you. As one of the new governors on the block, I really do look at this as an opportunity for states that should have been at the table in the beginning of this discussion and taken the lead.

My dismay was that we were kind of the

last ones brought into the discussion. I think that really states have a responsibility and an opportunity in fact to lead the way on health-care reform, whatever the definition of health-care reform is. I think it means different things to different people.

For a lot of people in Utah, it's just lower costs. For others it's universal access, single-payer systems. There's a lot of different definitions out there that are being wrestled with. And we come out of Washington, DC, with a one-size-fits-all approach.

Whereas I would rather see 50 states out there, laboratories of democracy trying to find their own ways to solve those health-care reform issues. And in Utah, we do have one of the health-care exchange windows that are out there that's having some success in bringing competition in a private sector setting with a defined contribution as opposed to a defined benefit for employers. Where employees can go to a portal on the Web and match up their needs with what is available

in the marketplace with a defined contribution.

I don't think it solves all of the problems, but it is a step down the right road. I think it will give us competition in a private sector setting. I think that will help us to keep costs down and help give us access to health care.

My dismay is the states have not been from the very beginning at the front of this discussion helping lead the charge with goals and objectives set out by Washington.

MR. MURRAY: Governor Beebe?

GOVERNOR BEEBE: At the risk of redundancy, I want to tag onto what Jack Markell said. I truly believe that the single most significant thing that has not been done, at least on a wholesale basis, although as Governor Douglas points out, it has been successful in some areas is the systemic change in the way we pay for this stuff.

The systemic change most basic to a long-term resolution of some of these spiraling and escalating health-care costs is changing the way we pay for it and changing the whole fee-for-service

model.

It is absolutely fundamental for both getting a handle on the cost, but I think it is also helpful for quality.

MR. MURRAY: And you think a state can do that on its own?

GOVERNOR BEEBE: I think a state can do that. And as far as I'm concerned, it's much like other things. The federal government can lead, follow or get out of the way. I think that that is where you are seeing more and more governors go.

Now we are hamstrung to some extent. To the extent that you've got requirements, and that's the reason you are hearing some folks say, and I know Dave believes this, that we've got to get a handle on costs. And we can't be hypocrites about this and ask the federal government to bail us out of everything and then still cry deficit spending.

You can be too hypocritical or you can be hypocritical—period--about any of that. I think Governor Douglas's point was a very short-term fix for a very short period of time to help get through

a problem that the states didn't create to begin with--with regard to increased access and increased demands on our Medicaid budgets is a short-term solution.

The longer-term solution is a systemic change that has already been talked about. I think states can do it. And ultimately I think states will do it. But part of that requires a little bit of flexibility that Governor Douglas was talking about.

MR. MURRAY: Governor Baldacci?

GOVERNOR BALDACCI: Just to follow along with Governor Beebe, whom I agree with. The federal government penalizes us every time we cut Medicare or try to refashion it. They take away three dollars for every dollar that we save. And we don't get the benefit of the savings. So, there is no incentive for savings.

So, in establishing a partnership in

terms of reworking it, the flexibility and the maintenance of effort, if we did have that, I'm sure that we can compensate for the lack of revenues that we are looking for to some extent if it were phased

out so that we'd be able to be in a better position.

MR. MURRAY: I have to say as a casual listener who doesn't spend all of my time with you folks, the message that you hear on the outside is much more about give us the money than it is about give us the flexibility.

GOVERNOR BALDACCI: But we cut because of shortfalls, but we have to cut $300 million to get $100 million in state savings. And we've just damaged probably more of the economy because of what we have just done. And there is no sharing of that savings with the federal government so they don't have incentive. That's the flexibility of maintenance issues we are talking about.

MR. MURRAY: Governor [Bill] Ritter?

GOVERNOR RITTER: Just from the perspective of what states can do, we had the CEO of IBM. We had a health-care economist David Cutler and then Kathleen Sebelius. They all said the same thing that data was crucial to this. So, the state, for instance, can pass legislation, which we've done in Colorado, that requires an all peered database, so you

really have a sense going into the data to see what people are paying.

Where the federal government comes in again is that's not all that good if you don't have any access to peer information around Medicare. So, here the federal government has the database we need access to, and why you are going to have shared solutions to approach that.

The starting point has to be for the state willing to go in and do the hard work of gathering the data and then trying to glean from that data where the savings are.

I think what your first question was about, that is a short-term thing. Thirty states have balanced their budgets using that promise of an extension. But by and large to really solve this over time, if you look for us back to 1992 no other part of state government spending has increased as rapidly as Medicaid.

So, it is important for us to get our arms around that. We are not going to do that without cost containment being part of the health-care

strategy. I think states have an absolute responsibility to start that conversation by gleaning whatever information it can to see where cost containment can come from without an impact on services.

MR. MURRAY: I just want to be clear. Many of the states knew at the time that they passed their budgets that that money probably wasn't going to come.

GOVERNOR RITTER: I don't know that that is accurate. You have the Speaker of the House. You have the Majority Leader, the administration, including Secretary Sebelius saying the House passed a version that included an FMAP extension. The Senate passed a version that included an FMAP extension. I think there was a great deal of reason to hope and believe that there would be that extension. One or two votes shy of getting there.

So, I don't really agree that states should have known it wouldn't have come.

MR. MURRAY: Governor Rounds quickly and then we will leave health care, because I know

you guys have already spent a lot of time on it.

GOVERNOR ROUNDS: One of the reasons you are probably hearing a lot of the discussion on health care is because it is such a huge part of our budget.

If you take a look at a lot of the of the other states that I think are similar to ours, if you looked at what education was in South Dakota, it is 49 percent of my general fund budget.

Medicaid and the associated costs involved with it is about right at $.36 but it didn't used to be that high. Most of us are still suffering through with revenues that are at about the 2008 or less level, and yet at the same time our budgets are going up.

Last year my budget went up in one area only and that was Medicaid by $50 million on $1.1 billion general fund budget.

MR. MURRAY: Governor [Chris] Christie, you talked last night, I gather. I wasn't here, but I've seen the reports. You talked about public employee benefits and the need to wrestle with that problem.

Does that rank on the same level with what we've been talking about here, health care? And is that one of those things that you can do? Is it something that inevitably divides Republican governors from Democratic governors because of voting patterns? Why is that so important?

GOVERNOR CHRISTIE: Because in our state, as Governor Douglas said, they have the second highest property taxes in America and that is why he thanks me.

If you are talking about affordability in the state, there is a finite amount of money--which is getting smaller and smaller--that is going to be raised by taxes because of the economy. And the public doesn't care whether you call it an income tax, a sales tax, property tax. All they know is they are paying it.

From our perspective in New Jersey--

having the highest property taxes in America--the idea that there has been one sector of our population that has been completely and totally shielded from the recession is, in my view, an issue of financial

fairness.

MR. MURRAY: That one sector being?

GOVERNOR CHRISTIE: Public sector unions.

MR. MURRAY: Across the board, teachers, firefighters, across the board?

GOVERNOR CHRISTIE: Yes. Because in an era over the last few years was 0 percent inflation. We have had average increases in teachers' salaries in New Jersey between 4 percent and 5 percent.

We have the overwhelming majority of teachers in New Jersey who pay nothing towards their health care, zero from the day they are hired until the day they die, themselves and their families. We have the highest-paid police officers in America. We have the highest-paid firefighters in America. And their salaries continue to increase.

So, if you're looking for a divide, I don't think it's a Republican/Democrat divide. It's a divide between the public sector unions and the private sector unions. Because in my state, you've got 35 to 50 percent unemployment among the private

sector unions, carpenters, pipefitters.

MR. MURRAY: Does anybody disagree with this?

GOVERNOR [Stephen] BESHEAR: Let me just say that this isn't a partisan issue because I think all of us have dealt in one way or the other with public employee pension benefits, health-care benefits.

In Kentucky, we passed pension reform that affected the pension benefits of every new hire. It's a lot more difficult, and we've got a constitutional issue about affecting the benefits of current employees that way. But we reduced the benefits of all new hires.

We negotiate every year a new health-care contract, and we don't have public employee unions in Kentucky. But we sit down with the employees and work through with the amount of money we've got what the benefits will be. And the amount of money this year is going to be much less than it was in any previous year. We will sit down and we will work out the best plans we can have.

GOVERNOR MARKELL: The entire

conversation so far has basically been focused on cuts. Everybody here has spent the last couple of years cutting. In Delaware, we've had to reduce significantly the number of people who work for the state. We've had to move out of leased real estate. We've had to renegotiate leases. All of our state employees took a pay cut last year.

So, it has been cut, cut, cut. And unfortunately we are going to be constantly in this mode of trying to be more cost effective and more efficient.

But we also know that we are not going to be in a position to cut our way to a prosperous future. We are not going to be able to tax our way to a prosperous future. And in the end, the only way out is to improve our economic climates so we create better and more jobs.

MR. MURRAY: Let's talk about that, and Governor Patrick, you made the same challenge. A crisis is also an opportunity. It may be hard to do when you are shrinking your budget, but you don't have any choice.

I'd like to get you to tell me the one thing, not a list of things, just tell me the one thing that you have done as governor that you feel has done the most to get your state where you think it's going to need to be five years from now or 10 years from now for the kind of economic climate that you foresee in the future.

Who wants to take that on first?

GOVERNOR BEEBE: I'll take that on. The single most important thing we've done is what Jack was talking about here--and that is create jobs. Because that is the way we are going to grow our way out of this recession.

Last year, we totally revised all of our economic incentive packages and legislation that allows us to do economic incentives. Before that we could do a lot of things for attracting a new business to move into Kentucky, but once you were there we really said thank you for being here and we are going onto the next one.

Because of the changes, we now can work with our existing businesses and help them

expand and grow and also provide incentives for that. It has created during this last 15 months more economic activity in Kentucky than we've had since the start of this recession.

MR. MURRAY: Are you also saying that your economic incentive spending now is not about trying to grab jobs away or grab plant locations away from another state, or at least not as much about that, and more about trying to encourage?

GOVERNOR BEEBE: We are trying to grow what we have. And we are trying to keep what we have. During this recession it has been just as important to keep the jobs that you have as it is to grow them. So, we are now doing both.

MR. MURRAY: And just very quickly, if you can do it very quickly, how do you do that?

How do you make that change?

GOVERNOR BEEBE: We legislatively revised our incentive packages so that our economic development cabinet can sit down with our existing businesses as well as businesses from out of the state and work with them both.

MR. MURRAY: Governor Herbert?

GOVERNOR HERBERT: I know you are asking for one issue . . .

MR. MURRAY: One thing, yes.

GOVERNOR HERBERT: But I think it is more than one issue. While one issue, I will tell you that four years ago we put together a 10-point plan for economic prosperity in the state of Utah which includes tax reform, natural resources, tourism, investment, research and development, education enhancement with emphasis on math and science and technology.

But we also cut taxes from seven to five. Again, we've created an atmosphere where the entrepreneur can have a chance to be successful. We try to grow from within. And you don't have to incentify people. In fact, you've got a fertile field for the entrepreneur to come and plant his seeds and expect to grow a crop.

So, at least in Utah it seems to be working well. The fact that we did it here four years ago has made it so we have not had as quite the crash

landing that some have had because of that. Again, a key is to create a fertile atmosphere for businesses to prosper.

MR. MURRAY: Let me let Governor [Mark] Sanford in here because he hasn't spoken yet.

GOVERNOR SANFORD: I just wanted to go back for one second to the larger notion of how you create fertile environment whether a company is coming from somewhere else or a company is indigenous to your state. I'll go back to the spending issue, which I know we were trying to leave. But I still think that as states we are just scratching the tip of the surface on the spending issue.

I say that because in South Carolina, for instance, we have seen a fall in the appropriate budget from about $7 billion down to about $5 billion and that's the budget everybody talks about. But that's really one-third of the pie.

The other two-thirds of the pie are fees and federal transfers. And when you include fees and federal transfers, actually we see the highest budgetary year we've ever seen with about $21

billion when you go all in.

I guess it was Churchill's quote that the beauty of the American political system is it always does the right thing--after it's exhausted every other possible remedy.

I think that the same holds true on this notion of government restructuring, government reform, budgetary cuts. None of us want to cut because our constituency will squeal and scream and make noise every time one tries to do so, legitimately, because they are stakeholders in that which they have invested in.

But if you look at what is coming next year as the stimulus funds dry up, it is going to be the mother of all inventive years with regard to government restructuring or tax increases, one or the other, because you really are going to see in all 50 states a real seismic shift as those federal funds dry up.

So, I think that next year maybe an amazing year with regard to states moving towards some of the efficiencies that you've seen in the

corporate world and for instance addressing public pensions.

Public pensions we have not yet scratched the surface on whether state, federal. . . .

MR. MURRAY: You're talking about challenges that still lay ahead. I am still trying to get people to answer the question: what is the one thing that you've already done that you think has had the most affect on creating the kind of environment you want to create five, 10 years down the road?

GOVERNOR SANFORD: I can give you a couple--unemployment security commission reform. We did that this year. Workers' comp. reform, all of those things are things that accrue to the benefit of a start-up in somebody's basement, a mid-size company, a large company looking to relocate to South

Carolina all go to the fundamental sole conditions for business in our state.

MR. MURRAY: Yes, sir, Governor Baldacci?

GOVERNOR BALDACCI: The one thing was energy in our state. We are the most oil

dependent state in the country. Eighty-six percent of our energy needs are imported. So, we've gone more to wind, offshore wind, onshore wind. We've done more renewable energy projects with biomass.

So, we've got a foundation for energy efficiency, renewable energy, domestic energy. And we think it is a national policy that's a winner for jobs.

MR. MURRAY: You're not going to tax those windmills?

GOVERNOR BALDACCI: No, I was very disinterested in what the governor . . .

MR. MURRAY: Did you want to say something? And then Governor Gregoire, and then Governor Rounds.

GOVERNOR FREUDENTHAL: Our

comparative advantage is the export of energy. So, what we've concentrated on is the power lines and investment with private sector in natural gas pipelines and railroads simply because as an energy export state, those are the underlying core infrastructures more so than highways. And the

private sector has been willing to make the investment.

You can see that manifest itself in our current fiscal circumstance because we more than doubled the capacity to move natural gas which has a revenue implication for us, which is one of the reasons we're in pretty good shape.

MR. MURRAY: Governor Gregoire?

GOVERNOR GREGOIRE: You asked for the one thing. I would say that we identified where is our economic future as the most trade dependent state in the nation. We also identified energy.

So, we've invested in research and development. We set a goal of energy jobs of 25,000 by the year 2020. We did an energy portfolio. We did tax incentives. We now are the fourth largest producer of wind power. The largest growing in terms of solar energy, biomass and so on.

Again, the goal of 25,000 jobs by 2020. We surveyed last year and we are at almost 100,000. So, I would say that is not only giving us jobs, allowing us now with China to do some exports

that we heretofore have not done. And we've identified it as a single industry where we can get four more jobs than in any other single sector in the state of Washington.

MR. MURRAY: Governor Rounds?

GOVERNOR ROUNDS: In 2003 we did what we called a 2010 initiative. A business initiative that was designed to be a business plan like a private business. Goal three was to become a recognized leader in specific areas of research and development.

We ended up creating 10 specific research centers and creating 23 new Ph.D. programs. It may sound like you're creating these, but the goal we had was to keep our young people in South Dakota. And that meant diversifying the economy and bringing back in more research opportunities for those kids that otherwise would leave.

I think that is going to change the landscape within . . .

MR. MURRAY: Is it working yet? Do you see it in the population trends?

GOVERNOR ROUNDS: We do. We are

keeping our kids here. The best evidence I've got is that we've got record enrollment in our university systems within the state.

MR. MURRAY: Yes, sir?

GOVERNOR MARKELL: Probably the two most important things we did, first of all, it's really about a change in culture, which is demonstrated by a significant reduction in the amount of time it takes us to respond to inquiries for business to as short as a day for approval. A very predictable, fast timeframe from our department of transportation, our department of natural resources. We know that when businesses are waiting in line and filling out forms, they are not putting the people of Delaware to work. That's one that’s critically important.

Secondly, you cannot overstate how important education is. So, we believe that the race to the top competition is huge. I do want to make sure that everybody else knows that the session, the economic development committee meeting after this one is going to focus on these very issues. That's

an advertisement for that as well.

MR. MURRAY: Governor Ritter, Governor O'Malley, Governor Paterson, Governor Douglas?

GOVERNOR RITTER: Like other states, we really staked our future on 21st century sustainable industries. And for us energy is the lead among them. Also bioscience, aerospace have been significant.

But in energy I have signed 56 laws in four years that have to do specifically with clean energy. It's been for us the ability to create an ecosystem. We joined all of our major research institutes with the National Renewable Energy Laboratory. And with that co-laboratory, market of the state as a research and development center for clean energy that has attracted private-sector research and development. ConocoPhillips is going to build its global Institute for Alternative and Renewable Fuels in Colorado along with Siemens coming there as well.

Then we've seen big manufacturing

jobs come as well. Bestest, its North American plants has 2500 jobs for manufacturing plants, estimates solar building inverters in Colorado. It's the first place outside of Germany in the world that they built them.

Those are just examples of big companies, but also medium and small. So, they are manufacturing. They are about innovation and for our purposes we think that is the way forward for us as a country, but certainly as a state.

MR. MURRAY: Governor O'Malley?

GOVERNOR O'MALLEY: We believe that the most important thing we can do for our economy today and also the economy of our future is to invest in the innovative and the creative capacity of our people.

Last year, we led all the states in terms of job growth in our tech sector. We moved from fourth to second place in terms of biotech. We sit in the corridor of science and technological innovation, the likes of which is unrivaled.

The US Chamber of Commerce says we are

one of the topmost entrepreneurial and innovative state economies among the 50. So, the most important thing we have done is the investments in education of our people and making college more affordable and connecting that innovation to the entrepreneurs that are creating the new opportunities and the new jobs that allow us to have a rate of job growth, which is twice what the nation's been for the last three months.

MR. MURRAY: Governor Paterson one thing.

GOVERNOR PATERSON: One thing that happened in New York that may be a little different is that obviously legislators are very queasy, especially in election years about making some of these tough decisions and creating these cuts.

In New York apparently, we didn't have to wait for a session to have that problem because our budgets were late 25 out of the last 30 years. In that period of time, what the state had done for awhile was just borrow from its own general fund to keep the state functioning until a budget was

passed.

Then we passed a law that would have emergency appropriation that would keep the government running from week to week.

Our budget is the only budget that is passed in April in the country. After six weeks of waiting and realizing that the legislature wasn't going to do anything, we started putting cuts into the emergency appropriation itself.

So, the legislature either had to pass those appropriations or shut down the government. Inevitably what happened was it took the legislators off the hook to make the decisions and placed it squarely on the executive branch. We were able in a series of weeks of doing this to basically pass the budget.

What I think it did was to change the culture because now we've found a way to address the issue of reductions without making people from both parties as politically vulnerable as they would have been.

MR. MURRAY: Governor Douglas,

Governor Beebe.

CHAIRMAN DOUGLAS: Well, Alan, we've had a number of economic and educational incentive packages over the years. But from a fiscal standpoint, for the way we were able to balance the budget without anticipating any additional federal Medicaid money, without accessing our reserves and cutting taxes at the same time, is through something we call challenges for change.

The legislature of Vermont is of the other political party, but realize we had to find a bipartisan solution to get through this difficult time. So, working with a consultant that the legislature hired, we passed this law that reduced the remaining budget gap, which is about 3 or 4 percent and without knowing exactly how we are going to do it. It's a leap of faith.

What we said is we have to fundamentally restructure how we provide services of government. So, we have instituted a performance-based contracting system. We created what we call chartered units where we say to an agency

you don't have to follow the strict rules of personnel and purchasing and other kinds of things in state government. Here's your appropriation. Do it your way.

We are reducing our inmate population through transitional housing and community placements that protect public safety but reduce costs at the same time.

So, we've got to fundamentally rethink how we do things not just go through traditional budget cutting.

MR. MURRAY: Governor Beebe, Governor Fortuno and then I am going to change the question a little bit.

GOVERNOR BEEBE: What I'd like to say is much more macro.

MR. MURRAY: Is it the one thing?

GOVERNOR BEEBE: Yes, it is. But it infiltrates the micro that everybody is talking about. It is the one thing. For us in particular and some of these other folks may take it for granted but we don't. We have imbued a mindset and an

attitude that links education and economic development inextricably to the point that everybody thinks of it just like they think of breakfast now.

When I say that and when I say where I am coming from I hope you'll appreciate this. Governor O'Malley brags about Maryland being first in the education rankings? And he should brag about it; it is something that he should never take for granted.

We are tenth. Who would have believed a few years ago that Arkansas would be tenth in those rankings. What that has done is it has changed both inside and outside of our state the image and the view and the relationship--and it's from high tech. It's from the Hewlett-Packards and the Verizons of the world and all of those jobs to the manufacturing sector where we have created over 25,000 new jobs in the midst of this recession.

It is the combination that Beshear was talking about in increasing what we already have and not forgetting our existing businesses at the same time we try to attract new ones.

It is all of the micro things that everyone is talking about. It's what Governor Rounds was talking about in terms of keeping your people in your state, but you've got to be able to not only educate them in your state but provide those good jobs so they don't go to Atlanta or Baltimore to get a good job.

It is all of the individual things that everybody is talking about. But the one thing--to answer your question--is the relationship between and the understanding that it is education that is the key to economic development. And when I am talking about education, I am talking about cradle to grave. I am talking about pre-K, K-12, higher ed, two-year institutions, adult education, workforce training and retraining.

If you have one single thing that you can point to as a state where you are going to lead this country out of whatever malaise it's in, it is the understanding by your people and a buy-in by your people that the relationship of education of every type and economic opportunity for tomorrow are

inextricably linked.

MR. MURRAY: We are back to education. Governor Fortuno, before I go to you, just for equal time reasons, we know who number one on the *Education Week* list was, and we know who number 10 was. Were any of you two through nine? If you were, raise your hand, because I don't want to leave you out.

GOVERNOR PATRICK: Massachusetts has the top performing student achievement in the Nation for three years running.

MR. MURRAY: Does anybody have anything else to say before we go to Governor Fortuno? Okay. Go ahead.

GOVERNOR [Luis] FORTUNO: We wanted to create the best business climate in the country. We did a number of things. Our permitting process was out of whack. Essentially, we have cut by two-thirds all of the permitting you need to put together whatever kind of business you need.

Secondly, we understood that government would not have the kind of funds needed

for infrastructure development. We approved and are implementing right now the largest most ambitious public-private partnership program in the country.

It's a program. It's not two or three projects. It's a whole program in every single area you can think of.

Thirdly, energy--and I agree with some of my colleagues--energy is key in our case. Forty-five percent of our economy is manufacturing. So, just imagine how important the cost of energy is. And we live on an island. Ask Governor [Linda] Lingle in Hawaii or others. It is very tough to produce cost-effective energy.

We are moving in that direction with portfolio, tax incentives, and what have you. Finally, because of all of the tough decisions we made last year, we are cutting taxes across-the-board at corporate level across the board this year.

MR. MURRAY: I want to change the question a little bit. I'm sorry, Governor Camacho, go ahead.

GOVERNOR [Felix] CAMACHO: For our

territory, we are so distant and remote and very much a micro-cousin as compared to the many states.

Our mainstays have been tourism and the Department of Defense with military installations there. I tried to implement changes by investing in infrastructure, by building schools, investing in our community college, our university, our seaport, our airport, water power, wastewater, roads, landfills which have provided jobs in construction and the service industry.

So, we would invest in foundational type of investments that would allow for growth in the future. Also trying to deal with the many long standing issues of lawsuits, entitlement type lawsuits against the government. Unfunded federal mandates and the like that have really haunted us for decades and trying to deal with the many fundamental issues. But it was mostly foundational types of approach that I've taken in my two terms to try to build for the future.

MR. MURRAY: Governor Brewer, I am going to get you in here before we move on. I am going

to ask you to tell me one thing, but I am going to acknowledge that we've heard two, three, 10. I give up. You can tell me as many things as you want to tell me.

GOVERNOR [Jan] BREWER: Thank you. Having been governor just a little bit over 500 days certainly was a challenge when I came in, because we were facing the largest deficit that the state of Arizona had ever faced in its history. So, we began certainly first and foremost by trying to get our budget balanced, which I think is very, very important to the business community to know that you have a stabilized government. We did that.

We have a structural deficit going into the next year. Certainly we did a yeoman’s job considering the fact that we had about a $8.2 billion revenue stream with a $10.3 billion cost of budget.

So, we did get the budget balanced. We went out to the voters for a temporary sales tax of which they responded overwhelming in the state of Arizona to give us a one cent sales tax increase for three years. And it passed by 64 percent, which again

helped us get through the bad times.

MR. MURRAY: And they did it to pay for?

GOVERNOR BREWER: Education and public safety, which is very, very important to me. Because you understand it’s at the top of everybody's issues in regards to jobs. That leads me to where we are at today. I think it is very, very important.

And we have addressed probably everything in those 500 days that you've all talked about. We've been on it and we've been successful. I'm very, very proud of that.

The bottom line is I think is business needs to know that they have a stable government that they have a well-educated workforce and then it was one of my big goals is to make it easier to do business in Arizona.

That meant to me putting a moratorium on all rules and regulations and helping the people that are looking to come to Arizona get through the red tape and the green tape. To reach out to them and to help those businesses that are already here

in Arizona so it can be stabilized. We have been successful.

We have brought over a billion dollars worth of capital assets into the state and thousands of jobs. We are proud of that. In 500 days, we have accomplished a lot.

MR. MURRAY: And for you, has this immigration mess been a distraction from that agenda? Because that is very clear focus, five points, this is what we want to do. Did you know it was going to be this big?

GOVERNOR BREWER: I did not know it was going to be this large. I knew that it was going to have a tremendous effect, of course, in the state of Arizona. But I think the people throughout the country realize that what happens here in

Arizona affects their states too.

It's an impossible situation they're living with. The feds aren't doing their job. If they're not able to do it, then we in Arizona feel that it is our responsibility to step up and help them do it.

MR. MURRAY: If you had a do-over, would you say, "Well, I think I'll put that one off and focus on . . ."?

GOVERNOR BREWER: Absolutely not, absolutely not.

MR. MURRAY: A different question now, and this time I am going to hold you to one. I'd like each of you to tell me the one thing that you didn't do that you really wish you had. A lot of you are leaving office this year or early next year and will be succeeded by someone else. Maybe the one thing you wish you had done and that you hope your successor does do.

Some of you will be back for more punishment. So, it might be the one thing you haven't been able to do. But again, the one thing that you have not done that you wish you had done to put your state in the position it needs to be for the next five or 10 years. We are running out of time this time. So, I'm really going to keep you to one. Governor Brewer you go first.

GOVERNOR BREWER: I think the one

thing that I wish that I could have given more of and that would be tax reform. I think that is really, really important. And that is on my agenda. And we are going to move forward with that in respect to jobs.

MR. MURRAY: Who wants to go next? Yes, sir, Governor Douglas?

CHAIRMAN DOUGLAS: Control property taxes. As I indicated earlier, they are very high. It's tough for a lot of families where our incomes are below the national average to find a decent place to live. We have the lowest vacancy rate in rental housing in the country and very low for owner-occupied as well.

We've seen a decline in our student population of about 13 percent over the last decade but property taxes and local school spending keep going up. So, that needs to be addressed.

MR. MURRAY: Governor Sanford?

GOVERNOR SANFORD: We proposed eliminating the income tax in South Carolina. We were unsuccessful in that. I think because we had

that larger debate, we were able to cut the marginal income tax rate for the first time in our state's history. We cut it from seven to five for LLCs, partnerships, etc.

So, it was a step in the right direction. But if you really want to free entrepreneurial talent, I think you better go to the root cause, which in part I believe is income tax.

MR. MURRAY: Get rid of it all together?

GOVERNOR SANFORD: Yes.

MR. MURRAY: And to what extent is that about your competitive position vis-a-vis other states? Because all of this I think is worth focusing on in the last few minutes that we are discussing.

We know what the situation of this

country is the degree to which we relied on consumers has racked up large deficits we have imported from the rest of the world. If you are going to turn that around in the next 10 years as a country we have to export. It can't be about moving the jobs around.

GOVERNOR SANFORD: We buy wholly into Thomas Friedman's notion that the world is flat. You've got six and a half billion people scattered across planet earth, and capital is fluid. It is going to go to places that in essence will reward or encourage it.

So, it is all about looking at a state like Florida that has no income tax. It's looking at Texas that has no income tax.

MR. MURRAY: That's why Lebron James went down there, didn't he? One thing?

GOVERNOR QUINN: I think the most important thing is to empower the voters, strengthen the voters. I believe in initiative, referendum, recall. We have recall on the ballot in Illinois this year. I would like to see more opportunity for consumers and taxpayers to enact laws by direct petition and referendum.

MR. MURRAY: I wish Governor Schwarzenegger were here because they have that power out in California and it created a mess. Does anybody disagree with that? Who wants to take it on?

Governor Gregoire?

GOVERNOR [Chris] GREGOIRE: Well, you get the situation I referred to earlier. When you have a vote of the people, it may look appealing on the ballot to vote for reducing class size and increasing teachers' pay but it isn't free. There was no revenue that came with it whatsoever.

MR. MURRAY: Do you feel like you are being anti-democracy?

GOVERNOR GREGOIRE: By no means; by no means. I just think that the same scrutiny that goes into the legislative process ought to go into the initiative process to include vetting it publicly--the pros and the cons, asking how are you going to pay for it, putting a fiscal note on it, doing all of the same sort of rigor that you do in any other formal legislation.

Just by virtue of the fact that it's initiative, it still ought to go through that same process.

MR. MURRAY: Do you have something to say on that point Governor Fortuno?

GOVERNOR FORTUNO: I believe we must make government responsive to our constituents. One way to do that is through e-government. I believe we can do a lot more there. We don't discuss it that much.

MR. MURRAY: I'm sorry, through what?

GOVERNOR FORTUNO: E-government; in Europe and other places they really have come a long way. I believe we can do more. We have an initiative, but I want to do a lot more there.

MR. MURRAY: To get more response.

GOVERNOR FORTUNO: Exactly, so people from their homes or businesses can do a lot of what they normally do with government and not even having to move from their desks or homes.

GOVERNOR CAMACHO: In our case, I

think the initiative that we have undertaken but have yet to complete is with the information technology. There is a lot of data and information out there, but harvesting that data and insuring that it is properly gathered and used to make informed decisions I think is critical.

So, we've undertaken major initiatives in trying to develop the architecture for government, but I hope my successor completes that. Again, with data information that is accurate and efficient, you can make informed decisions.

MR. MURRAY: Governor Paterson, the one thing that you didn't do? You are one of the governors--It's a record year, by the way. We know at least 24 governors will be out of office. You will be gone. What is your one big regret, the one thing you wish you had done that you didn't do?

GOVERNOR PATERSON: Appoint myself to the U.S. Senate.

MR. MURRAY: The most insightful answer of the day. Somebody will follow that. Go ahead, Governor Ritter.

GOVERNOR RITTER: In my case, I wish I would have found a scheme for actually funding higher ed that is a dedicated scheme of some kind, simply because we do think it is so tied to economic development. And in deep, deep recessions like this it is very vulnerable, higher education is.

It is not caseload driven. We spend 97 percent of our budget on five areas. So, the two areas that aren't totally caseload driven K-12 and higher ed. And higher ed is the more vulnerable of the two, and they take such a hit.

So, you are doing something very counterproductive to economic development in the long-run to make it through what seemed like a short-term recession. It is longer than I think most people thought it would be. We need some schematic in our state to make sure that we adequately fund higher ed.

MR. MURRAY: Governor Beebe, you can go now.

GOVERNOR BEEBE: I wasn't going to

tell you anything. I didn't want to follow Paterson.

The one thing I regret, and hopefully will finish it given the opportunity, we didn't completely remove the sales tax on food. We were one of those states that taxed food to the highest extent of our regular sales tax. It was 6 percent. They've been

talking about it for 50 years, Republicans and Democrats alike, from Huckabee to Clinton nobody ever did it.

We knocked four of the six off, and it took two years to get it done. We're down to two cents. I regret we haven't gotten rid of the two cents, but hopefully we are not done.

MR. MURRAY: Governor Heineman?

GOVERNOR HEINEMAN: Hopefully, I'm going to be around for a few more years, but I would say this. We passed the largest tax relief package in the history of the state. We still need to lower taxes more if we are going to be competitive in the job market both domestically and internationally. So, it's lower taxes.

MR. MURRAY: Can you afford to do that?

GOVERNOR HEINEMAN: Can you afford not to do it, Alan? I think you have to.

MR. MURRAY: Governor O'Malley?

GOVERNOR O'MALLEY: The one thing I wish I had: the flexibility to do more of has targeted

tax credits for innovation, the R&D tax credits, the biotech tax credits. The things that are in our strength as an innovative economy. I think those have ripple effects. I think they pay themselves back.

We have increased it somewhat, and I think those were one area.

MR. MURRAY: You don't worry that that gets the government into picking and choosing industrial policy, distorting economic effects if you have tax credits for certain activities and not for other activities?

GOVERNOR O'MALLEY: I think if you do a survey of your state and do it in an honest, open and transparent way, you can identify what your competitive strengths are. And any business invests in their competitive strengths. It makes them stronger and allows you to make the tide rise for service industry and other things not even connected to it.

We've been very successful in that. It hasn't hurt us. In fact, that is why we had the

rate of job growth that is better than most states in those sectors.

MR. MURRAY: Governor Patrick, did you want to respond to that or do you want to tell me the one thing?

GOVERNOR PATRICK: I want to build on that point because I hear this argument all of the time. I think we ought to have, as a couple have said, a robust and modern and above all simplified tax system to encourage business development.

I think playing to your strengths and our strengths is unique from state to state and also reflecting that focus the tax policy is right. We have a life scientist initiative here, $1 billion initiative over 10 years. It has some targeted tax incentives as a part of that initiative. And it is one of a handful of innovation industries and is the reason why we have not gone as deep into recession as the rest of the country and why we are coming out faster than the rest of the country.

Clean tech is another area. IT is another area. These are areas where we have this

whole innovation economy is a sweet spot for us here in the Commonwealth, and it's what we have focused on. And it is why, I think the Philadelphia Fed reports that we are outperforming 48 other states.

MR. MURRAY: And while you have your microphone on, the one big regret?

GOVERNOR PATRICK: My one big regret is this; although, should I have the honor will get to this in the second term.

We spent a lot of time and effort trying to address concerns that businesses raise about one-stop shopping when it comes to dealing with state government. Someone who takes them by the hand and walks them through a simplified regulatory process. We made a lot of good progress there.

But it turns out poor people want the same thing. They want one-stop shopping. When they present for human services needs, they don't want to have to be sent to multiple different offices. They want the same simplicity in dealing with their government.

I think Governor Fortuno's point

about e-government is one way to respond to that. But for a lot of those clients, their access to the Internet compromises that idea. So, I'd like simplification for the regular person in the same way we are trying to deliver that for businesses.

MR. MURRAY: Governor Christie?

GOVERNOR CHRISTIE: I've been here six months, Alan. I don't have a lot of regret.

MR. MURRAY: What's a big one for next year?

GOVERNOR CHRISTIE: The big plan for next year is for New Jersey--given that we are so noncompetitive from a tax perspective--is to continue to reduce spending in a way which is going to allow us to become more competitive with our neighboring states, Jack's state, Pennsylvania, because we are not.

We have to be on a long-term plan over the next four years to be able to do that. We dug this hole for ourselves. Put aside the national recession, our policies that we picked in New Jersey over the last decade, we dug this hole for ourselves

and we are going to have to dig out.

MR. MURRAY: Governor Markell?

GOVERNOR MARKELL: One of the most frequent concerns I hear from small businesses, especially throughout the state, has to do with inability to access credit in any kind of affordable way. While we did create a program that has facilitated that to some degree, so far we have not been able to take it to scale. That is one of the things I'd like to focus on.

MR. MURRAY: Who haven't we heard from? Governor Herbert.

GOVERNOR HERBERT: Like Governor Christie, I haven't been here that long. It's been about a year since I've been inaugurated, so I have no regrets. I think we are doing what we need to be doing in Utah.

What I have learned here has become self-evident that every state has unique challenges, unique opportunities, and need to find unique solutions for their own particular situation.

We have states that have very little

public land. Some of us in the West have a lot of public land. We are blessed with natural resources, and traditional fuels make it a little more difficult for us to be on the renewable side as the only source of energy.

I have a state that is one of the fastest-growing states in America and has the highest birthrate of anyplace in America. So, my education challenge in paying for education is way different from some of the other states.

Some have in-migration. Some have an out-migration. Border state challenges, inland state challenges, they're all different.

The challenge for me--and I think for all of us going forward--is to express to our constituency what we are in fact doing to address those unique challenges.

We sometimes get drowned out by what is happening in Washington, DC, and some of the national challenges. And people don't realize they may be national challenges, but they may be not the same unique challenges we face as states.

So, I will end up where I began. I think we need to be taking the lead on a lot of these issues. I believe in federalism. I believe there should be a balanced approach as to how we govern in a state with Washington, DC, having a role, but states having a balance and a counterbalance to what is happening in Washington, DC. This organization I think is an organization that can really lead our governments in our unique ways.

MR. MURRAY: Let me just follow up on that and get a few people to weigh in before we go here. I don't want to go back to health care. We've covered that pretty thoroughly what you want from Washington and don't want from Washington in terms of health care.

Health care aside, health care aside, what is it that you'd like to see from Washington that would make your jobs better, would enable your state to do what it needs to do over the course of the next five to 10 years? Governor Freudenthal?

GOVERNOR FREUDENTHAL: I follow on my colleague from Utah's point. The point of view

of people who have public lands what we'd like is a lot less attention from the federal government and a lot more capacity to actually integrate the development of those properties with the remaining economy of the state. It's like living with a 900-pound gorilla that just flails around.

MR. MURRAY: Anyone else?

GOVERNOR SANFORD: Sustainable fiscal policy out of Washington. I think that that is the giant elephant in the room when you think about policy in Washington because the store of value of one's currency at this point is eroded based on international expectations. I think of what comes next --

MR. MURRAY: Interest rates are low,

currency is still holding up pretty well.

GOVERNOR SANFORD: For the time being. I think that there's a lot of contingent liability, if you want to call it that, from the standpoint of us as states being able to trade with a whole bunch of other places around the world based on the trajectory role in Washington.

MR. MURRAY: Let me get Governor Baldacci.

GOVERNOR BALDACCI: The one thing would be flexibility out of Washington, true flexibility and true partnerships with the states. I think we can help them to solve a lot of problems. We don't need the money as much as we need the flexibility, because they don't.

MR. MURRAY: Some people really want that money.

GOVERNOR BALDACCI: I understand that, but if the trade-off is the flexibility, we can make up the money over the longer term. But it really is true flexibility with all of the different regulations.

MR. MURRAY: Governor Ritter?

GOVERNOR RITTER: It sort of follows what Governor Markell said. It's access to credit for small businesses. And we've made this point both in governors' meetings and privately. Regulators have made it very difficult for small businesses to get access to credit even when it seems like they

should, given their history.

We appreciate the need for different types of regulation and financial system, but it feels to me like they crimped the system in really the wrong place. A state like Colorado heavily relies on small businesses for our economy. They are a very big part of the economy, and yet it has crimped our ability to grow because there's just not access to credit.

We put together our own program. It is called a small loan reserve. And it works but it works at this minor scale compared to what the federal government could do if in fact they appreciated small businesses, the role that they play in the economy. And the regulators taking a more rational view towards the need for them to have access to it and not to over regulate or to over crimp it in places they shouldn't.

GOVERNOR [Phil] BREDESEN: I agree with everything that has been said on the access for small-business, the credit access. But I would add that the transportation investments, the

infrastructure investments, the things we used to do as a major league country that our competitors in China and Europe are doing, we've got to make those investments in our infrastructure in order to have a better future for our kids.

GOVERNOR MARKELL: Opening up as many export markets as possible.

CHAIRMAN DOUGLAS: No unfunded mandates.

GOVERNOR CAMACHO: In our case, I speak for the ancillary areas or the territories that there be equality or equity. Many times there are federal programs in Medicaid, Medicare, pre-existing conditions that is currently existing with this health-care reform that apply to the states but not equally to the territories. So, there is inequity in federal policies as they relate to territories.

MR. MURRAY: We've crammed a lot of information into an hour and a half. I'm going to ask you one last question by show of hands: Given all the pain of the last couple of years, if you had to do it all over again would you do it? We've already

heard from Governor Paterson on this, but the rest of you if the answer is yes let me see your hands up.

It is slow, but they are getting there. They're getting there. Thank you very much. I've enjoyed it.

CHAIRMAN DOUGLAS: Alan, thank you so much. And thank you colleagues for your participation. As Governor Markell said, the economic development committee is going to continue perhaps on some of the same themes at 3:00 p.m. So, please join them.

We are adjourned.

(Plenary session adjourned at 2:37 p.m.)

COMMONWEALTH OF MASSACHUSETTS

I, LAURIE J. JORDAN, do hereby certify that the foregoing is a true and accurate transcription of my verbatim notes, to the best of my knowledge and ability.

WITNESS MY HAND, this 14th day of July, 2010.

Laurie J. Jordan

Professional Court Reporter

NATIONAL GOVERNORS ASSOCIATION

SUMMER MEETING

Sunday, July 11, 2010

THE FEDERAL BUDGET DEFICIT: RISKS AND CHALLENGES

GRAND BALLROOM

SHERATON BOSTON

39 Dalton Street

Boston, Massachusetts 02199

PARTICIPANTS:

GOVERNOR JAMES H. DOUGLAS, VT, CHAIR
GOVERNOR JOE MANCHIN, III, WV, VICE CHAIR

GUESTS:

FORMER SENATOR AL SIMPSON, CO-CHAIR, NATIONAL COMMISSION ON FISCAL RESPONSIBILITY AND REFORM

ERSKINE B. BOWLES, CO-CHAIR, NATIONAL COMMISSION ON FISCAL RESPONSIBILITY AND REFORM

P R O C E E D I N G S

(9:47 a.m.)

CHAIRMAN DOUGLAS: We'll get the final plenary session under way. We've got two distinguished guests to talk about an important topic. And we'll also, of course, handle the reports and recommendations from our committees and the elections of next year's executive committee and officers.

So, please find a seat, and we'll get our session under way.

We're honored this morning to have Senator Al Simpson and Erskine Bowles, who are the co-chairmen of the President's Commission on Fiscal Responsibility and Reform. They're going to talk about the fiscal challenges facing our nation and the types of options that we need to consider to reign in our federal deficit. They haven't been given an easy assignment. I think that's an understatement, but we're grateful that they've undertaken it.

Everyone here is well aware that not since the end of our Second World War, when our ratio of federal debt to GDP peaked at about 109 percent have we experienced debt burdens that threaten the economic future of our country. At that time, we were able to grow our way out of the debt crisis. But given current global conditions, that prospect is not as likely today.

Our federal debt to GDP ratio ranges throughout the second half of the last century between 25 and 50 percent. It's now up to 62 [percent]. But the GAO projects that if we maintain our current spending habits and do nothing about it, we'll surpass the high we set in 1946 within a decade and approach Greece's current debt to GDP ratio, which is about 115 percent. That's obviously not a formula for long-term economic success. And the commission faces a daunting challenge in suggesting a path forward toward fiscal responsibility that is both realistic and politically achievable.

Well, it’s not easy, but something that governors are used to doing. As we’ve said a number of times throughout our meeting, we have to balance budgets on an annual basis. And since we’ve been working through the greatest fiscal crisis since The Depression, a lot of governors have been getting some practice implementing lean government. And we hope that some ideas will come out this morning with our distinguished panelists that will be helpful to them and helpful to the future of our country’s fiscal condition.

I want to call on our colleagues to introduce their constituents, who are our distinguished presenters today. And we’ll start with Governor [Dave] Freudenthal.

GOVERNOR FREUDENTHAL: Thank you. You know, it’s a delight to get to introduce Al. I’ve known him for a long time. We have a very collegial relationship. But if you’ve heard him before, you’re likely to hear it all again today.

Most of you are aware of Senator Simpson. I’ll tell you that I first became acquainted with him when I was 24 years old, working for a Democratic governor in Wyoming, on his staff. And Senator Simpson, then in the Wyoming House, obviously in the Republican leadership, he and Ed Herscher would sit around and plot the course of the state in a truly bipartisan fashion. I would never accuse Al of being nonpartisan, but he does know how to work in a bipartisan manner. I think he's the right guy for this job. He has both knowledge and wisdom.

But he also has a trait which I think is important in politics, which is a sense of humor. You have to have humor in order to get through what it is we deal with and the seriousness with which we take it. So, we're proud of Al; I'm particularly proud that Al's no longer in politics and Wyoming.

You know, Al, if you turn on your hearing aid, you could hear. But we are delighted in Wyoming to claim Al as one of our own. And he is obviously a successful senator, and has done lots of things in his life. But mostly what he does is try to do the right thing by this country and by our state. And so we're delighted--and I think I look forward to hearing you, Al.

CHAIRMAN DOUGLAS: Thank you, Governor Freudenthal. And Governor (Bev) Perdue, would you make an introduction.

GOVERNOR PERDUE: Well, I think we all look forward to hearing Senator Simpson talk too. But I will tell you one thing for sure, you'll love hearing from Erskine Bowles, who is one of North Carolina's strongest leaders.

You all have known him probably in his role as head of the small business administration under President (Bill) Clinton. And then he was the President's Chief of Staff. But after that, we lured him back to his home state where now he serves as the president of the greater university system. He has taken on this role as co-chair of this National Commission on Federal Responsibility and Reform because he believes this.

I've had the opportunity for several years, and for almost a year and-a-half as governor of North Carolina to watch his every moment, his decision making, the fact that he is not just going to talk the talk with us, he has walked the walk right in our own state.

And let me tell you what I mean. As president as one of the largest constituent university systems in the country, we'd like to tell you it's the best, because it is, he has had to cut his own budget. And this is what he's done He has cut $575,000,000.00 out of the corpus over the last three years. The system today is 30 percent smaller than it was when he was sworn in as president five years ago. Twenty-three percent of those cuts came from administration.

I can attest as somebody who loves that system and understands the value of education in the new economy, that Erskine Bowles has not harmed teaching and learning in any way. He has just simply done things differently in lieu of destroying our academic core. He prefers moving the university in the right direction. Even though he and I have laughed and said that’s as painful as moving general assemblies and legislatures in the right direction. But he’s gone forward in lots of critical storms and endured the criticism. And he’ll do that as the chair or the co-chair of this committee.

He’s figured out a different way to incent teachers’ compensation--the professors; the workforce. He’s developed some new paradigms around health care. And he understood that in our state, because we’re one of the fastest-growing states in America, that he cannot rely on the old ways--the bricks and mortar--to educate our people.

And as a result he’s been passionate about distance learning; we now have 135 distance learning degree programs around the world. And I’m told that it’s larger than the University of Phoenix. And so, we have done that very quickly with his leadership.

I believe the best thing I can tell you as someone who calls Erskine Bowles when my ox is in a ditch, I'll say, what would you do? He understands the seat that we're all sitting in. He understands FMAP; he understands jobs; he understands that we've got to continue to grow this economy while we continue to downsize government.

He is great leader. He is great American. And I'm so proud that he's a great North Carolinian. Something that he told me that's the funniest today, because he too, has a sense of humor, Senator, is that he said you know, Bev, when you introduce me, just tell them that I right now I'm the chairman, the president of the university system, but I'm actually between fortunes. I've lost one, but I need to make another one. So, that's what my goal is.

Erskine Bowles, thank you for doing this for our country.

CHAIRMAN DOUGLAS: Thank you both gentlemen, welcome.

SENATOR SIMPSON: Governor Perdue, I wish you had introduced me. It would have been much more charitable. Well, of all the introductions I've ever had, Dave, that was the most recent.

I'll tell you about Dave, he related he was a 24-year-old chief staff guy for a wonderful Democratic governor, Ed Herscher, the longest serving governor in our history--12 years. People look at Wyoming as a Republican state; that's not true. Mike Sullivan Democratic governor, eight years. Gale McGee, 18 years in the U.S. Senate. Ron Colio, 10 years.

Anyway, the thing with Dave, the only thing is his father and mother were our co-chairmen when we ran in '78; we being this woman I've been living with for 56 years--she said living with me was a religious experience--a living Hell!

But Dave has been a wonderful governor, a tremendous force. He's got a lot of guts, takes on the tough ones. And I admire him greatly, and have. And his wife, Nancy, got to know her. She’s a district judge--federal district judge-- and a superb woman from my home town of Cody, Wyoming.

Now, this lasts 10 minutes, so hang on tight, because Erskine and I travel only as a pair. We ride shotgun on each other. It’s a lonely life out there in hostile territory, and all of you know the feeling.

But I did want to address some way, when I walked in here, made a comment and I was taken aback, didn’t have time to respond. I want to respond right now. Yes, I did sleep in this suit. So, I hope that takes that off the table.

I couldn’t have a finer companion in this cause than Erskine Bowles. He’s a man I trust completely, and admire, and respect. He’s a grand gentleman, indeed.

First, a personal note. My dear dad was the governor of Wyoming, and also a U.S. senator, Milward Simpson. He loved the office of governor. He could lead and he could see the results. He said in the Senate, he could never see the results of anything after everything would disappear into the rabbit hole that he was working on, usually from a brilliant staffer on either side of the aisle.

As governor, he loved the fray, and was plenty good at it. And he loved self-deprecating humor. His favorite was this, and he would tell it often: this old guy's out driving his pick-up down the road, got everything in it that he owns, and a highway patrolman stops him. He said you're going a little fast, aren't you? He said no, I can't believe it, who would believe that. You got a lot of stuff back there, don't you? Yeah, mm-hm. Where you goin? Well, he said you are speeding, he said haven't you got a governor on that truck? And he said, no, he said that's manure you smell. And so, the old man got a lot of mileage out of that one.

Now, this commission is one tough goal. I have been addressed as a Republican toady covering for President [Barack] Obama, to get him off the hook. I honor the office of President. If a President asks me to do something to pitch in and help our country, I'll always respond, regardless of party difference.

I think it's called being a citizen of a fine country and doing your share. And in this one, I'm in for my six grandchildren, and Erskine's in for his seven. This is where this one is.

The President has one tough job, as do each and every one of you. But if one is a leader, you take a ton of guff from people who know little and are motivated by what I always said are four great charges--emotion, fear, guilt, or racism.

That's how you pass or kill a bill in the U.S. Congress: emotion, fear, guilt, or racism. Too bad, but that's that way it is. So, I had another word in mind other than guff, but I'll leave it at that.

So, here we go. There are many who

hope we will fail. I can tell you we've met them all. They talk, the conflict is everywhere. Cutting back versus coughing up, those are nontechnical terms. Austerity versus stimulation. Flash words abound. Cut is the best flash word of all, and gut makes two. And then tax is another one. They're all good. But all 18 of us are still in the room together. Good people of deep, deep differences, knowing the possibility of the odds of success are rather harrowing, to say the least.

But I do have the naive belief, and I think Erskine shares it, that we can come up with a plan to stabilize Social Security, and assure its solvency 75 or more years out. But as we address it, the keening wail of cut goes out through the land, or gut. Good heavens, it's . . . if people can't grasp that disability insurance will be unsustainable in less than 10 years, it's grown double since 1980. I won't go into figures, that just makes people's eyes glaze over. But old age and insurance will only pay out 75 percent of its benefits in 2037. It won’t go broke, it’s just going to pay out 75 instead of 100. And that date will keep moving closer with population growth and aging. Unsustainable, unconscionable, and predictable.

But there are many options out there. Over two dozens options out there will work, and we work on them all. And I think if we could resolve that, there’d be a sense of confidence in the land that would be good to portray.

We have Dr. Coburn and Andy Stern, the union member and a very conservative member of the Senate in Oklahoma. Two very good men with sharp minds and sharp knives going over the defense budget without hurting our troops and the mission. Plenty of fat in that baby. And then they say well, we’re probably going to . . . don’t want to touch the defense budget. That’s not true. We’re going to go wherever the fat is. And that will be the tough part.

But here's where we are. Every shred of tax revenue at this point goes only to three things, Medicare, Medicaid, and Social Security. I see Erskine scratching out. He was going to cover that, but I took care of it for him. You'll have to work on it. I'm almost through, Erskine.

And so, the rest of the federal government, including fighting two wars, Homeland Security, education, art, culture, you name it, the whole rest--veterans, the whole rest of the discretionary budget is being financed by China and other countries who are slowly building, and China now has $92 billion of our little IOUs. And we do that, we're just borrowing to do everything but those three items.

Medicare is the monster of the Midway. It's hard for us even to get around it--get our hands around it. But we're going to have to have some trigger in there, some trigger device in there.

Medicaid, boy, you people get the

whole load on that one. The working goofs are at it, one on discretionary, one on mandatory, and one on revenues. We have a fine staff. And with, I think with patience, what we're trying to do first in the commission is establish patience, do our homework, comedy. And the biggest one is trying to establish trust in each other on this commission. That's tough to do in this world, in this country. Trying to lessen suspicion and we're working all that--on all that now.

Well, there, if you thought I was going to go on, I'm not. But we want to hear from you, you're in the trenches. I'd just say one other thing as to the magic flash word of tax. The other day one of the more zealous--a zealot is one, who having forgotten his purpose, redoubles his efforts.

Now, so, one of the great zealots of our time talked about his favorite anti-tax President, Ronald Reagan. Well, I said I knew Ronald Reagan. You're no Ronald Reagan, but I'll tell you, I knew him well. And I quoted the four big tax increases that were done by Ronald Reagan; seven lesser ones; and a total of 132 billion in tax increases under those eight years. And why? To make the government run. And that was his fine eight years as one of our most beloved Presidents. So, for that I will be--then receive mail tonight and tomorrow that I spoke again to raise taxes and put a vat on top of the income tax, plus something else. I don’t know what it will be, but it’ll be a royal hammer blow. And I thank you for listening. But we want to hear from you. Erskine.

MR. BOWLES: As you can see, I have no need for a joke writer anymore. I just steal everything Al says and it seems to work perfectly. I will tell you, Al, I do know one rule of politics that you don’t. And that is always be introduced by someone you contribute to.

GOVERNOR PERDUE: That is not true.

MR. BOWLES: Governor Perdue has been my friend. I have been her supporter. I believe in her. She is strong. She's tough. And by God, she gets the job done. And last night, she signed a balanced budget for North Carolina. And she's got a lot to be proud of.

Al Simpson's the best partner I've ever had. We're trying to do one thing, and that is all this commission to build the same kind of trust with our fellow commission members as we have built among ourselves. And I'm confident that's what it takes to be successful.

In 1997, as some of you know--I know Deval remembers--I negotiated the balanced budget with Newt Gingrich and Trent Lott. And I had to spend months and months and months locked up in conference rooms with them. And you Democratic governors owe me a lot for that.

But we did build up trust. We built up confidence, and we got the job done. And we got it, in the long run, done by looking at what made sense for the country as opposed to thinking about parties.

I'm going to try to just add to

what Al said. I think it’s a fact that as a nation, we face the most predictable economic crisis in our history. This crisis that we just are going through now, many people didn’t predict. This one is as clear as a bell. This debt is like a cancer. It is truly going to destroy the country from within.

And like Al said, it is basic arithmetic. Today if you just look at the mandatory spending, which is principally Medicare, Medicaid, and Social Security, it does consume 100 percent of the federal revenues. That does mean that every dollar we spend on Homeland Security, the military defense, education, energy, infrastructure, transportation, all borrowed and have borrowed from foreign countries. That is a formula for disaster.

Over the next 10 years, spending is forecast to grow by two trillion dollars; 500 billion of that will come from Social Security; 500 million from Medicare; about

300 billion from Medicaid, of which you all participate. And about 650 to 700 million from interest.

By the year 2020, if we leave things on automatic pilot, we will be spending a trillion dollars a year on interest. Just think about that. All that money going somewhere else to create jobs and opportunity somewhere else.

We can’t grow our way out of this. We’ve had every economist you can imagine look at this, and we could have decades of double-digit growth and not grow our way out of this enormous debt problem. We can’t tax our way out. That doesn’t solve the aging problem of America. It doesn’t solve the fact that healthcare is growing at a faster rate than the economy is.

The reality is that we’ve got to do exactly what you all do every day as governors. We’ve got to cut spending or increase revenue, or do some combination of that. If we want to get to a balanced budget by 2020--and there’s no magic about 2020--we have to take one trillion dollars out of the deficit in 2020, a trillion dollars. If we want to get to a deficit to GDP ratio of 2 percent, then we've got to take $675 billion out of the budget in that year alone. Not cumulative between now and then, but in that year alone.

I thought it was interesting as I thought about what I would say this morning, that the, you know, the G20 met two weeks ago in Toronto. And they're dealing with the same exact problems that we deal with in the states. And that is, how can we protect what is a truly very fragile economic recovery. At least it is in our state. And at the same time, slow and then stop, and reverse the rising level of debt that I believe jeopardizes my grandkids' future and our country's standard of living.

And the G20 approved two goals. The first is a relative walk in the park, and that's to cut the deficit in half as a percent of GDP, by 2013. And when you start at a 10.6 percent deficit to GDP, that ain't any heavy lift, believe me. But we should be able to do that. And that's not a heavy goal for the U.S.

What is a very heavy goal is the second one, which was to stabilize the debt as a percent of GDP by 2015. And to do that, we have to get the deficit to GDP ratio down to 2.8 percent by 2015. And that means we have to take, in 2015, $250 billion out of the federal budget. And it's do-able. But it's tough. And I'm going to talk about some of that--specifics.

President Obama I think has made it clear; he's been clear when he's met with Al and me in private. He's been clear, I think to the American people and public. He said that he's going to make recommendations next year that have real budget cuts in them, that will reduce the cost of the entitlements and help restore our nation's long-term fiscal health.

I think there is a canard out there now, that says, well, you can't do both. We can do both. In fact, since the recommendations we're making don't take effect until 2012, we've got about 18 more months of this economic recovery for it to gain a foothold before any of our recommendations take place. So, we think that’s enough time for our recommendations to take place; enough time for us to get the fiscal house in order and then begin to balance the budget.

I thought I would tell you the principles that are going to guide my own decisions on the committee. And Al and I have discussed these, and I think we’re in agreement on most of them. But they’re all pretty simple.

The first is, I don’t want to do anything that doesn’t protect the truly disadvantaged. I think that’s an obligation of government, and one that I’m willing to shoulder.

Second, I think while we balance the budget, we’ve got to continue to invest in those areas that make America strong and competitive. Whether it’s education or infrastructure, or research or innovation, it’s no sense having a strong balance sheet and also not having a strong country. We've got to be competitive. It's a knowledge-based global economy.

Third, I think we've got to make sure that America is safe and secure. But I don't think that means we have to be the world's global policemen or that we have to be involved in nation building. I think other nations have to do their part. Our military budget now exceeds the military budget of all the other G20 put together.

Fourthly, I think we've got to reform the tax code, to broaden the base and simplify the code, and to make America more competitive. We can talk about various ways to do that. But clearly, we've got to close the tax gap. And I wish Mitch Daniels was here because he can talk about it more clearly than I can.

But most importantly, I think we have to eliminate or sharply curtail these things that are called tax expenditures. But what they really are is just spending by another name. And if you look at the total cost of tax expenditures, they actually equal all of the income tax that flows into the federal government. And they equal 50 percent of the revenue.

I have put on the table that we ought to establish caps that keep revenue at or below 21 percent of GDP. I didn’t just pick that off the ceiling. It’s the number that we have had every time we balance a budget in this generation. I also have called for instituting a plan to reduce overall spending to not more than 21 percent of GDP by making some really tough choices. If you look at the forecast in the CBO’s forecast, spending is projected to go to 25.4 percent. So, that’s a big, big jump to get it down to 21 percent of GDP.

We can do that, but we have to reduce discretionary spending, and we’re going to have to make some tough choices. As I was telling one of the governors a minute ago, what we do is not so hard to figure out; it’s the political consequences of doing it that makes it really tough. The same decisions you all have to make every day in the states.

If we can’t agree on specifics, then one of the things we can do is freeze all of the discretionary spending between 2012 and 2015. That would generate $125 billion in 2015, and will get us half way home to President Obama’s goal.

We also have to reform the entitlements and reduce mandatory spending. As Al said, one of the things we’re going to try to work for is extending the solvency of Social Security for 75 years.

As it relates to healthcare, there are lots of recommendations that we are considering now. But the one that we really have to tackle is how do we pay for quality and not quantity for healthcare, as you all see every day.

Like the Brits just did, my goal

for what percent of deficit reduction should come from spending and what percent should come from revenue I'd like to see something similar to what the Brits did, where they had 74 percent of a deficit reduction on the spending side, and 26 percent on the revenue side. Whether it's that or two-thirds; one-third. But I think it has to be something where it's disproportionately large on the spending side.

And lastly, I would just say that none of these recommendations that we're going to make should take place prior to fiscal 2012, in order to protect a very fragile recovery.

That's where we are. I think we've made a lot of progress. We've had three different working groups, one on revenue; one on mandatory spending; and one on discretionary. We've been meeting, and it's been as bipartisan as you can imagine. I don't think you could tell the . . . a recommendation that's come forward so far whether it came from a Republican or a Democrat.

So, I’m really pleased with the progress we’re making. I think we’re establishing trust and confidence. And I hope we can make some real progress. I know I like working with this guy.

CHAIRMAN DOUGLAS: Governors, feel free to . . .

GOVERNOR BEEBE: Mr. Chairman.

CHAIRMAN DOUGLAS: Mike, Governor (Mike) Beebe.

GOVERNOR BEEBE: Two or three observations. I don’t know that I’ve ever heard a gloomier picture painted that created more hope for me. I mean, you--if there is any hope, it’s the approach that’s been taken. It’s the--and I’m not trying to be obsequious--Brian, I’ll tell you what that means later on.

But you two, and the whole team, and the objective and honest approach actually creates hope. At least it does for me. So, if . . . if it’s possible to tell us how bad things are are and make us feel good about it, I think both of you have done that. And I appreciate the fact that while you have plenty of other things to do, you’ve taken on this monumental task.

I only wish we could put you in every corner of the country for everyone to be able to listen to. And particularly those who are strident on one extreme or the other. Because the honesty with which this came across, I think has to at least affect enough people that Americans would have enough courage to do what needs to be done based upon the leadership and the recommendations.

Senator Simpson, if you and Dale Bumpers, and David Prior could go with Joe Manchin, could go into the Senate chamber and spend a few weeks with the folks we’ve got there now, and teach them about honest debate and collegial disagreement, instead of the rhetoric and the harshness that at least from the outside appears to exist, what a better place America would be. Thank you, sir.

SENATOR SIMPSON: I just have to

say that Dale Bumpers, wonderful earthy, wonderful lawyer. If you remember the final pitch for President Clinton was done by Dale Bumpers, which should be recorded, it was about loyalty, and it was powerful. And then of course, Dave Prior and Barbara are very dear and special friends and come to see us in Wyoming. That is true.

And I went into the chamber a few years ago and Bumpers was wandering around. And I gave him a big hug and we slapped each other. And some guy came from the Republican side of the aisle and said what were you doing there? And I said giving a hug to Dale Bumpers, who is a great and dear friend. He said, I wouldn't do that again. Great stuff.

Let me just tell you one other thing about those tax expenditures. There are 200 of them. And do you know what they are? They're home mortgage interest deduction; they are employer deduction of healthcare premiums. And they go on and on. And they went on the books as a tax cut. And to get them off, they're called a tax increase. I don't know who figured that one out years ago, but they sure laid the snares. Because a tax expenditure appeared as a tax cut, which everyone cherished. And to get them off, and if we got them all off, or a lot of them, or some of them, we'd be well toward home, and today it will be called a tax increase.

CHAIRMAN DOUGLAS: Governor Manchin.

GOVERNOR MANCHIN: First of all, I want to second Mike's evaluation of that presentation. I think it was excellent. I would only ask that in the spirit that we, as governors, have to have a balanced budget amendment and when our forecasters and our economists come to us and lay out the not-so-encouraging news financially of our states, we have to do what you just laid out that should be done.

I would ask respectfully, what is the impediment? Why the urgency is not there for this country to get its financial house in order? And how may that be done?

SENATOR SIMPSON: Want to try that one?

MR. BOWLES: Yeah. You know, we don’t have a balanced budget amendment, so we don’t have to do it. And there probably are some good reasons not to have one when you have the -- have the military responsibilities that we do from time to time.

GOVERNOR MANCHIN: Sure.

MR. BOWLES: My experience has been the Congress generally acts when it has to, and only at the very last minute. And we can go on and survive as a nation for three, or four, or five more years and do nothing. But every day we delay, that old compound interest catches up with us. And every day we delay, more and more dollars go out of the country. And every day that we delay, we have fewer dollars to spend on education and infrastructure. Every day we delay, there’s another small business has been crowded out of the capital markets by the government's borrowing. And when that happens, as you know, small businesses in West Virginia can't grow and can't create jobs without money.

So, when it becomes a crisis, then you're going to have to act. What we're trying to do is get ahead of what I'm confident I can show you just in arithmetic, is the most predictable economic crisis in history and try to do something now, when the pain would be relatively small. Because if we wait, it will be really, really tough.

CHAIRMAN DOUGLAS: Governor [Jack] Markell.

GOVERNOR MARKELL: Thanks. First of all, I agree with my colleagues, a really outstanding presentation. Two quick things: We've got a very strange way at the federal level of investing and paying for infrastructure. Something that, Erskine, you mentioned briefly. But it does seem to me that unless we end up separating, I know in Delaware, and I'm assuming in most states, I don’t know for sure, you know, we’ve actually got a separate capital budget, which we really don’t seem to have at the federal level. Until we do that, it does seem that we’re probably going to be shortchanging those investments. And were Governor [Ed} Rendell or Governor [Arnold] Schwarzenegger here, they’d probably make the same pitch. I think that’s one thing.

And the second thing that, Erskine, you also mentioned when you talked, you mentioned briefly the issue of healthcare. And, you know, we’ve got to find a way to pay for quality, not just pay for, you know, quantity. And you mentioned it briefly, but I do think that there’s a disproportionate amount of money in there. And if we don’t figure that out, it’s going to be really difficult to get to some of the targets that you--that you’re trying to get to.

MR. BOWLES: Yeah, I certainly agree with both those comments. This healthcare is the big enchilada. Just to tell you how big it is, today Medicare and Medicaid spending amount to approximately 5 percent of the GDP. If we don’t fix it, Medicare alone is on a glide path to get to 22 percent of GDP. Now, remember, I said I wanted to hold all spending to 21 percent of GDP. And the average revenue in this country historically has been at about 19 percent of GDP. So, we’ve got to get it under control.

And because Medicare and Medicaid are growing at such a fast rate, it causes the interest on the debt, our deficits cause us to have to borrow more and more capital. And interest will be at 38 percent of GDP if we don’t get off this glide path.

We’ve had . . . we’ve gone to see, Al I have, every interest group, I think in the country, to listen to what their recommendations are. And most of them have told us what you can’t cut. We haven’t had many people--I’m sure you governors don’t either--have anybody come tell us, well, cut this, this makes a lot of sense.

But we do have a lot of good recommendations on the healthcare side that we're exploring. Some that I think make a lot of sense. And we're getting it from both sides of the aisle. And I think we'll be able to come up with some recommendations that governors will say thank God.

CHAIRMAN DOUGLAS: Governor Schweitzer, as long as you're not obsequious.

GOVERNOR SCHWEITZER: I'll stay away from that. As governors, as chief executives, we find very early in our careers that there are an infinite number of good ideas, and they call cost a little bit of money, And our responsibility is to say no to most of those.

Most of us have the ability to do a line item veto. Some of us have mandatory vetoes. And so, at the end of the day, we balance our budgets by saying no to somebody--almost to everybody.

My concern is that we do have a

Blue Ribbon commission. We have some of the finest minds, including the two of you, in the country that will make recommendations. But we all have commissions and boards, and they always make recommendations. And some of us think those are good ideas, and some of us don't. But then you have a Congress that has to move on it. What is the process? Is this a recommendation? Do you have some teeth? The President's going to carry this ball, but what does he do about the House and the Senate?

MR. BOWLES: We have baby teeth, which is better than no teeth at all, I guess. Unfortunately, seven of the senators, who had been sponsors of what would have been a legislatively mandated commission, walked at the very end. And it only got 53 votes instead of 60 votes.

And that would have been much more impactful than what we can do. I think that's fair to say.

SENATOR SIMPSON: That was the

saddest thing. They wouldn't have gone to the floor with setting up the legislative commission, instead of this one as an executive order. They wouldn't have done that. But seven of the co-sponsors voted against it when it came to the floor. Including a remarkable array of people who had co-sponsored--well, they're all co-sponsors--but they had fought for it for three, or four, or five years.

Somebody said, well, what was the purpose of that? As far as I can discern, it was to stick it to the President. That's where we are in Washington now.

MR. BOWLES: Our baby teeth are that if we get 14 out of 18 votes, so 60 percent wasn't high enough, you know, from the Senate. We've got to get 80 percent. And we have six members of--six Senators and six Congress people; three Republicans and three Democrats from each body. But if we can get 14 votes, then Senator Reed has agreed to bring up our recommendation for an up or down vote. And if it passes in the Senate, then the House has agreed to vote on it, too.

So, but we've got to get, you know, 80 percent. And we've got people, you know, every extreme you could imagine. So, we have some teeth, and we're trying to build the trust and confidence, and the sense of urgency, that will make people agree that we have to act and act now.

CHAIRMAN DOUGLAS: Governor Herbert--I'm sorry, Senator Simpson wanted to jump in.

SENATOR SIMPSON: I would just say that those seven though, have now come to us and said we're ready to help. And that's very helpful to us.

MR. BOWLES: But if we had--if we had 12 governors, I guarantee we would get to an answer tomorrow, because you all are used to making these decisions. You know the importance of them, and you wouldn't put it off.

MR. [Gary] HERBERT: Well, thank you.

Maybe baby teeth and baby steps here, as I hear it from the people of Utah, you know, the biggest concern is this growing debt. And the . . . just the lack of sustainability. We just feel like we’re going towards a precipice that there’s no retreat from, and we’re going to go over the edge.

I know the phrase that seems to have been coined in politics is fuzzy math. And it appears as we’ve just pierced this 13 trillion dollar debt here this past few weeks, made national news, but we get different numbers from different branches of government. The executive branch says one thing, the congressional branch says something else. Is there any ability for us to have a frank and brutal and honest discussion on what the actual debt is? And the ongoing liability. Is it 13 trillion with an ongoing liability of 50 trillion? Can we get everybody on the same page and have reality triumph over politics to take off the rose-colored glasses that seem to come to the forefront during political campaigns and really get everybody on the same page as far as these are in fact the real numbers, and real obligations, so that we can in fact address it?

SENATOR SIMPSON: Well, Erskine and I knew that was the problem from the beginning. So, we--with Social Security we use only the actuary, only the actuary. That gentleman, I believe, has been there about 30 years, Steve Goss. People really don’t like to read that report. And it’s all there.

And then there are two trustees that are yet to be appointed, hung up in the Senate confirmation process. These trustees were to report in June. It’s a bipartisan group; they tell absolutely these hard figures. Those two people haven’t been appointed yet. But we use only the actuaries of the healthcare system. We’re not out to use any other thing. And people really are irritated by that, because that’s where the meat is, and that’s where the authority is, and that’s where the honesty is--in the actuary.

And then with regard to the rest of it, we use the Congressional Budget Office, and not the Office of Management and Budget. So, we stick, but Erskine can . . .

MR. BOWLES: Yeah, we made it, the two of us, before we agreed to do this, because you're exactly right. You know, there are a zillion different ways to look at numbers in Washington. But arithmetic is something I can do. And . . .

SENATOR SIMPSON: He is the numbers guy. Did you know, I just sit here and watch him. Look at this stuff that we . . .

MR. BOWLES: We absolutely, we agreed that we were going to use CBO numbers. We told them we weren't going to use the administration's numbers under any circumstances. And we were going to use only the actuary numbers as it related to Social Security, Medicare and Medicaid.

CHAIRMAN DOUGLAS: Governor

Sanford.

GOVERNOR [Mark] SANFORD: Let me just say up front, that again, I echo the sentiments of a variety of colleagues who have praised both of you guys. I remember when I was in Congress, Erskine, I was always particularly impressed when you were Chief of Staff with the way that you would return a call that day, which I think is just incredibly impressive. And Alan, I've long admired your work.

That having been said, tell me what's wrong with the skeptics' viewpoint. It alludes to, at least at some level, to what Governor [Brian] Schweitzer was getting at, which is, you know, we've seen a lot of commissions come and go through Washington. You know, you have a prescription that's built on the presumption that the economy will get better by 2012. If that does not materialize, and I think that there are very reasonable grounds under which it might not materialize, then what happens to the recommendations if the economy is still weak and you haven’t seen it take off--lift off in the economy here over the next 18 months, too-- is it not impossible, and if you look at the 50-year moving average, you know, debt to revenue to GDP has been about 20 percent very consistently post World War II, that’s been the moving average, to bump it up to 21 percent? Isn’t that going to be awfully tough given that average? And frankly, you know, losing home deductibility on one’s house, you can call it a tax extender, tax whatever, but a lot of people would in fact see that as a tax increase, and I mean, fight vociferously against it. And then three, again going back to Governor Schweitzer’s comments, you know, a commission alone without the heat of the President and the bully pulpit of the President, I think, is going to matter very, very little. And so, you have a President, who at this point, is not out in front of this. I think we’re running out of time.

There’s an interesting book, I think it’s Reinhart and Rogoff, a professor from the University of Maryland and from Harvard who wrote a book called *This Time it's Different*. It chronicles the last 800 years of financial history. And once you get to about 90 percent debt to GDP, really bad things start to happen to one's economy. And we're awfully, awfully close to that number. Aren't we too late with regard to time, given the fact that the President isn't engaged, and we're still at the commission level?

MR. BOWLES: Yeah, Alan said he couldn't quite hear, so I'll . . .

SENATOR SIMPSON: Yeah, I have a hearing aid, but I left it in the hotel. And somehow with the reverberation, I can hear all that, hear here, but I don't quite get this corner. So, that actually was a tough question, and therefore I'll give it to Erskine.

MR. BOWLES: We finish each other's sentences. We have dinner together, the two of us, all the time. We are partners, completely.

All good questions, Governor

Sanford. There are lots of skeptics. Some commissions have worked, some haven't. Al served on one that worked very well, on the Iraq Study Commission, where I think now 59 of the recommendations have been adopted.

As I've said, you know, I did personally negotiate the first balanced budget in our generation, so I know it can be done. And if I could remind you that when we set out to do that, there wasn't a news organization in the country that believed that it was possible. And we got it done. And we did it by building up trust and confidence and a sense of urgency.

Secondly, on the debt to GDP ratios, when I left Washington in 2000, the debt to GDP ratio was--this is for public debt. That's where you get confused, Governor Herbert, because some people talk about the public debt, some people talk about the gross debt. And then some people talk about all the unfunded liabilities.--The public debt now, is about 9.6 trillion. The gross debt is about 13 trillion as you just said. And if you count all the unfunded liabilities, it’s about 52 trillion dollars. So, it gives you a pretty wide spread.

But when we left, the public debt was about 35 percent of GDP. Today it’s 64 percent of GDP. The average since 1957 is 45 percent of GDP. And to kind of understand what the gross debt is, just add 30 percent to all of those numbers I just gave you. There is lots of scholarly work. In fact, we had the people who wrote the article Governor Sanford referred to come and speak to us--Professor Reinhart. And when debt to GDP gets to 90 percent, then you can almost guarantee that you’re going to start to lose, for every incremental increase in debt, about 1 percent GDP is going to fall off the wayside. So, it really does have a real negative impact. It’s called reverse leverage. All of us in the business world have dealt with it.

But it’s a real problem. I do

think if we . . . I think we have a small chance to be successful. And again, the reason we have a small chance is I think that we have built up confidence in each other. And we do have these baby teeth that will allow us to get this to the Congress and get an up or down vote if we can get a recommendation to come out of the commission.

CHAIRMAN DOUGLAS: Governor Baldacci.

GOVERNOR [John] BALDACCI: Just a lot of ground to cover, but let me just also echo along with what Governor [Mike] Beebe said. It’s been very refreshing. It’s also been very sober. But I think we don’t hear it enough. And as Governor Beebe said and I would concur, you all ought to be in all quarters of the country talking on a regular basis.

We were there in ’94. And we were there to balance the budget for the first time in a generation. And I want to compliment you and the administration on being able to do that.

Because it seems though during that ‘94 period with the shutdown and everything, it was really bad, the worse it’s ever been, until they started writing stories about in the 1830s when the members of Congress used to shoot each other. So, it wasn’t as bad as that, but it was pretty bad. We don’t want to bring those habits back.

But at the same time, it seems like it’s gotten a lot worse. Just seems like it’s gotten even harder than it was back then. And you two are kind of just the only two voices out in this whole area where it seems to be so negative. And it’s kind of following along with what Governor Schweitzer said. Unless you folks are prepared to take a full-court press and get out there on a more public stage, and just use all the opportunities you can, and then more so and the President embarking on grabbing this and just showcasing it that much, I don’t know really how your recommendations are going to be able to go very far.

SENATOR SIMPSON: We hope we might

be able to get to legislative language in our report, which would be the master stroke if we could do that. But that would be an important goal I think that Erskine and I have, that we would do some legislative language as we . . . as we submit the report.

But it is--we don't have--we feel if we went around the United States and we had hearings now, right now, that the people would see a bit of discord in the commission. That would not be helpful.

The three working groups report to the full commission at the end of each month. The working groups meet in private. And they have to, because they talk about all the flash words that you've just heard.

And then of course, there was a request that we come out with our report in October instead of November. Therefore, every politician running could cherry pick the report, and just go home and say do you know what these nuts are up to. That would be the result of that. So, there--we're--we can't do anything. We stick with December 1st.

But someone mentioned, how did we really get here? We were trained, all of us, for the last 60 years, to bring home the bacon. And when we went home to our districts, we had a staff person, or two, or three. And when the guy got up and said we need a new dam down there on Henry Ford, great, write that down, will you, Harriet or Harry. Get that, we'll get that for you. And we need a new airport terminal; we need this. And your job was just to go home and get it. And then run, and then worship at the great God of reelection. And that's how we got here.

But now, the pig is dead. And there's no more bacon to bring home. And it's . . . it is . . . you just . . . it's there. And it's shocking.

CHAIRMAN DOUGLAS: Governor Doyle.

GOVERNOR [Jim] DOYLE: Thank you. I'm interested in a couple of your sort of visions of where this is headed into the future. There isn't a big spender among any governors here anymore. Maybe they were originally, and we may call each other names, but given every budget we've been through . . . and so, what we're going to confront, I see, I . . . many of us won't be in office, but this economy is going to rebound, we hope sooner rather than later. And the amount of unmet need rather than the need that we've cut is real.

So, Senator Simpson mentioned the dam and the terminal, well there are some dams and terminals that do need to get built that we have been deferring because of the situation that we've been in.

Demands, President Bowles has noticed, but in higher education that we've deferred because of the situation. I think the governors, in the next couple of years, one of the great pressures that they're going to have, and this will be--I'm interested in how this relates to your work and how you see it playing out over time--is that these resources are going to be a little bit better in the next few years, and the demands that have been deferred over the last four years are getting so intense, that the claims on that money, the little bit of money, the little bit of increase that's coming in is going to be enormous. The people that you've said, as Governor Schweitzer or someone has said, all of the no's that we've said, there are going to be a few that are very, very important that we've said no to. Not because they were bad ideas, but because we didn't have money.

So, as you see the economy rebound and, you know, we can argue and economize; I I guess we'll know, and only time will tell, how quickly it rebounds. But the demands we . . . we have also I think we could . . . well, I could I assume most governors here could give you a long list of unmet needs of things, very legitimate needs that we have had to defer. So, it's going to be, you know, it is the economic crisis that has people cutting. And the rebound, as you all know from your experience, is going to have people moving towards trying to meet some of these needs.

I guess my question--what I'm interested in is a little bit of what's been asked already, but not just where your recommendation goes, but how, over time, over a five-, 10-, 15-, 20-, 25-year period of time, if you--if the country--agreed on a certain course that we should go, which I would assume would be a balance of the new investments that we have to make, but the cuts that have to be made and the . . . how do you enforce that out over a 10-, 15-, or a 20-year period of time that is going to happen? So, your recommendations are in many ways in this economic climate pretty easy to, at least at a state level, we all have agreed to almost every cut anybody could come up with, because we just have had to. But it's just going to be a lot harder to agree with those in the next few years.

So, I'm interested in sort of your thoughts on--I recognize you say your chances for success are slim, even in getting this adopted--but what is your vision about if we have a pathway we should be on and we agree on, it's one that isn't going to happen in one year or two years? It's one that's going to happen over decades, a long period of time. And what's the mechanism to see that that would occur?

MR. BOWLES: I think you're partially right. The part that I think you ought to be concerned about is, I don't think you can anticipate no matter how much the economy improves, any additional help from the federal government. They just simply do not have the resources. If you look at the 10-year forecast, and it gets worse as you go out, not better; you're looking at deficits of at least $700 billion dollars every year.

So, those of you who have balanced your budgets by using the federal stimulus dollars, which run out this year, you're going to be left with a darn big hole to fill. I know in North Carolina, we have a billion and-a-half dollar hole there. Plus we have a tax that's running off, and that's going to place a huge responsibility on us.

I think about what Governor Perdue has had to do in order to make us more efficient and more effective, and make the tough choices she's had to make. They're no different than the ones that I have at the university. I have cut, last year, administrative costs by 23 percent. I do have 30 percent fewer employees today in administration than I had five years ago. I did fire 900 people last year, all on the administrative side of the ledger. You know, I did increase the workforce. You know, we froze the salaries; we put in furloughs.

We're going to have to make you, as governors, and we as administrators of other areas, we're going to have to continue to make really, really tough choices if we want to have resources left over to invest in education, and infrastructure, and economic development. But I don't think we can . . . we can count on having additional funds from the federal government to bail us out again. The pig is dead.

SENATOR SIMPSON: I think, one thing out there that so many people out there who come to the town meetings and so on, and they'll get up and there'll be great applause, and I'll tell you what you need to do, congressman or governor--not you guys--you have to balance the budget. We don't out there. But they'll get up and they'll say I'll tell you what you ought to do, now let's get cracking. You get rid of all earmarks; get rid of all foreign aid to anybody; and get rid of all waste, fraud, and abuse, and that'll get us there. That will get you five percent of the hole.

So, when they say get rid of Air Force One, and cut pensions, and just tell them to quit playing around, they're just showing off. Because if you . . . if you did those three things, all of it, earmarks, foreign aid, waste, fraud, and abuse, that'll get us five percent out of this hole.

And yet, when you go out in the land, so much heavy language and cheers from the crowd, if half the people there with gray hair and 65 bitching about the government are on Medicare. So, should we say well, then you, you mean, you're out of the touch here. You're . . . we're going to cut that off.

But Dave over there, what was it, a year ago, Dave, you said to the state of Wyoming, you go back into your own agencies and you cut 15 percent, wasn't that it? And we're not going to do it across the board. You're going to figure it out. They all know where the fat is. You know, people achieve now, the first thing they say is when I came here, I had a staff of ten, but now I have 30. Oh, that means you've succeeded. Yeah, it's a . . . it's a great thing. Well, I won't say anything more.

MR. BOWLES: I'll just add to that. You know, you all have made a lot of the tough decisions that they haven't made at the federal government. Let's . . . let me just give you one easy example that’s difficult to do.

It’s been--I don’t know how long--but it’s been a long time since we’ve had a pay raise as civil servants in North Carolina. And Governor Perdue has had no choice; she’s got to balance the budget. In Washington, they’ve had pay raises of 2 percent; 3.9 percent; and 3.5 percent over the last three years. And President Obama has a proposition for an increase of 1.4 percent next January. No way.

Now, how much do we save if we freeze federal civilian pay at 2010 levels? We save about $2 billion a year. Is that going to get us to the Promised Land? No, but those are the kinds of decisions that you’ve already made, that we have to make as recommendations in this budget.

CHAIRMAN DOUGLAS: I saw four hands. And so, if I could ask my colleagues to be as expeditious as possible. We’re a little beyond our allotted time. Governor Rounds.

GOVERNOR [Mike] ROUNDS: Thank you, sir.

Gentlemen, thank you for your service. Governors have the responsibility constitutionally to balance their budget. They cannot borrow money in most cases. The federal government has to have the ability during times of emergency to be able to take . . . to take care of national issues. But at the same time, is there any structural change that can be made that would--other than a Constitutional Amendment--which would bail or pull Congress, and these are good people; we send them there; they're solid individuals. But is there a way to structurally change the make-up to make Congress accountable for the promises which they make that the next generation of Congressmen have to pay for?

At some stage of the game there has to be some accountability for what you promise that you're going to deliver. Is there anything in the recommendations, other than Constitutional changes, that would allow that to occur?

MR. BOWLES: Alan is the legislator. But that's the whole problem we have with something like Social Security. Talk about something that's, you know, a third rail. You know, we promised more than we can deliver. The same thing with healthcare. You know, we did a great job of accessing--of taking up access this last time. But boy, we didn't do very much on the cost side, I can tell you that.

And you can see by the forecast I gave you what a significant issues that is. But on healthcare--I mean on Social Security--we're going to run through this "trust fund" by 2039. And the trust fund will be gone, all the interest on the trust fund will be gone. And by law, the payments to Social Security recipients have to drop that day by 20 percent in order for the revenues to match the outlays. And pretty soon, they'll have to drop by 24 percent. And so, what you're going to get from Social Security is going to go down if we do nothing. And so, what we have to do is figure out a way we can fix it, which we believe we can. So, that those payments drop at a much more gradual manner, or that we get additional revenues to maintain that level of benefits. But it’s going to go down unless we take action, because they promised more than they can deliver. And you can find that in every single area of the federal budget.

SENATOR SIMPSON: Let me just add one thing. There is--and this is not about partisanship--I have no idea what’s going to happen on election day, but it’s going to be disruptive. Appropriators are resigning. Both parties, people who are on the Appropriations Committee, that’s a whole new game to watch appropriators begin to step aside, because they’re the money guys. They’re the guys that have been setting it up and shoveling it out. And that’s an interesting thing to watch. I have no idea what’s going to happen. I don’t cherish any result over another. But I’ll tell you, it’s going to be a big wake-up call around the whole United States. And I have no idea where it’s going, but thank heaven we have a month then to work through the wreckage and see what’s happened. And maybe . . . and then watch out for a lame duck session, where people have just been saving stuff in their back pocket for 10 years, and have resigned after 20 years in the Senate, and say well, here’s this baby that I never could get through. And I’m working it.

But the other one, with regard to Social Security, there’s a fray that’s called scheduled benefits and payable benefits. Scheduled benefits in 2039 will not be made. Payable benefits will be made. There will be enough to make payable benefits, and they will be substantially 20 to 25 percent different than scheduled benefits. And that’s the way it is if you do nothing. So, when you hear people say, and they do, we’re going to deal with that. Well, each year you wait, this is . . . this is just a boulder rolling.

CHAIRMAN DOUGLAS: Governor Gregoire.

GOVERNOR [Chris] GREGOIRE: Well, I join the cause in saying thank you for your service, your leadership, and for joining us today. I have to share with you, there isn't a person here that doesn't want you to succeed. Behind all that is a concern I'm sure by all of us. Does that mean that it's going to result on more demands on the states? In other words, more unfunded mandates, more rolling downhill. The concern of most governors here is are we going to be able to do healthcare reform, or are we just being asked to pick up a tab that we otherwise wouldn't be asked to pick up?

So, with that in mind, we want you to succeed very much. What can we do to help you be successful? How can we partner with you so that your efforts will not result in the kind of skepticism that you heard here, but real reform and real change for all of us?

MR. BOWLES: Governor, you're exactly right. One of the ways we balanced the budget in 1997 was that dirty word devolution. And we did devolve a lot of services without appropriate funding down to the states. And that helped fix up the federal budget. Caused you a lot of headaches.

I don’t think you’re going to see a lot of devolution coming from us, because the stakes are all, you know, are all broke, you know, are all in the same situation the federal government is. So, devolution is certainly, in my personal opinion, not the answer.

How you can help us is we can’t , , , we don’t have the resources. We’re a deficit reduction committee, so we’re not spending hardly any money. But so, we don’t have the resources to do one of these national campaigns, and we’ve got to get the word out. So, our hope is to meet with people like you all. We’re meeting with the National Chamber. We’re meeting with, you know, anybody who will let us come meet with them. And we hope that you will spread the word that we’ve got to take action, and take action now. And deferring it to some later period of time is just irresponsible.

SENATOR SIMPSON: I think one of

the things that we’ve already been hammered with is how much are you guys making. That’s a wonderful treat, because I get a coach fare out of Cody, Wyoming, and I can’t get in first class, because I can’t walk my emaciated frame in there, and I’ve got a new knee. So, I’m paying the spread between the coach and the first class. Don’t feel sorry. And then we get a whole per diem for one night, and government rate. And we pay that. And we pay everything else from our own pocket. And people chip on us, how much you making? You guys are making a ton out there. That’s always a good one.

And then our budget is--our budget for the whole thing is $500,000.00. And with that, we’ve hired Bruce Reed, a very able guy and a fine staff. We have young college students we have borrowed from the agencies of the government. We have--we can’t borrow from --we can’t borrow from a Congressional staff.

The House Budget Committee has 75 people and a budget of $10. million.

We have, what, 18 staff and a budget of $500 grand. But if we had any more, we would be in peril. We have to look like we're in rags and stagger through the village, you know, with a tin cup. And that's what we're doing beautifully, although we wear good clothing.

CHAIRMAN DOUGLAS: But you sleep in your suit. Governor Perdue.

GOVERNOR PERDUE: Thank you. Just a suggestion, Mr. co-chairs, and thank you for a really interesting presentation. As you read the title of the assignment you have, it's the federal budget and deficit issues. I would suggest that you wouldn't get a list of whines and complaints if you would ask the governors here, who we, I mean, we think of ourselves as the teammates. We're all in this together with the Congress and the Senate and the country. And we have some really good ideas that might not save you billions of dollars, but I could spend a half hour with you and give you 10 ways to fix Medicaid cost and help me do what I need to do in the state.

I would think that would be a really helpful piece of information for you to have to include in your report. Some of the trimming of the bureaucracy and the red tape that people like the governors have to go through to do any kind of substantive change in their states.

I have a Medicaid waiver that has been two and-a-half years in process of being authorized. And that is ridiculous. And I would believe there are hundreds of those things. We wouldn’t give you but 20 or 30, whatever you’d ask for, Erskine. But I know with the leadership of this organization, we have some core solutions to things that would really help the bankrupt states be more efficient.

MR. BOWLES: Thank you. That’s what we came for is your ideas. And, you know, to talk about something really controversial, let’s talk about Medicaid.

I mean, Medicaid is an enormous

cost. You could say from the numbers I gave you earlier, it is a cost that's going to grow and grow and grow. And of course, you all are paying a big portion of that.

I personally think that we've over promised; that we promised more than we can deliver. And I think the taxpayers can afford to make sure that everybody has a darn good Chevrolet, but nobody ought to get a Cadillac at the taxpayers' expense. And that's a very controversial opinion. But it's also based on reality of what we actually can afford to do. And so, we are looking for ideas on the Medicaid side that can help us bring down the cost of Medicaid. So, that we can actually give people what we can actually afford.

SENATOR SIMPSON: And don't forget the new healthcare bill is on the table. We didn't take this on if the President said you know, what we jut accomplished there is off the table. We said--and he didn't, you know, he didn't challenge and he said it is on the table.

But here is something that's on the table, I think. I think in year 2014, under this bill, and they're still sorting through the stack, that states can throw their Medicaid back to the federal government. And some state, the DC if I'm not mistaken, the District of Columbia said we want to accelerate that, throw it back right now, and went to court to be sure that that burden would go back. And if that's the . . . that . . . I'm not . . . that's the first . . . I'm just not certain. But I think in 2014, there's some trigger mechanism in this new bill that enables the states to throw it back, or portions thereof, to the feds, which just makes the problem greater from the standpoint of what we all are portraying.

CHAIRMAN DOUGLAS: Governor [Bill] Ritter has graciously yielded his time, so we can try to get back on schedule.

But as we wrap up this discussion, I wonder as an association, if we might follow up on the points that Governor Gregoire and Governor

Perdue made.

First of all, think about specific recommendations we would have, based on our own experience in managing in difficult times. We talked a lot about that at our roundtable yesterday. And convey those ideas to our guests and their commission, to the extent that they would be helpful in forming their deliberations.

And secondly, later in the year, when the commission gets to the point of a recommendation with 14 of the 18 votes, a very diverse group of people from different walks of life, perhaps NGA would care to endorse that process and urge the Congress to support the recommendations of this bipartisan commission as an important step to get our fiscal house in order. I don’t know how you’d feel about that.

But I think we’ve expressed a lot of support for the work they’re doing, and the need to move toward some fiscal stability in the country. But if there’s interest in that, we could draft a letter and circulate it during the coming months and move forward. Why don't we do that?

Well, this has been a great discussion with two great Americans who've stepped forward to undertake a difficult task. I know all the governors are grateful to you for doing that, and wish you well in your deliberations. And we want to be here to help. We're all in this together as we serve to improve the lives of the people of our states, and make sure that future generations can bear a fiscal burden that's not oppressive.

Thank you so much for being with us today. It's great to have you.

It's time to move to the reports of our committees and recommended policy positions. All the governors have a packet of recommended policy statements color coded by committee at your place. And we'll proceed to adopt them. They were all sent to the governors originally on the 25th of June. And the standing committees, of course, have reviewed them, along with our staff.

First, is the Economic Development and Commerce Committee, by Governor Markell. Unless . . .

GOVERNOR MANCHIN: I believe that --I believe my good friend from Montana might have a motion here on all of our committee reports.

CHAIRMAN DOUGLAS: Natural Resource?

GOVERNOR MANCHIN: No, all of them.

GOVERNOR SCHWEITZER: I move we go in block.

CHAIRMAN DOUGLAS: By golly, you're using a lot of big words and Latin phrases today, Brian. Governor Schweitzer moves we adopt all the recommendations from all the committees in block, is there a second? Seconded. Discussion? All in favor of the motion say aye.

GOVERNORS: aye.

CHAIRMAN DOUGLAS: Opposed, no?

The ayes have it. We have approved them all. Thank you committees for your outstanding work.

I want to pause for just a moment to thank our gracious host and his team for their wonderful hospitality. Governor [Deval] Patrick and Diane, Dave O’Brien, Kim Whittaker, the entire Massachusetts Host Committee has been outstanding. We’ve had a great time. Thank you, Deval, so much.

I also want to thank the NGA team. Ray, David, John, all the policy directors and their staff have done an outstanding job. We’ve had a great annual meeting. But throughout the course of the year, they do a wonderful job for all of our committees.

Many of you may not know Susan Dotchin. I know Susan is here, but she’s our planner who does all the logistics for our meetings, has done so for quite a few years. And want to thank Susan for her continued work on behalf of NGA. Susan, thank you.

As we move to the time of

transition of the association, I want to thank all of my colleagues for your participation, your hard work, your focus on some important issues. We live in a very diverse country and the membership in the National Governors Association reflects that diversity. We come from different areas of America; different points of view. We reflect the priorities of the people we serve. And sometimes in challenging fiscal and policy environments, those differences become evident. But the diversity of the NGA I think is also its strength, and it has been for more than a century. And I’m confident that we’ll continue to work to find ways to achieve consensus, to find common ground, and move forward on behalf of the people we serve in the best interests of the American people.

So, I want to thank you, especially during this challenging year as we’ve focused on healthcare reform and other priorities. And although it’s been challenging, it was less so because of the opportunity to work with an outstanding gentleman from West Virginia.

And it'll be a privilege and honor to present him to you in just a few moments. In order to do that, let me call on Governor Beebe to report for the Nominating Committee.

GOVERNOR BEEBE: Thank you, Mr. Chairman. On behalf of the Committee, it's my privilege to recommend Governor Mitch Daniels of Indiana on the Executive Committee, together with Governor Deval Patrick, Massachusetts; Haley Barbour, Mississippi; Chris Christy, New Jersey; Ed Rendell, Pennsylvania; Jim Douglas of Vermont; Chris Gregoire of Washington. For NGA Vice Chair, Governor [Dave] Heineman of Nebraska. And for NGA Chair, Governor Manchin of West Virginia. I move the nominees be accepted in your terms, in block.

CHAIRMAN DOUGLAS: Any further nominations? If not, all in favor of the motion say aye.

GOVERNORS: aye.

CHAIRMAN DOUGLAS: Opposed no? The

ayes have it. You've adopted the report of the Nominating Committee.

Before calling Joe up here, I want to give Governor [Gary] Herbert just a moment to talk about next year's annual meeting in Salt Lake City. Yes, I know, most of us are rotating out, but the emeriti are always welcome.

GOVERNOR HERBERT: Well, thank you, Jim. Again, it's been a great meeting, and we thank Governor Patrick for his hosting, and for the opportunity we've had to be here in Boston. I think we've been able to accomplish a lot.

I can tell you that this is the best summer meeting that I've ever been to. It's the only summer meeting I've ever been to, but it was great to be here, and again, talking about important things. And I think we have an impact on national politics by what we do as governors.

We had a very elaborate video prepared to extol the virtues and the beauty of Utah. But because of the flood yesterday, caused by Jan Brewer, causing rain to come up on the protesters, it’s not functioning right now. And we didn’t have the $3.5 thousand it cost to put it back up. And being the fiscally conservative state that we are, in light of what we’ve heard here today, you’ll just have to use your imagination.

Utah has actually hosted the NGA before. But it’s been a long time ago. In fact, so long ago, I’ll just mention it was the year that Chuck Yeager flew faster than the speed of sound. Television was in its infancy, and “Meet the Press” made its television debut. Jackie Robinson broke the color barrier in baseball. And there were only 48 states in the Union. It was also a year that is near and dear to my heart, because it was the year I was born. The year was 1947, which is the last time that we had the opportunity to host the National Governors Association. And it’s safe to say that things have changed significantly since that day.

We had a few hundred thousand people in Utah, and now, it’s one of the fastest growing states in America. We have just under 3 million. So, things have changed in Utah. But we've learned a lot of things. Our hospitality from the West is still as great as it ever has been. And we had an opportunity to host the world with the 2002 Winter Olympics. And we're anxiously looking forward to welcoming the National Governors Association to their annual meeting next July 15th through the 17th. So, we hope that everybody will take advantage of that opportunity.

Utah is a state of very diverse beauty. We have seasonal activities that everybody knows about, our skiing, and what we would say is some of the greatest snow on earth.

We also have beautiful red rock country, where you have outdoor recreation, mountain biking and hiking, Jeep safaris. We have five national parks, whether it be Zion or Canyonlands or Archers or Capitol Reef. We have some very outstanding beauty. In fact, right now, we have an increase in tourism in Utah to our national parks, in spite of the downturn in the economy. And right now, we have, in fact there are more international visitors that come to our national parks than we have Americans. It's being discovered that we have a lot of beauty there that's being appreciated.

And one of the last things I'll just mention here as I invite everybody to come and participate is, there's a lot of outdoor recreational activities, as you would find in an inner mountain West state. Great opportunities. The skiing is something that people understand and appreciate. But golf is also a mainstay. And so, what I have here to present to Governor Manchin and Governor Douglas is a ski cap in representation of our ski season and the greatest snow on earth. And Utah is also one of the states where you can actually go skiing in the morning and play golf in the afternoon. So, I'll give you a ball marker and a divot repair tool that show . . . that kind of exemplify the opportunities.

You can actually go ski in the morning, golf in the afternoon, and water ski in the early evening. So, again it’s a unique demographic, a unique climate. And we look forward to hosting July 15th through the 17th, the 2011 National Governors Association Summer Meeting. So, we welcome one and all.

Now, we’ve got some staff here. Everybody who’s here, that’s stayed to the bitter end here gets a ski cap and a divot kit. So, we’ll just pass those out. Have we got those out already? Oh, good. All right. We’ll see you next July. Thank you very much.

CHAIRMAN DOUGLAS: Well, Gary, thanks so much. As we’ve all learned, it’s not an easy task, but I hope a pleasant one. And we appreciate your stepping up to the plate to host the Association next year.

As we saw the camaraderie between Senator Simpson and Mr. Bowles earlier, I’ve enjoyed that camaraderie working this past year with an outstanding vice chairman. He is a great governor of his state. He is a good personal friend. And he’s going to make a fine leader for the NGA. Ladies and gentlemen, our new chairman, Governor Joe Manchin.

GOVERNOR MANCHIN: Thank you so kindly. Thank you so kindly. It has really been my pleasure to serve you the last year as the vice chairman, to my friend, Jim Douglas of Vermont. And he’s a man of enormous integrity and honesty. Characteristics that run deep, it really does in the culture and tradition of New England.

Now, he also has another New England trait of being frugal, not cheap, but frugal. He is the only state that does not have a balanced budget amendment, but operates as if he does. And I think that speaks volumes.

He is tight with his state’s money, but he is generous in his heart. And I think all of you found him to be a tremendous leader, a great friend, and an easy conversationalist. And Jim has a way about him that I think is so refreshing.

Throughout his term as chairman, he’s maintained a focus on helping states change the healthcare delivery system, to both increase the quality of care, as well as to make the entire system more cost effective. And I think he has led by example in what they’ve been able to do in Vermont. And we’re very appreciative of that and sharing it with us.

Throughout the national healthcare debate, Democrat and Republican governors have struggled to find common ground. And the discussions we’ve had are often tense and contentious. I don’t know of any other time, I’ve been here six years now, and that one probably strained us as much as any. But we still stayed together. And I think this is the last and best hope that America has of a bipartisan effort to really cure the most difficult problems that we have in America. And it sits right here with the NGA.

His debates, however, recognize the

differing views of all of the governors. And Jim was able for all of us to be able to express our viewpoints. He understood the bipartisan nature of the organization, which is the cornerstone of our association. And we were founded over 100 years ago based on this cornerstone.

And it’s easy for each of us to stay in our partisan comfort zone. And we’re getting a lot of encouragement from the national down to the state tickets. It is more difficult to reach across the aisle and say that you can support a provision, a statement, or policy offered by the other party. However, that is exactly what Jim did. He reached across the aisle for all of us. And we all met, I believe, in a very collegiate exchange.

As states move into the implementation stage of healthcare reform, his leadership has continued under the guidance of the NGA. He has convened two major summits, bringing together your healthcare implementation teams from around the country. These summits and teams have been able to draw framework for a new, more cost effective healthcare system in their states. Challenges remain, however, for ensuring the vision becomes a reality. But the work Jim has begun will continue for the next years.

As Jim completes his year as NGA chair, he's also leaves the office after eight years of being a very successful and popular governor, and has won four elections. Jim has been a public servant for 30 years, as he was elected to the state legislature the same year he graduated from Middlebury College.

Jim, all I can say is that we thank you. We honor you as our friend, and we wish you Godspeed and well in whatever you endeavor. We know you will continue to bring people together as you have with us. God bless.

CHAIRMAN DOUGLAS: Thank you.

GOVERNOR MANCHIN: In Jim's own way, he said he's never had to use the gavel with such a friendly group. Let me just say as we close our meeting in one of America's oldest cities, and I want to reiterate what all of us, the spirit of extending the hospitality that Deval and Diane have done in opening up their beautiful state and their beautiful city of Boston, we appreciate so much. And I can tell you, each of . . . each of all of us felt extremely welcome. And it’s been a wonderful experience to be back up in the Boston area for me and Gail. But for all of the people who come. And thank you again, Deval, and all of your staff. Because I know, I’ve seen all of the volunteers and all of the hard work that goes into these meetings. And they went beyond the call, and it shows. Thank you.

So, as we close out, as we close out the meeting in one of our oldest cities, we’re calling to action, and my initiative will be one of America’s newest challenges. Two of the biggest questions as governors we face are, how and when do we get to economic recovery; how do we increase the standard of living for all of our citizens. These aren’t easy questions, but making sure that more of our citizens have an education beyond high school has to be part of the answer. Both for economic recovery in the short term, and a better standard of living in the long term.

We need more high quality graduates with college certificates and degrees. Many more than we’re on track to have over the next decade. Some of the statistics I’m going to share with you; it’s really alarming.

If you look at the economic literature, it is clear that a good 75 percent of productivity change in the U.S. economy, which is the source of all increases in real wages and real income, is due to the education and training of our workforce. But we also have to be--have real and lasting limits on what we can spend. That means we’re doing and we’re going to have to have some changes in how we provide and pay for higher education.

This is difficult, because everybody has become comfortable in what we’ve been doing for far too long. Higher education is one of the areas where states have a lot of the responsibility, and where governors can, and must play a leadership role.

When I thought about my initiative, I looked at it this way. As a governor, what and how do we have the most input in education. Primary and secondary education, secondary education, as a lot of our constituents would believe, that we have total control. And we have, in fact, very little control. But in higher education, we do have. We appoint most of our governing boards. We have a tremendous impact in the funding that goes into our colleges, individually, collectively. So, I felt that was an area where we, as governors, could play a role.

This is why my initiative is called Complete to Compete. Complete to Compete. It’ll focus on improving the performance of higher education systems all over the country. The name of the initiative says it very plainly. If we want to compete economically, we're going to have to have more students completing college and quality certificates and degrees.

And we have to do this with more limited resources, without reductions in the quality of our graduates. We can't afford to wait until the economy and our budgets improve to embrace the college completion agenda.

By 2018, almost two-thirds of the jobs in this country will require some kind of higher skill sets. A generation ago, only about a quarter of our jobs required that level of education. Our college completion rates are not what they need to be. We went from first in the world to number 12 in the world in college graduation. At the same time, we spent more money on higher education. We need to get more out of the higher education dollars we spend. So, when you're spending more and the results are being less, you've got to change.

I think we heard two fine presentations from our Senator Simpson and Mr.

Bowles that basically lay out the stark reality of what we're dealing with. At our current college completion rates, we'll be three million degrees short of what the workforce will demand by 2018. And we'll be eight million degrees short of, once again, leading the role in college attainment at the time.

If we don't improve college completion rates in this country, our children will be less educated than we are. This will be the first time in the history that that has happened in the United States of America. We will not only be less competitive in the global economy, but we will be less secure as well.

Complete to Compete will focus on two basic priorities. Improving how we measure performance and higher education. Our colleges and universities measure a lot, but not enough of it is about how well students are doing and moving towards certificates and degrees. Especially our low income and minority students and working adults, non traditional students as we refer to them.

Better metrics will help us make better decisions about how to spend our limited dollars state by state. Especially when it comes to the increasing graduation rates for those students most at risk of not completing college. NGA has developed a set of common completion metrics that I will ask all of you to consider adopting and reporting publicly.

The document in front of you outlines the metrics. My state of West Virginia is already collecting the data to report on these metrics. And we will publicly release them soon. These metrics account for students transferring in and out of institutions, and both full and part-time students, as well as other factors. So, that we have a consistent way of talking honestly about performance at the state and campus levels.

Collecting more accurate data is an important starting point to help us figure out what we need to do to improve college completion rates. We will also look at how states can most effectively evaluate the productivity of their higher education systems, increasing the number of high quality certificates and degrees for the dollars that we invest.

Number two, developing and adopting state policies that promote college completion and efficiencies. If we expect better performance from our colleges and universities, then we need to reward through our policies. For example, we need stronger incentives for institutions and students to focus on getting though college, not just getting to college. Most of your states are like mine, they basically we pay and we reimburse based on FTE, full-time equivalent. We do nothing based on outcome. How many have you gotten through. We're changing that formula. We're doing it now in our state. And we're going to recommend to you all a way that you can do that in your state.

It includes funding campuses on the

basis of completion, as well as enrollment. And we will create a plan that makes graduation for low income, and minority, and adult students a top priority. There will be more rewards and incentives based on that, which we think will have better outcome.

It also includes transforming remedial education, so that it costs less and produces better results in creating ways for students with a lot of credits, but no degree to come back and finish their degree.

We couldn't figure out why in the world so many people are taking college courses in different parts of your state institutions, but basically when they want to transfer, they don't all transfer. They're made to take it over and spend that dollar over and over and over. We think that we can help in that arena also.

Throughout the year, we'll work with governors and their staff, as well as the higher education business leaders in addition, to create these metrics. We will develop a series of best practices and policy action governors can take to achieve increased college completion. Convene a national summit of governors, higher educational leaders, and other key individuals to raise awareness of the need to improve college completion, and existing dollars without sacrificing quality.

I don’t think that people today believe that without spending more money you won’t get better results. And I believe we can prove that by spending more money we’ve gotten far worse results. So, we have to change our thinking.

Across the nation, there are a number of states and institutions that have already implemented policies and practices designed to increase completion with limited resources, and without taking shortcuts on qualities. We can and we will learn from each one of you in the best practices that you have put forth in your own states.

It’s going to take all of us working together; all of us pulling together. We still face big fiscal challenges, and we will have one of the biggest freshmen classes of governors coming in, in the nation’s history, in January.

But as I’ve said earlier, we can’t afford to wait. States must lead the way on this agenda. Our colleges and universities educate a majority of American students, and our economies depend on having more high quality graduates.

As the international marketplace becomes more competitive, our path forward is to improve completion rates for our colleges, universities, and other post secondary institutions. The future jobs and incomes of our citizens demand it.

I look forward to working with each and every one of you in this coming challenging time that we have, and to the millions of Americans who are trying to make life better for themselves and their children through a college education.

It is the American dream that we all aspire to. We've got to make sure that we fulfill it now. Thank you, and I look forward to working with you. God bless.

As we finish and conclude our business now, we are going to go to the governor's only luncheon before you all depart. We'd like all of you to attend if you possibly can, if your schedules will allow. So, we will be convening that immediately if you will. Thank you.

(Proceedings concluded at 11:30 a.m.)

COMMONWEALTH OF MASSACHUSETTS

I, PAULINE L. BAILEY, PROFESSIONAL COURT REPORTER, do hereby certify that the foregoing is a true and accurate transcription of my stenographic notes, to the best of my knowledge and ability.

WITNESS MY HAND, this 14th day of July, 2010.

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Pauline L. Bailey