

S. HRG. 109-801

**THE FUTURE OF THE GULF COAST: USING TAX
POLICY TO HELP REBUILD BUSINESSES AND
COMMUNITIES AND SUPPORT FAMILIES AFTER
DISASTERS**

HEARING
BEFORE THE
COMMITTEE ON FINANCE
UNITED STATES SENATE
ONE HUNDRED NINTH CONGRESS
FIRST SESSION

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OCTOBER 6, 2005
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**THE FUTURE OF THE GULF COAST: USING
TAX POLICY TO HELP REBUILD BUSI-
NESSES AND COMMUNITIES AND SUPPORT
FAMILIES AFTER DISASTERS**

THURSDAY, OCTOBER 6, 2005

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 10:06 a.m., in room SD-215, Dirksen Senate Office Building, Hon. Charles E. Grassley (chairman of the committee) presiding.

Also present: Senators Lott, Snowe, Kyl, Santorum, Bunning, Baucus, Lincoln, and Schumer.

**OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S.
SENATOR FROM IOWA, CHAIRMAN, COMMITTEE ON FINANCE**

The CHAIRMAN. I call this hearing to order.

Last week, this committee focused on our second phase of tax relief with respect to the aftermath of Katrina. The committee has responded quickly and decisively to the hurricane.

Ten days ago, President Bush signed into law the immediate tax relief package, and I thank Senator Lott for his input, as well as that of Senators Landrieu, Vitter, Cochran, Shelby, and members of this committee—most importantly, Senator Baucus—for working with me in a bipartisan way on that.

Now we hope to pass the immediate health care and income security package as well. Unfortunately, we have run into a Senate speed bump. A few Senators are blocking the bipartisan Finance Committee immediate health care and income security package.

If they were lone rangers, we would have cleared the package by now, at least through the Senate. Unfortunately, the White House is working against me behind the scenes, and I resent that, considering how I have delivered for the White House so much over the last 5 years.

Now, Senator Baucus and I are working together on that package, and we will continue to do so. I appreciate the determination and focus of Senator Baucus. He has put a lot into moving these two immediate packages.

He has heard from the Gulf Coast region, and so have I. What the people there are telling us, is to move very quickly. They especially want us to move quickly on this package of tax relief. As the Governors who appeared before this committee last week told us, time is wasting.

We cannot dilly-dally on Capitol Hill as people in the region face real-world decisions. And that is not just about their immediate health concerns or whether they have a job, but are they going to come back to Louisiana or Mississippi or are they going to stay someplace else, and then that region will suffer longer if they do not go home.

So, to the people of the Gulf Coast, I promise that we will move expeditiously. So I am directing staff to ready the next Finance Committee package for our return from the Columbus Day recess. We intend to continue to work on this package in a bipartisan manner, so I promise to expeditiously move forward.

At the same time, I promise to move with an eye towards the best use of taxpayers' dollars. We need to marry our compassion for the displaced persons and damaged communities with our attention to fiscal discipline.

We need to find the most efficient and effective ways to use the Federal resources under this committee's jurisdiction to carry out the overall policy of rebuilding.

I would like to reiterate four principles designed to guide our consideration of the next phase of the hurricane relief, and these are principles that I also stated to our Governors.

Number one. Market forces are going to have to be the prime mover in getting the region back on its feet. Whatever policy initiatives we look at should be designed to speed up market forces that are already in play.

Number two. Ascertain and deal only with uninsured losses. The taxpayers should not be bailing out insurance companies or underwriters. This principle is a corollary to the first principle. That is, market forces ought to work their will, and losses ought to be borne by those who undertook risk.

Number three. Within the category of uninsured losses previously referred to, we should focus limited Federal resources on those who are most in need. We should focus on small business. In the Gulf region, like most of the rest of America, small businesses were creating most of the new jobs.

Now, that does not mean that large corporations, even multinational corporations, should not be considered in our proposal. It does mean, however, the incentives and loss recovery should not be designed to duplicate what major corporations, multinational or otherwise, are predisposed to do on their own.

Number four, and last. The incentives and loss recovery should be front-loaded and should be time-sensitive. We should send signals to business and others to move aggressively and to move quickly, and for them to feel free to come back to the region, that they will have support.

There should be a distinct beginning and a distinct end to the policies that the Finance Committee is considering. This principle is important for fiscal discipline as well.

Now, in recent days, reports of mismanagement and excessive payments have continued to come from the relief effort. American taxpayers are compassionate, but they rightly expect their hard-earned tax dollars to be spent very wisely.

Now, Congress has hastily approved an open-ended appropriation in excess of \$60 billion. That well-meaning but quickly approved

open-ended appropriation has produced many tales of wild and wasteful spending.

That bill, of course, was not in this committee's jurisdiction. It was not under our watch. It does not mean, from this committee's standpoint, that the Federal Treasury door should be swung wide open for every conceivable tax cut or spending proposal related to the Gulf Coast region. So, as Secretary Snow will be our first witness, I hope he can give me some assurances on that latter point.

Senator Baucus?

**OPENING STATEMENT OF HON. MAX BAUCUS,
A U.S. SENATOR FROM MONTANA**

Senator BAUCUS. Thank you, Mr. Chairman. Thank you for your leadership. As a true leader, as the Chairman of the Finance Committee should, you stepped up when you saw the dire straits in Louisiana and the Gulf Coast and worked with me, and you fashioned a bill which directly helped the people in Louisiana.

You did what was right. You did not listen to those who have bureaucrat reasons why something should not pass, delays that are easily put in place. You were not swayed by politics, you were not swayed by some who were seeking political advantage. Rather, you just stepped up and did what was right, working aggressively and hard to put together, first, a tax package, and second, a health package.

I commend you for that, and I know the people in Louisiana and the Gulf Coast commend you for that. Frankly, I think most people in the country who know about your efforts also commend you for it, and I just want to thank you personally for what you have done.

As you know, Mr. Chairman, 2 weeks ago in this very hearing room we focused on lessons learned from rebuilding in the past, that is, what worked and what did not work. Today, with that perspective, we will examine what specific steps need to be taken to get people in the Gulf Coast communities back on their feet.

As we move forward, I believe we should keep track of three points. The most basic point is, we should put people first. Even before the storm, the affected States represented some of the poorest in America.

Twenty-two percent of Louisianans and 23 percent of Mississippians lived in poverty. About 1 in 5 Louisianans lacked health insurance. Mississippi has the highest percentage of elderly with Medicaid coverage. Texas, the State with the largest number of evacuees, has the highest percentage of uninsured in the country.

Many victims of Katrina did not have the resources to relocate. Many lived in housing that was more susceptible to damage. Thousands of victims, now housed in shelters across the country, lacked the basic safety nets that many Americans take for granted: a savings account, an IRA account with cash to draw on.

Nearly 70 percent of the adult Katrina evacuees surveyed in Houston did not have a bank account, savings account, or a checking account from which they could withdraw money. Seventy percent.

Our primary goal in reconstruction should be how to help these people get back on their feet through various tax measures such as Earned Income Tax Credit, Child Credit, Work Opportunity Tax

Credit, Housing Credits, and other appropriate means, whatever works and what would be pragmatic and practical.

Further, when it comes to helping the working poor, we should consider going beyond the immediate area affected by the hurricanes so that all across the country, the poorest Americans, are not hurt so badly by the next emergency.

Second, when it comes to business incentives, we should focus tightly on the core problems: on infrastructure, transportation, communication, on small businesses that need to rebuild and reinvest, and on natural resource industries like energy, forest products, and agriculture that have suffered huge losses.

I have personally visited the Gulf. I did so a couple of weeks ago. I have staff on the ground today. One person from my staff reported to me just yesterday that employers in St. Bernard Parish have already laid off 10 percent of their employees. With more layoffs expected in the coming months—and we will have more—we have to make sure that these employers have incentives to keep employees and to hire again.

Third, we must spend money wisely. The American people are justifiably angry that their tax dollars seem wasted on a relief effort that, in the first few days, was too little and too late. We must not repeat that experience during the rebuilding.

Montanans are good neighbors. All Americans generally are good neighbors. They want to help, especially in times of need. But they also want there to be a sound plan, coordination among various agencies, and accountability, and that is why Senator Grassley and I sent a letter to the inspectors general that will be charged with overseeing the rebuilding, requesting that they provide recommendations as to what Congressional oversight model will be the most effective in preventing waste, fraud and abuse.

In 1871, in the charcoal shadow of a city that had been leveled by a fire, Francis Test wrote: “Our houses may be burned, but our energies are just the same. They cannot be destroyed.” That is what Francis Test wrote after he survived the Great Chicago Fire. He lost his home, his business. He witnessed a disaster of Biblical proportions, and yet he did not lose hope.

Today, the Gulf region stands in a similar crossroads; much of the Louisiana and Mississippi coastline has been damaged. But the people of the Gulf region are determined to rebuild. We are determined to help them.

So my message to the people in the Gulf is, we are there with you. We are determined to help rebuild the region. We want to do it right. The only thing is, if you are going to do something, do it now. If you do it now, you do it right the first time. We intend to do it right the first time. I look forward to hearing from our witnesses to see how we can accomplish that.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you very much.

We now have Secretary Snow, Secretary of the Treasury, to tell us about the administration’s Gulf Opportunity Zone and how that is seen to help revitalize a region devastated by Katrina.

We appreciate your perspective for the administration. We recognize the efforts of the administration in responding to the needs of

those in the Gulf region, and appreciate the time that you take to be with us.

Secretary Snow, unrelated to your appearance here today, because I know you travel overseas some to represent our government on economic issues, I want to tell you, I watch what you do over there very closely in the Group of Eight, and other meetings you have.

It seems to me you have spent an awful lot of time on international aspects of things affecting our economy, and I think you do a very good job. I just wondered if I could take this opportunity to say to you not only that I think you do a good job there, but when and if you ever see the Chinese again, tell them that I do not think that they have really moved according to the spirit of what they wanted to lead us to believe they were doing with their currency back there in July when they announced that. It seemed to me like it was going to move very quickly, or that there would be adjustments, and I have not seen much benefit from that policy change.

Do you want to proceed now with your testimony for today? I do not expect you to comment on what I said. [Laughter.] Because that is not the purpose of this hearing. I just want to take advantage of your good work overseas; if they care what we in Congress say, I have said it.

**STATEMENT OF HON. JOHN W. SNOW, SECRETARY,
U.S. DEPARTMENT OF THE TREASURY, WASHINGTON, DC**

Secretary SNOW. Thank you very much, Mr. Chairman, Ranking Member Baucus. It is a pleasure to be here. Senator Bunning. I always enjoy the opportunity to appear before the Finance Committee. Let me say that I have reviewed, Mr. Chairman, your statement.

I listened intently to Senator Baucus's statement. I think you have provided, both of you, in your statements, an excellent framework for proceeding, a framework that recognizes the need to size the problem properly.

We need to be fiscally responsible, but we do need to respond. We need to respond in ways that really help the victims and focus the relief on the victims. If we are going to rebuild the area, as certainly is the case, as you are committed to doing, as the President is committed to doing, if we are going to help people rebuild their lives as you are committed to doing, and as we are committed to doing, then we have to rely heavily on incentives to the private sector, because the surest way to rebuild those communities, the surest way to help people rebuild their lives, is to get the private sector investing, creating jobs, and growing and expanding.

That is the idea, basically, behind the Gulf Opportunity Zone. That is the core idea behind the GO Zone, that by providing short-term tax incentives in these zones for the affected area, both small business—through the section 179 expensing, raising the expensing levels from \$100,000 to \$200,000 for a couple of years, and then the 50-percent expensing generally for structures and for equipment—and the energy of the private sector will be unleashed and ignited. And as the energy of the private sector is unleashed, the rebuilding process will be accelerated.

Now, that is the core idea. Complementary ideas, of course, are found in our other proposals for the homesteading, for the credits for employers who hire people in the region, and this very good idea of worker recovery efforts.

They all fit together, and they all tie to your opening statement, Mr. Chairman, that we should target on the real victims. We should employ market forces to encourage the rebuilding. We should focus Federal resources where they do the most good and where they are most needed. We should remember the deficit. This will, for a period of time, elevate the deficit.

But it does not need to take us off the path that we were on to reduce the deficit significantly over the next few years. I think if we manage all of this well, we can help people rebuild their lives. We can help the communities come back. We can also do it in a fiscally responsible way that allows us to achieve our deficit reduction goals.

We will only do that, though, Mr. Chairman, if the principles you laid out, and that Senator Baucus articulated, are adhered to as this process goes forward. With that, I thank you for the opportunity to appear before you.

[The prepared statement of Secretary Snow appears in the appendix.]

The CHAIRMAN. You were a lot shorter than I thought you would be. [Laughter.]

Senator BAUCUS. That is the new sort of technique, be short.

The CHAIRMAN. All right.

Mr. Secretary, once again, thank you for your being here and doing a good job.

There are a number of tax provisions that could be implemented in the Gulf Opportunity Zone in order to encourage investment and development. What makes the provisions that the President has proposed, like bonus depreciation and increased section 179 expensing, the preferred tax provisions for this purpose? And that is not an effort to denigrate it, because I do not disagree with those. But I think we need to flesh out why you think those ought to be a primary tool.

Secretary SNOW. Mr. Chairman, I think there are a couple of reasons why they should be the primary tool. One, they are good tax policy. They use the tax code to create incentives in a way that is consistent with good tax policy.

They, in effect, lower the cost of capital. They make returns on investing capital higher. We know we always get more of everything we tax less. Here, we want more capital in the area because more capital leads to more jobs.

These are tried and true measures. They have worked. We have seen them work. They were incorporated in the legislation that came through this committee, Mr. Chairman, that has put the American economy on this strong path of consistent elevated GDP growth for the last 2½ years, 27 months or so of straight job pick-up, prospects for non-inflationary growth going forward.

What lies at the heart of this extraordinarily good performance that revived the recovery that we are enjoying are the tax policies that came through the Finance Committee that drew on the idea of lowering the cost of capital.

Expensing for small business was part of the 2003 tax proposal. The 50-percent bonus depreciation was part of the proposals that came through in 2002, as I recall, to help get the economy moving again. They have worked.

They are tried and true. We know they work. I am confident that, if we apply them here, that the prior experience will be replicated, and we will see them energize rebuilding efforts in the region.

The CHAIRMAN. Yes. Secretary Snow, the President's proposals on tax incentives, they also fit into a larger plan for Federal relief for the Gulf region. Some of those obviously do not come under your jurisdiction, so maybe I should not expect you to testify.

But I assume you have been in some intra-cabinet discussions of other areas. That is a very broad question that you can give a broad answer to, and I want a broad answer, but also I would like to have you look at other plans that the administration might be figuring in the area of housing.

If you could, tell us how there is interaction between the tax policy and expenditures for housing, so that what we do in this committee would complement, rather than duplicate, efforts.

Secretary SNOW. Yes, Senator. The housing, of course, is provided for, as a measure of initial impression, through the Stafford Act, with the provision for up to \$26,000, I think it is, depending on the circumstances, to be available to people who have lost their housing.

The CHAIRMAN. But that is meant to be for temporary housing, right?

Secretary SNOW. Well, it is a sum of money to help them get through.

The CHAIRMAN. So it could be for a permanent place as well.

Secretary SNOW. It could assist them on that as well.

The CHAIRMAN. All right. Sure.

Secretary SNOW. Then, of course, there is insurance. Many people have access to insurance—flood insurance, housing insurance, mortgage insurance, and so on—which will help them deal with this situation.

Then there is the broad importance, I would say, of a recovering region where people have opportunities to have jobs, make a good living. If we create an environment in which people can make a living, can have jobs, they will be able to borrow and get mortgages, and go to the banks, and savings and loans, and thrifts, and credit unions.

It is critical that we get the region going forward with economic activity, because that will create the jobs; it creates the wherewithal to have the borrowing to rebuild the housing stock in the region. So, I think it all sort of fits together here, Mr. Chairman.

I think it is important as we go forward that we avoid duplication. One of the things I worry about, following on your good statement and Senator Baucus's good opening statement, is that we not look at these things in isolation.

Because if we look at things in isolation, we will be spending money here, and we will be spending money here, and we will be spending money here, and they will be duplicating each other and raising the bill for the taxpayers of the country, or drawing on the

credit of the country, in some way, in ways that go beyond what really is needed.

So, I would follow your opening statement and suggest we really target what we are trying to accomplish, focus on the needy, focus on those who were not insured, and the neediest among them, and make sure that the relief that is being provided is provided in a way that is efficient, effective, targeted, tailored, and not larger than required. We do not want to waste money here.

The CHAIRMAN. Senator Baucus?

Senator BAUCUS. Thank you, Mr. Chairman.

Mr. Secretary, I have two questions. I would like to ask them both, then you respond to both of them after I ask them both.

First, how are we going to measure how well we, the Federal Government, Governors, and so forth, are doing in recovery? What are the metrics? How are we going to quantify, how are we going to measure, whether or not we are doing what we want to do?

In that regard, I might point out, how are we going to measure whether the poor people in the Gulf region get helped, especially because, even though you cite GDP growth, average incomes, and so forth, if you look at the real-wage income of people in that area of the country, in the last couple of years, their wages have actually fallen.

Adult workers' wages have actually fallen. Female full-time workers' wages have fallen. The same with families. The poverty rate has increased during the 3 years after the tax cut. The economy may be doing well at some levels, but for an awful lot of people, they are in worse shape.

So when we talk about recovery, my first question is—and then I will ask a second question later—is how are you going to measure this, and how are we going to focus on poor people who really are a disproportionately high population in that part of the country?

The second question gets to your efforts—the administration's efforts—contrary to those of this committee, and most of us in the Senate, on how to provide health care benefits.

We have legislation that we think makes good sense, legislation that, if passed, would get health care benefits to people right now. The administration has opposed that. The administration says no—waivers. The administration says, well, we could grant waivers to States under current Medicaid law, and that will provide the health care benefits.

In correspondence between Senator Grassley, myself, and the administration, the administration fails to cite any statutory authority under which they think they can give uncompensated care benefits to hospitals whose uncompensated bills are clearly very high due to the disaster.

Second, the administration has said to us, in correspondence, we will work with you to try to make the States whole with respect to Medicaid reimbursement, admitting that they do not have legislative authority to do so.

So on the one hand, the administration talks about waivers to help people. The administration cannot cite statutory authority for waivers with respect to uncompensated care. It cannot do it; it is against the law.

Second, having admitted that it is against the law, they need Congressional support with respect to making States whole under Medicaid reimbursement. So, those are the two basic questions.

Secretary SNOW. Right. Senator, on the first, of course, it is a question that encompasses, but goes way beyond, the people in the Katrina region. You know the statistics as well as I do. There has been a long-term trend suggesting that too many people are not moving up fast enough who are at the lower income levels, and that is contributing to concerns about income inequality.

The fundamental issue there, I think—we have talked about this before—is education, and having an education system that really works, to make sure that everybody gets access to an education that makes them employable, that gives them the skills that are valued in our economy.

It is an economy that is one that is changing and putting greater emphasis on skills, on intellectual skills, which calls for higher commitments to education. The administration, as you know, has some initiatives on that score. This will not change things immediately. It is generational.

But I do think, as we confront the nature of the world and the forces that are at play in a globalized economy, we need to make sure that the citizens of the United States have the skills, the education, the capacity to learn, that will equip them to deal with this.

That is at the center of this income inequality, because the marketplace will reflect the value of people's skills in the marketplace. If they do not have skills, they will not get reflected. The other thing is, you have to keep the economy strong, because where we do not have a strong, growing economy, we do not create jobs. If there are not jobs, it is the poor who suffer the most.

So, here in the Katrina-affected area, I think, as the Chairman said in his opening statement, putting a major emphasis on market forces to incentivize small businesses—which are the engine of job creation—to incentivize small businesses to rebuild or to start up, come in, take administration of the 179 credits—and they are very generous credits, twice the standard of what is available generally.

Senator BAUCUS. My time is running out. Could you address the second question, please?

Secretary SNOW. Yes. I am not really familiar with the issue. I think it is more in Secretary Leavitt's lane than mine. But I will reflect your concerns, as expressed here, to Secretary Leavitt when I see him, in fact, scheduled later today.

Senator BAUCUS. I think you will find the facts are as I stated them to be. The administration does not have the statutory authority.

The CHAIRMAN. If you are going to see Secretary Leavitt, tell him to get the White House to back off of our bill. There are people hurting down there, and we need to get some help to them.

Secretary SNOW. Mr. Chairman, I will reflect those views to Secretary Leavitt, and otherwise.

Senator BAUCUS. And I know my time has expired, Mr. Chairman. But what are the metrics? What criteria? How are we going to measure whether we are getting the job done down there?

Secretary SNOW. Senator, right now there are an awful lot of unemployed people down there. There are an awful lot of businesses

that are shuttered, that are not open. I think we are going to see a good recovery, probably. We want to front-end load it, as I think you and Senator Grassley said. The measure will be, are businesses opened? Do they put out "Help Wanted" signs.

Senator BAUCUS. Mr. Secretary, you were a good businessman. I know when you ran your company that you had to have certain standards that had to be met, certain numbers had to be met in certain categories. I just urge you to come up with those categories and those benchmarks, those numbers, so we can measure whether or not we are doing the job. Thank you.

The CHAIRMAN. Senator Bunning?

Senator BUNNING. Thank you, Mr. Chairman.

Secretary SNOW, it seems to me that one of the first challenges is going to be getting a workforce back in place. Obviously, this is a different challenge than we faced in Lower Manhattan after September 11.

In that instance, while there was disruption of the business community in the localized area, the general workforce was not displaced, so businesses were able to find workers once they were up and running and ready to employ folks.

Is there anything this committee should be considering that would help to address this workforce challenge?

Secretary SNOW. Senator Bunning, that is a very, very good point you are raising. We have, in the package we sent forward, a proposal to provide employers with credits. These credits, I think, are 30 percent of wages up to \$6,000, or something like that.

Senator BUNNING. Yes. But they have to have somebody to employ.

Secretary SNOW. The hope is, and I think the expectation borne out by prior experience is, if we incentivize small business to come back into the region, they will come in. There are thousands of people who were displaced who want to come back.

I met a number of them, as maybe you did, traveling to Houston, traveling to those communities where the displaced people are. They want to go back. As businesses come back up, the businesses will need employees.

Senator BUNNING. Well, they have to have places to live, Secretary. Right now, the place cannot house anyone. You can incentivize all the businesses you want to relocate in a depressed area, but you have to have a workforce to handle that business.

Secretary SNOW. Senator, it will take some time, and it will occur by businesses setting up, looking for people, people wanting to come back, finding temporary housing, going to banks and getting funding and using proceeds of insurance policies to rebuild.

People are intent on rebuilding and going back. I have seen this countless times in conversations with the displaced people. They want to go back, Senator. There is a will here to rebuild.

Senator BUNNING. Well, we will see if they do, and if they can.

Secretary SNOW. There is a will to rebuild.

Senator BUNNING. There is a short window that we are going to have to really accelerate the business community, incentivizing the business community, and then having a workforce.

In your written testimony, you expressed opposition to the Federal Government acting as a backstop for local and municipal bond

issuances. Can you address this concern more fully? What proposals have you heard that cause you concern, and why are you opposed to those proposals?

Secretary SNOW. Senator, this issue is an awfully important one. Some of the proposals we have seen would have the credit of the U.S. Government extended to State and local issuances, to State and local bonds.

That would be a serious mistake. It would be a serious mistake because the investors in U.S. treasuries are investing in treasuries with the expectation that they will not be obligated for State and local bonds.

Senator BUNNING. But is it not true that State and local bonds have a cap? The municipal bond issuances in each State and local area have caps on the amount of money that they can issue bonds for.

Secretary SNOW. They do. But none of that obligation is the responsibility of the general taxpayer.

Senator BUNNING. I am not saying it should be. But I think in this instance, in this type of tragedy, we ought to look at the caps that the Federal Government puts on these local communities and take a look at raising those caps so that they can do for themselves what is needed to be done.

Secretary SNOW. In the context of 9/11, there was some relief granted along those lines, on the private activity bonds and other things. As a matter of general tax policy, we frown on such things, but in extraordinary circumstances like 9/11, they were utilized.

Senator BUNNING. I believe, in tragic displacement and the ability to rebuild, I think this is an event that is just as bad, if not worse.

Secretary SNOW. Senator, it is devastating. This event is devastating. What we are trying to do, and you and the members of the Finance Committee are, is to come up with the right set of policies that are appropriate to these circumstances that do not put the general Treasury or general taxpayers at undue risk.

We want to work with you to help the rebuilding of both the communities and the lives, but consistent with those sorts of principles that the Chairman articulated in his opening statement.

Senator BUNNING. Thank you.

Senator BAUCUS. Mr. Snow, I do not want this hearing to leave the impression that this is the legislative process as usual. That is, we have an emergency here. It has been 6 weeks since Katrina hit, and yet this country is not responding.

The administration, in my judgment, is just not responding in near the way it did after 9/11. After 9/11, this country responded right away, the Congress did, the administration did. We sprung into action.

The Medicaid Katrina health provisions, as the Chairman and I have worked on, we have worked with all the members of this committee on this legislation, we have worked with all the States affected, the Senators of States affected, the Senators as well as the Governors, both sides of the aisle, they all want this legislation passed, and passed now.

The Medicaid benefits that this Congress enacted to help the victims associated with 9/11 was passed right away. We are sug-

gesting the same eligibility requirements for Katrina victims. It has been 6 weeks now. Where is the administration? Where is it? Six weeks.

The administration does not have the authority to do what needs to be done. It is slow-walking, it is opposing, it is obfuscating, it is delaying, it is not acting. We are a country of good people. We want to help people in need. We want to do what is right. We want to respond to people in need.

I must say, I am dumbfounded at the inability, it seems, of this administration to stand up and work to get it done. Again, obfuscation, delay. Not the case with 9/11. With 9/11, boy, we were there. The administration was there.

What is the difference between New York and the Gulf Coast? What is the difference? Why is the administration not responding to the victims of the Gulf Coast?

Secretary SNOW. Senator, I think we are responding.

Senator BAUCUS. No, you are not, Mr. Secretary. You are not when it comes to health care. I am talking about health care needs. You are not, and we must.

Secretary SNOW. Senator, \$62 billion—

Senator BAUCUS. Now, Mr. Secretary, I am not going to let you slide off and not answer the question. I want you to directly, if you can, answer the question with respect to health care needs. The \$62 billion. First of all, most of that is not spent. Most of that is not spent. About \$20 billion is.

In fact, many of us in the Congress are saying, well, maybe you can take the cost of Katrina out of the remaining roughly \$40 billion of the \$62 billion that was appropriated. But we are talking about lower-income people. We are talking about States that need to address their health care needs under Medicaid because of all the huge burdens on those States.

The administration does not have the authority to address those health care needs. I just want you to know, I think this committee has a great sense of urgency. We have acted right away. We did it the right way, and we did not waste time. We thought a bit before we acted. Now we want to act, and the administration is saying no.

Secretary SNOW. Senator, I think the Congress has been very responsive.

Senator BAUCUS. I am talking about the administration.

Secretary SNOW. Well, the administration has worked with the Congress to produce the responses that you have legislated.

Senator BAUCUS. It has not. It has stopped the Katrina health care bill.

Secretary SNOW. Senator, I will look into the health care issues. They do not fall directly in my lane.

Senator BAUCUS. Well, that is what I am talking about right now, is health care.

Secretary SNOW. That falls under Secretary Leavitt. I told you earlier, I will be pleased to speak with him to reflect your concerns there. But I do not have enough knowledge of the specifics of these waivers to be able, really, to elucidate on that subject very well. But I will reflect your concerns.

Senator BAUCUS. Well, I appreciate that, Mr. Secretary. You are the Secretary of Treasury, not Secretary of HHS. However, you are part of the administration.

Secretary SNOW. Right.

Senator BAUCUS. You are part of that team.

Secretary SNOW. Right.

Senator BAUCUS. And I just urge you very strongly to carry the message, and carry it forcefully.

Secretary SNOW. But I would hope you would agree that, outside of this area, you have seen a very responsive administration. We worked with you on the \$62 billion. We worked with you on the individual tax proposals that came through here a week or so ago that were well-conceived legislation. We have sent you our proposals for the GO Zones.

Senator BAUCUS. Right. I understand all that, and that is all good. But I can just tell you, there are also health care needs.

Secretary SNOW. I will look into it.

Senator BAUCUS. If you could pass that on forcefully, aggressively.

Secretary SNOW. I will, Senator.

Senator BAUCUS. Say, hey, you guys, we have to get something done here.

Secretary SNOW. I will.

Senator BAUCUS. Thank you.

The CHAIRMAN. Senator Lincoln?

Senator LINCOLN. Thank you so much, Mr. Chairman. I apologize for running late today. I thank the Chairman and the Ranking Member for bringing us here today, because we have to discuss the issues that have befallen our Nation after Hurricane Katrina and the other disasters that have hit the Gulf, and how we move forward from here, not just in the response to these natural disasters, but also the evidence that it has brought us in terms of where we are as a Nation and the volume of people in this country who are working so desperately to keep their heads above water—no pun intended—in terms of what we have just seen, but certainly the idea of being able to work, to raise a family, and to make a contribution to our American family.

We are one big American family, and the fabric of that family is dependent on whether or not these working families can provide for their children, can provide a home life.

I have to say, as a working mother myself, the one thing—the one, single thing—if we could give to Americans from the U.S. Congress, it would be time. It would be time, Mr. Secretary.

If we could give mothers and fathers the kind of time to spend with their children and their families to create the kind of values in those American families that would then structure and strengthen our American fabric, it would be so critical.

But we have families working two and three jobs just to make ends meet, to make sure their children not only can get to school, but maybe have that one after-school activity, whether it be Scouts, or softball, or what have you.

So, I guess I have already deviated here, but I would like to just bring attention to one thing particularly here in regard to the natural disasters, Mr. Secretary, and that is, it was exactly 1 month

ago today since I began my quest to provide the health care coverage to Katrina survivors through Medicaid.

The Chairman and the Ranking Member have been unbelievably helpful. They have been forceful, they have been strong, they have been willing to work with everybody to try and come up with something that is going to make sense.

We have providers in our State, a month ago, who have been working 24/7, and started working 24/7, who were there, working all throughout Labor Day weekend to be able to provide the kind of care that these dislocated members of our American family needed.

They still do not have the peace of mind to know whether or not they are going to get reimbursed, whether they are going to get adequately reimbursed, whether they are going to have to go to the State and humiliate our State and have our State humiliate the States that are suffering in order to get that reimbursement.

So, Mr. Secretary, I would just say, I have tried hard. I withdrew my amendment in good faith, and certainly believing in my Chairman and Ranking Member here, and they have done everything, and are continuing to do that.

But to my colleagues, and certainly to this administration, I am not giving up. This is not just the other members of our American family from Louisiana, Mississippi, Texas, and Alabama. It is our States, too, because we already are a State where we have high Medicare, high Medicaid provider situations.

If we find that we are not going to get the kind of reimbursements we need, we are going to put in jeopardy the services available to Arkansans. So, I just plead with you, Mr. Secretary. We have not gotten there yet. We will be continuing to offer what we can, but we are going to need your help. It is going to need to be real.

We are going to have to face the reality of what people are seeing in terms of their needs of care, and what providers have been willing to do, without being asked. Without being asked, they have been there and provided what their fellow Americans needed.

So, I sure hope that, as a Nation and as a Federal Government, Mr. Secretary, you can work with the other members of the administration and really come forward to work with us to provide what they need.

But switching gears back to some of the other things that we would like to talk about here today, Mr. Secretary, in the wake of this experience that we have had, it is so important for us to work in a bipartisan spirit for some innovative solutions, for the really unprecedented challenges that we face in our Gulf region.

I really am hopeful that, in the weeks and months ahead, that government at all levels will be able to work in a collaborative effort to address the needs of those who have been so immediately impacted by this disaster.

Secretary SNOW. I agree.

Senator LINCOLN. If we cannot be a "we" country at this time, we should be ashamed of ourselves. If all we are going to focus on is the "me," and who gets credit, and who gets the political win for whatever happens here, we should all be ashamed of ourselves.

I think it is so important that we take seriously our responsibility to address the broader policy issues that these natural disasters, Hurricanes Katrina and Rita, have brought to light, such as emergency preparedness, obviously, community development, and the fact that today, in 2005, in the greatest country on the face of this earth, poverty is still so pervasive, particularly across the South, and indeed across our Nation.

So, Mr. Secretary, America and the world saw the face of poverty very clearly in the aftermath of Katrina. We saw a situation where many of our poorest families were left to fend for themselves, not even able to afford a bus ticket out of town. And I do believe that we have an opportunity here to lift these fellow members of our American family up and give them an opportunity.

We have tried hard, and through the leadership of these two gentlemen in welfare reform and some of the initiatives we have taken with TANF, we have really done, I think, an excellent job in recognizing the unbelievable challenges many of these families face, most of which are working, Mr. Secretary. They are working. They are out there.

In 2001 and 2003, Senator Snowe and I worked together with the President to make sure that working families of many low-income children were included in the Child Tax Credit. You probably are familiar with the debate and how ongoing it has been.

Unfortunately, a recent report highlighted this weekend in the *New York Times*, issued by a nonpartisan tax policy center, showed that almost one-third of the children in this country do not qualify for the Child Tax Credit because their families' earnings are too low.

This is a point I tried to make desperately for 3 years. And when you break the findings down by race, it is even more disheartening. About half of all African American children and half of all Latino children are left out of the full Child Tax Credit because their family earnings are too low to qualify.

In response, Senator Snowe and I have introduced legislation that would build on our previous effort to make this credit work for those who need it really the most, Mr. Secretary.

We would lower the income qualification thresholds to \$10,000. Some wanted to go to \$7,500, because there are people earning that little, Mr. Secretary. This would allow the children of a single mother making minimum wage, working 40 hours a week—every week of the year, mind you—to qualify for this credit.

Under the current version of the Credit in 2004, a single or widowed mother in my State of Arkansas, working full-time at minimum wage, which is \$5.15 an hour, brings home a gross income of \$10,712 a year to take care of her family, and that comes to a threshold.

So I want to know, Mr. Secretary. Can we count on the administration to work with Senator Snowe and myself to correct this inequity and ensure that those low-income, hardworking families that really need this credit to reinvest in their children, in the Nation's future, in the leaders of tomorrow, can we count on the administration to help us with that, that refundability of that child tax credit?

The CHAIRMAN. Mr. Secretary, you can answer that question, but I want that answer to be considered outside the confines of the purpose that we are talking about, helping people with reinvestment and creating jobs. Go ahead and answer it, and then I will go to Senator Schumer.

Senator LINCOLN. Mr. Chairman, I have to say, these are working families that can reinvest.

The CHAIRMAN. I do not disagree with you. In fact, I helped you on that at one time.

Senator LINCOLN. Yes, sir.

The CHAIRMAN. And then we had to back off when we could not get it through the House. So, I do not dispute the facts that you have. But I want to make sure that we are talking about immediate relief because of Katrina, and we would not be having this hearing if it had not been for Katrina.

Answer her question, then I will go to Senator Schumer.

Secretary SNOW. Yes, Senator. We appreciate your comments, and particularly your talk about the outstretched arm of America. I have seen that outstretched arm of America. All parts of America have reached out to help the victims.

Senator LINCOLN. They have.

Secretary SNOW. They really have.

Senator LINCOLN. It has made me proud.

Secretary SNOW. Me, too. It has been a bipartisan effort. I applaud everybody for the way Congress has responded, for the way the business community has responded, the generosity of people in all parts of the hospital community, the NGOs.

On the Child Tax Credit, let me look into it. We will have a conversation with you and Senator Snowe and see if we cannot find some way to work together on it. Generally, indexing ensures, as I understand it, that the intent of a provision keeps pace with inflation, and de-indexing would violate that principle.

But you made an argument that goes beyond that. You are not arguing for Katrina, you are arguing it generally, so we should have a general discussion on that in the context of a broader policy than Katrina, and I will look forward to that.

Senator LINCOLN. Right. I would just remind you, as we talk about de-indexing, these people's wages have not risen and they have stayed stagnant for almost 7, 8 years now.

I would just remind you that a single or widowed parent that is working full-time—full-time, Mr. Secretary—does not even qualify for this benefit to reinvest in their families and in their children.

Thank you, Mr. Chairman.

The CHAIRMAN. Senator Schumer, just a moment. You are going to think this is very unfair. Hear me out, first. I have been very liberal with the time because there were only two or three of us here, and I did not know a lot of other people were going to come in.

So, could I ask you to make your statement, but get your first question in before the fifth minute has evaporated, and then he can answer your question? Because I have five or six other people whom Senator Baucus and I are going to have to live with when everybody else runs for the woods.

Senator BUNNING. Mr. Chairman, some of us have more questions.

The CHAIRMAN. Well, since Senator Baucus had a second round, you will get a second round.

Senator BUNNING. Thank you.

The CHAIRMAN. Go ahead.

Senator SCHUMER. Thank you. Since I come from Brooklyn, I am not running for the woods yet. We do not have any woods left.

The CHAIRMAN. All right.

Senator SCHUMER. First, Mr. Secretary—and thank you for being here—my question is about all this tax relief as a way to help in the Gulf. Normally, I am sort of agnostic as to which works better, spending or tax cuts. In certain places, one works better, in certain places, the other. I do not have this doctrinaire view that it always has to be tax cuts or it always has to be spending.

But I will tell you this. Our experience in New York, which is not totally analogous, was that the spending programs worked much better than the tax cuts, for several reasons.

First, most of the businesses that were hurt were so badly hurt, they did not have any income. To give them tax relief would not matter. Most of the other businesses that you wanted to lure down there with some tax cuts, they were not enough.

There are very few businesses that went back downtown because of tax relief. The one place where tax relief was effective, which really does not apply in New Orleans—it may apply in some other areas—was keeping businesses that were ongoing from leaving.

While we were not totally successful with that—we had some success—but as a result, with the help of both Senator Grassley and Senator Baucus, of the \$20 billion New York City received, \$15 billion was in spending, and that has been spent wisely.

Of the \$5 billion in tax cuts, we have \$2.5 billion that were unused. We are now asking that they be recycled, as I said, with our two leaders' help, into transportation spending.

When I see these numbers bandied about, \$40 billion in tax cuts here, \$60 billion here, I wonder if anyone has taken into account—and I am not saying you, Mr. Secretary, but some of the people from the Gulf whom I understand want to help their people—what works.

I do not think we should just have a grab bag and say, do everything. We just cannot afford it, given our deficit. So that was my first question. Do you have sympathy with that notion?

Secretary SNOW. Senator, I have broad sympathy with the idea that you target tax cuts. Anything like the numbers that you have cited there would be disproportionate to the situation. The tax cuts we have proposed have a cost to the Treasury of only, I think, something on the order of \$1.5 billion. I think beyond that, no, I would agree with you, it would not be efficacious.

Senator SCHUMER. All right. Good.

The second question, since I did not get into the woods yet on my 5 minutes, is this one. It relates to Katrina, but it relates in general to the deficit problem that we have, which many of us are very worried about. I think we on this side of the aisle get a bum rap.

In other words, most of the debt that has piled up in this country has been under Republican presidents, and the one Democratic president we have had in the last while actually had an admirable theory on debt.

Somehow, folks on the other side of the aisle do not think tax cuts—and maybe even this administration—contribute to the deficit. Well, again, I am agnostic. Entitlement programs and spending contributes to the deficit, and tax cuts contribute to the deficit. It is pretty objective.

The numbers I have here are that three-fourths of the publicly held debt in this country, in the history of the country, has been added under the last three Republican presidents.

How can the administration, given the Katrina relief that we are looking at, given the debt situation, given the fact that with the economy not going great, but Greenspan still feels he has to raise interest rates, in part because of the debt situation, how can we justify further tax cuts?

I am not talking to Katrina, targeted in the limited amount that you are talking about, but the overall tax cuts. Given all the spending needs we have and given the inability, when we cut back on spending, for every dollar we cut back on spending, it is much easier to add \$5 to the deficit on tax cuts. Can you tell me how you can justify the administration asking for further tax cuts, given the deficit?

Secretary SNOW. Outside of Katrina?

Senator SCHUMER. Yes. Outside. Yes.

Secretary SNOW. General tax policy. What the administration's proposal is, is to simply extend the provisions that would expire in 2008, the dividends.

Senator SCHUMER. But that makes things worse, does it not, sir?

Secretary SNOW. The dividend and the capital gains, Senator, this is a long philosophical debate. But what we know is that today the revenues of the U.S. Government are rising at a rapid rate. The revenues, the receipts of the U.S. Government, are up some \$100 billion over what was foreseen a year ago.

The reason is, the economy is performing at such a good clip. It is growing way above trend line. Businesses are more profitable. More people are working, some 4 million more working since that tax relief was provided in May of 2003.

So I think the evidence here is pretty clear that what we have is a growing and expanding economy with more people working, with businesses more profitable, directly because of the tax relief that the Congress provided in May of 2003.

Senator SCHUMER. The tax relief has helped create the deficit, has it not?

Secretary SNOW. Senator, no. I think what we have now is the tax relief leading to a strong economy, leading to more receipts, which are critical for closing the gap.

Senator SCHUMER. We have heard that since 1981. As I mentioned to you, three-quarters of the debt has occurred in the three administrations that have had the philosophy that tax cuts lead to so much more growth, that it does not contribute to the deficit.

The facts, sir, are just the opposite. Look at how much the deficit has gone up since George Bush became President. And the bottom line is, the majority of it occurred because of tax cuts.

Secretary SNOW. Senator, I would disagree. I think the majority—

The CHAIRMAN. Senator Schumer, I hope you are going to help us cut taxes to encourage investment down there in Louisiana and Mississippi. That is what we are trying to find out.

Senator SCHUMER. This is a separate question, Mr. Chairman.

The CHAIRMAN. I know it. But you are talking like you do not want tax cuts for investment in Louisiana and Mississippi.

Senator SCHUMER. No. I want them targeted so that they work.

The CHAIRMAN. All right.

Senator SCHUMER. In New York, we did not do as many as are being proposed here, and most of them, or half of them, did not work.

The CHAIRMAN. All right. Go ahead and answer his question. Then I will call on Senator Bunning.

Secretary SNOW. I was going to say, Senator, and I will not belabor the point, but if you do an analytical review of expenditures and receipts over the last 5 years since the President took office, what you find is that the biggest contributor to the deficit is the economy itself, the weak economy the President inherited that led to a recession, then 9/11, which hurt economic activity and led to lots of homeland security rebuilding costs, and then the collapse of the equity markets, which took so much, \$7 trillion, out of the equity values of the country and hurt the tax collection side on capital gains and options and so on. That is really where these numbers come from.

As I say, I think now, with the tax cuts working to create prosperity, we are seeing the receipts rise at a good level. I would be ashamed to lose that because it is going to help close the deficit.

Senator SCHUMER. Thank you.

The CHAIRMAN. Thank you.

If I could take Chairman's privilege here, just for a minute. There was \$580 billion to pay down the national debt when the Republicans controlled Congress. Mr. Greenspan says that this great expansion we have had in money coming into the Federal Treasury and our economy is directly related to the tax cuts of 2001 and 2003.

Lastly, under this tax policy and under the leadership that Senator Baucus and I have had of this committee—and maybe we have not always agreed on all the tax policies, but we sure agreed on the 2001 tax policy—we have, I think, \$220 billion more coming in this year than we anticipated just 8 months ago.

Senator Bunning?

Senator BUNNING. Thank you, Mr. Chairman. The fact is, the number is \$230 billion, but that is all right; give or take \$10 billion here, it is not a big deal.

The fact of the matter is, during the Republican administrations, the proposed tax cuts also were accompanied with spending reductions that were never enacted by our good friends on the other side of the aisle that controlled the House and the Senate at the time. So, there is enough blame to go around.

I have two questions for you. A concern has been raised that some companies may not be able to take full advantage of accelerated depreciation or expensing provisions that are being proposed. One remedy that has been suggested is to extend the loss carry-back period. Is this proposal one that the administration would endorse?

Secretary SNOW. Senator, that was utilized, I think, in 9/11, a 5-year carry-back. It does help get at the problem that you are addressing here. We would be prepared to work with the committee to tailor a proposal along those lines that worked.

Senator BUNNING. All right.

Could you comment on the proposal made by Governor Barbour last week? In particular, he suggested unlimited expensing of investment costs for small businesses, a zero capital gain rate, and a \$50,000 tax credit to rebuild or purchase a new home.

Secretary SNOW. I have not seen the proposals or had a chance to price them out. There is some merit in this idea of lowering capital gains. There is just no doubt about it.

Senator BUNNING. We are talking, just for the area.

Secretary SNOW. I am agreeing. But I am saying, generally, lowering capital gains is a good thing. I think lowering capital gains should—

Senator BUNNING. What about for building homes, a \$50,000 tax credit for those that need to rebuild a home that has been destroyed by Hurricane Katrina or Rita?

Secretary SNOW. Senator, I would want to look at that and price it out and see the cost of it and how it would affect the other things that are being done, because, as I said earlier, I think it is important to look at things in conjunction with the other things we are doing. But we would be prepared to look at it and give you our assessment.

Senator BUNNING. Well, we do have a package that we have been dealing with on Medicare and Medicaid, particularly for Katrina, and we do not seem to be able to come to a conclusion on it.

We will get Secretary Leavitt in the room and make sure that he understands what we are talking about.

Thank you, Mr. Chairman.

The CHAIRMAN. Senator Snowe?

Senator SNOWE. Thank you, Mr. Chairman.

Welcome, Mr. Secretary. A couple of questions. I also chair the Small Business Committee, and one of the concerns that I have had is making sure that the small business applications are expedited in the Gulf region.

We have already gotten estimates of more than 1.4 million applications that have been referred; received: 59,000, pending: 37,000, and very few applications have been approved: just 478. So, obviously, we need to do a better job in expediting those applications.

The point is that, what would assist in this process in making it more efficient is to ensure that we have IRS personnel co-located with the small business personnel so that we could expedite the process of applications. It is important to have those forms readily available to the people to make some decisions, because otherwise people who are applying do not have the documentation that has been destroyed.

So I, the Chairman, and the Ranking Member of this committee sent a letter to the Internal Revenue Service, and Mr. Everson responded by saying, "We will convey our willingness to provide on-site assistance to their disaster assistance workshops."

What I am asking you for today is assurance that that will happen. Are they physically present now?

Secretary SNOW. I do not think so, Senator, but I am told—and this is hearsay—that the IRS has worked out a process with the SBDCs to expedite, in accordance with what you are seeing here, the transmittal of tax receipts to them so the loan process can move faster. But there is an effort under way to move the loan process along.

Senator SNOWE. I know. But I do not understand. Can we have people on-site to do this, to make it more efficient, just to have the actual approval and verification of their tax documents and records, because that will be the only records available?

I mean, I think it really is essential. We have to get beyond, well, it is going to happen, it might happen, they are doing it. We just have to get this done. Frankly, rebuilding the small business component of the area is going to make all the difference in restoring their economic lifeline.

When I see what is pending here for applications, and we only get 478 approved, it tells me we have a huge problem and a major gap. We have to get it done, and IRS can be pivotal in that respect. So can we have them co-located in the Gulf region and make it efficient with the Small Business Development Centers?

Secretary SNOW. I do not see why not, but there may be something I do not understand. We will look into it and see if we cannot do everything possible to expedite this process so these loans can, as you say, get accelerated. We need to get them moved along.

Senator SNOWE. Yes. It is absolutely vital. I mentioned it to some of your people last week here. I really do think it is crucial. We have to move this process along, and I am very concerned about it. If this is the one means to do it, we ought to be providing it. I just do not see why it would be so difficult.

Secretary SNOW. I will get back to you on that.

Senator SNOWE. Would you, please?

One other question on emergency housing tax credits. Is that something you are giving any consideration to as a way of building available housing, using the housing tax credit, increasing caps for States so that they can be eligible to have a pool of money available so we can expedite that process of building?

Secretary SNOW. It may be in the deliberative processes, but I have not seen a review of that proposal yet.

Senator SNOWE. Well, I would hope that that would be something that could be considered as part of the overall package, because I think it really would be useful. It works well now currently, so I think that we could use that model as a basis for rebuilding housing in the region.

Secretary SNOW. Senator, we are prepared to look at a lot of things here. As I said in response to Senator Bunning's question, we have to make sure as we proceed that we take into account what the size of the problem is, what we are trying to fix, and make sure we do not have duplicative approaches, but rather tar-

geted and tailored approaches to get it done. So we have to look at this as a totality, but we will certainly look at this.

Senator SNOWE. Yes. I think, frankly, using working models might help in this instance. It would, I think, prove to be efficient. Thank you, Mr. Secretary.

The CHAIRMAN. Senator Santorum?

Senator SANTORUM. Thank you, Mr. Chairman.

Just to pick up on where Senator Snowe left off, I just want to commend to you the bill that Senator Kerry and I have introduced called the Community Development Home Ownership Tax Credit, which is S. 859, a piece of legislation that I think would help a lot for home ownership for low-income, affordable housing.

I would encourage you to take a look at that as you put together your proposals to try to help both in rehabilitation, as well as home ownership, as we try to reinvest in the Gulf Coast. So, I commend that to you. I do not know if you have a position on that or whether you would comment on that.

Secretary SNOW. Senator, is this the legislation that Secretary Jackson is a champion of and has showed up in the budget? I think we are talking about the same thing, the affordable single-family housing legislation.

Senator SANTORUM. Yes. Yes.

Secretary SNOW. That was part of our original budget. I have heard Secretary Jackson speak positively of it, and it is certainly something we are prepared to work with you on.

Senator SANTORUM. Thank you. I appreciate that, Mr. Secretary.

As we watch the recovery efforts in the Gulf Coast, one of the things that I was struck with—and certainly in talking to people who are evacuees from that area, as well as others who have been working down there—is the incredible role that charities played in the recovery effort. While the bureaucracy may not have responded well, certainly charities did, and people of faith, the churches, in particular, did an outstanding job, and continue to do an outstanding job.

So, I just want to suggest that we consider the CARE Act, which is the charitable giving bill, as part of this recovery effort. If we are going to rebuild communities and neighborhoods, we are going to have to have strong input from the nonprofit sector, from churches, from community groups, civic organizations.

Rebuilding communities is not just putting up houses and starting businesses, it is connecting people, building civic associations, building communities, real communities where people interact and have social capital.

So, I would strongly encourage the administration to get behind the charitable giving provisions of the CARE Act and come forward with something that is supportive of that.

Mr. Secretary, do you have a comment on that?

Secretary SNOW. Well, we are broadly supported, Senator, as you know. The administration is eager to expand charitable giving and provide support for organizations that help serve Americans in need.

That is basically what the CARE Act is all about. So the broad purposes of it, the broad objectives, are something we are in full concert with. You know we tried administratively to do some things

through the IRS and the Treasury Office of Tax Policy to make it easier for people to give, and we want to continue to talk with you and work with you on the CARE legislation. We are in full support of its objectives. There were some technical issues, I think, that our staffs have been talking about.

Senator SANTORUM. Well, I would specifically refer to one provision which I know is not all that popular in some quarters, and that is the non-itemizer deduction. I know that there are many who do not believe that that will raise a lot of money or encourage a lot of charitable giving. I happen to hold a contrary view, depending on how it is constructed.

But the idea that 80 percent of taxpayers in America do not get any tax benefit for giving to charities and are given no incentive to give to charities, to me, ignores a very powerful force out there in giving, and we need to create, in my opinion, and hopefully yours, greater incentives for those who just do not happen to either make a lot of money, or have complex taxes—and a blessing in many respects that they do not have complex taxes—and happen to fill out the short form.

Secretary SNOW. I will look forward to working with you. I agree with the broad objectives here. Absolutely.

Senator SANTORUM. Thank you.

One other, final point. Senator Lieberman and I, when we introduced the CARE Act, included in the CARE Act proposals for Individual Development Accounts. One of the things that, again, if we are trying to build the ownership society the President talks about, again, I would encourage you to look at not only home ownership, but savings, investment, and ownership so we can begin to build folks who have financial literacy, which is a big problem in a lot of our poorer communities, people who have savings accounts, have investments, and are able to use that investment to start a small business or help them with that down payment for the home.

Thank you. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Kyl?

Senator KYL. Thank you, Mr. Chairman.

Mr. Secretary, I understand you had an opportunity to visit with Senator Schumer a little bit about the effect of the capital gains and dividends. It seems to me just a slight review of that is good before I ask you this question.

Much of what I learned, I learned from one of the people who is going to be on the next panel, so I will give you an opportunity to rebut to Hon. Jack Kemp if you would like to do so.

But what I learned from him was that sometimes reducing tax rates actually stimulates economic activity, even to a point at which you end up, if you are interested in revenues to the Federal Treasury, getting more revenue than you would have at the high rates.

Now, when he explained to me that a 100-percent tax rate probably would not generate a lot of tax revenue, the light bulb went on and I got the point.

Now, this President, after 9/11, wanted to stimulate our economy. With the tax cuts of 2001, and then 2003, we have clearly done that. The numbers reveal that, over the last year, we are going to be collecting to the Federal Treasury \$262 billion more in

Federal revenues than we did last year. It is now about \$80 billion more than projected, and probably it will be closer to \$100 billion by the time the year is out.

I have been talking to some folks that represent the investment community. Their view is that we will get over Katrina, from an economic standpoint, relatively quickly, and in fact should have a pretty good fourth quarter.

But the real concern is the signals that some in Congress are sending that, just maybe in the reconciliation bill, we will not do as we projected in the budget, to extend the capital gains and dividends rates currently in effect for 2 more years beyond 2008.

Now, here is the predicate for my question. Some say, well, since they do not expire until then, we can wait to act until then.

The first part of my two-part question is, in terms of an investment horizon, is it the fact that investors are looking maybe 4 and 5 years out to earn the return on their investment, and they are just a little bit interested in what the tax rate is at that time, so that it is important for us to conform the tax rate here to the individual rate and get it until the end of 2010, number one?

Second, as I think you responded to Senator Schumer, with respect to alleged revenue lost to the Treasury, not only does the lower capital gains rate increase revenue to the Treasury, but is it not also true that any savings that would occur, we would not see theoretical savings for 2 years anyway, so it is not something that would be used to pay for Katrina today, this year, or next year, all of which argues, it seems to me, for moving forward to extend the rates for another 2 years on capital gains and dividends. That is my two-part question to you, Mr. Secretary.

Secretary SNOW. Senator, thank you very much. Like you, I have studied under the tutelage of Professor Kemp and agree, obviously, with what you say. The evidence is all before us. The President inherited an economy in steep decline.

The 2001 and 2003 tax reductions, of which the dividends, capital gains, and lower marginal tax rates are the critical parts, put us on a whole different course, a course today where 4 million additional people are working, we have had well above trend line growth for 2½ years, and American companies are highly profitable, businesses are profitable and have strong cash flow, and they are investing. The economy has turned around. The economy, in steep decline, that the President inherited has been turned into an economy of rising prosperity across our land.

And the important point is, the deficit is coming down. Because as more people are working, as businesses are more profitable, as they are expanding and growing, tax receipts go up. That is when you get tax receipts. When equity markets perform well, when businesses perform well, when people are working and have better jobs and wages are rising, tax receipts rise. So, absolutely.

I think you know our position, the administration's position, the Treasury position, is we need to make the tax cuts extended. Make them permanent if you can, but extend them for sure, because the time horizon of investors is always out in the future.

That uncertainty about whether or not those lower marginal tax rates, on whether those dividend rates and capital gains rates will be available to them undermines their investment behaviors. We

do not want to undermine investment behaviors, we want to encourage good investment behavior.

Senator KYL. So the worst thing we could do for the economy generally, and also for rebuilding the economy in the Gulf Region, would be to increase taxes.

Secretary SNOW. In my view, that is absolutely the case.

Senator KYL. Thank you. Thank you, Mr. Secretary.

Thank you, Mr. Chairman.

The CHAIRMAN. Senator Lott?

Senator LOTT. Thank you, Mr. Chairman, for holding this very important hearing. I know that we have had Secretary Snow before the panel for a long while, and I do not want to drag this out too long because we do have other witnesses. But I want to thank Secretary Snow for being here, for the job he does, and for his comments this morning.

Also, it is good to see my good friend, Jack Kemp, here again. I know he will have some interesting things to say. He is passionate about his positions, as always.

If you think I could be described as the Al D'Amato of Mississippi in the past, you ain't seen nothin' yet. [Laughter.] I am just getting started. I want to work on how we can help people who need help.

Senator BAUCUS. And knowing the Senator and watching him the last couple of months, I will second that. [Laughter.]

Senator LOTT. But thank you for being here.

I am also very proud that the second panel will include two outstanding individuals from my own State of Mississippi, Tate Reeves, who is our State treasurer, and Dianne Bolen, who is the executive director of the Mississippi Home Corporation. They are very familiar with our needs in Mississippi regarding bonding and housing issues, respectively, and I will look forward to hearing from them.

I also want to thank our Chairman and Ranking Member for their efforts to be of help to us with the Katrina situation, including passing the Emergency Tax Relief Act of 2005 that is now in effect.

It is providing critical assistance in the form of cash flow relief, employment incentives, housing incentives, taxpayer assistance, and charitable giving incentives. It is helping. It is the most positive thing that we have done in Congress so far.

We have had a lot of good talk, but not a lot of good action yet, but I believe we are going to get it done. I firmly believe that we need to do this in a thoughtful way. We need innovation. We need to do some things differently from what we have done in the past.

I am really intrigued and supportive of the idea of a Gulf Opportunity Zone, a GO Zone. I support that and will offer legislation which I hope the Chairman and the Ranking Member will take up, and that we will push aggressively through the Congress.

We do need to increase the \$100,000 cap on section 179 small business expensing for investment and equipment. The bonus depreciation for purchase of equipment is a necessary feature and one which was employed with success after 9/11.

We do need the investment tax credits to help businesses rebuild, and there are a number of provisions in the GO Zone proposal that I am very excited about and I believe will attract business back,

reinvestment, as well as getting those that were there to move forward aggressively.

As I have looked at our situation in Katrina, at some point you have to begin to get in some order. The number one thing we need is to get people back to work. Once they get a job, we will find them a place to live. Some of them are living and sleeping on their front porches and in tents, and we are trying to get berthing barges, we are trying to get temporary housing.

But once they get a job, everything begins to settle down. We will help them find a place to live. Then their kids will get back in school, and then the clean-up will be completed, and then we will begin construction. So this is so important. We have to have those incentives in there. I do not want to go into more specifics because I want to move on to the next panel.

Just two questions, though, for you, Mr. Secretary. One concern I have is a proposal from some that would exclude certain businesses that are vital in importance to recovery of the Gulf Coast, such as gaming, from the benefits of the GO Zone provisions. I want to be clear that your proposal does not discriminate against various businesses on the Coast. Is that correct?

Secretary SNOW. That is absolutely correct, Senator.

Senator LOTT. And I am saying that as a Southern Baptist, but also as somebody who acknowledges that that industry employed 17,000 people in the Mississippi Gulf Coast before this hurricane, and they have been very responsible in the aftermath.

They have kept their workers on the job. They are helping with the clean-up. The hotels are back open. The State legislature has addressed the issue. We are on track to have them back in business very soon, so I want to make that clear.

Now, the other thing is that the New Market Tax Credits are an existing Treasury program that incentivizes private sector investment in these distressed areas. With minor changes, we could make that applicable to the Gulf Coast. Would you be supportive of that? Have you looked at that?

Secretary SNOW. Yes, Senator. Treasury administers the New Market Tax Credits. We have done two things that I think will be very helpful to the Gulf Coast. You may want to think of things beyond that. But, one, in effect, bonus points for applicants within the zone, within the Gulf zone.

Two, waiver of some application dates, recognizing that people in the area have other things on their mind. That combination of, in effect, bonus points if you are in the zone, with extra consideration for applicants from the zone, will lead to more of the Gulf Zone area applicants being successful. But certainly we would be willing to work with you to talk about other modifications. Those were done administratively, and other things could be done legislatively.

Senator LOTT. Right. Right. Thank you, Mr. Secretary. Our people are hurting and need help. They need incentives. I believe one of the best ways to do it is through the programs that you administer. I look forward to working with you.

Secretary SNOW. Thank you.

Senator LOTT. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Schumer?

Senator SCHUMER. Thank you, Mr. Chairman.

Just one final question. As you know, Mr. Secretary, myself, Senator Graham, and others have been concerned with currency manipulation in China. This is our last opportunity to talk to you before you go over to China in about, I guess, a week.

So let me just say that when you last presented the currency report, you said that you would find manipulation if their behavior did not change in the coming months.

Now, China did revalue by 2.1 percent, but to Senator Graham and I the big saving grace there was that market forces could allow, as fluctuation, as much as 0.3 percent a day.

It was our belief that that would expand the 2.1 percent, because you know the markets, if not manipulated, if the Chinese are not forcing the currency to stay where it is, would have probably gone up.

Instead, what we have found is that, over the 10 weeks since the Chinese announced this policy, the yuan has appreciated less in 10 weeks than China said it would allow it to appreciate in a single day. To me, that is greater evidence of currency manipulation.

I would just like to know your views. What is going to happen on the trip? Will you, if they do not do anything else, stick by your statement that you will find currency manipulation by China? Clearly they are not letting market forces take hold. They are afraid to let go.

Secretary SNOW. Senator, you are right. The Chairman opened with some observations on that same point.

Senator SCHUMER. And that is why I felt I could take the liberty of bringing it up as well.

Secretary SNOW. We will be meeting with the Chinese authorities on economic policy and political leadership to make the case that it is time to see greater flexibility, that the commitment has been made, the initial step was made, but we need to see more flexibility incorporated into the currency, reflecting real demand/supply market forces.

Senator SCHUMER. So if they did nothing else, your view that they are manipulating their currency would be likely to be found in the next report stands? You are not backing off?

Secretary SNOW. Senator, what I said then, I stand by. I want to continue to evaluate the situation.

Senator SCHUMER. All right. Well, I am glad you stand by what you said. Thank you.

Thank you, Mr. Chairman. I appreciate the extra question.

The CHAIRMAN. Mr. Secretary, I want to thank you for appearing, not only for the Treasury Department, but for the Small Business Administration, HHS, and all the other departments you sat in for today.

We are going to call our second panel now, so would the second panel come to the table at this point?

We have a distinguished second panel today to explore how tax relief can help in the rebuilding after Katrina and Rita. We have witnesses that will have particularized knowledge related to the use of enterprise zones.

We are also pleased to have witnesses who bring us firsthand knowledge about the needs of those impacted by the tragedy, and how tax policy might assist in meeting those needs.

As I have noted before, we have a responsibility to use the taxpayers' resources judiciously. I expect our panel this time to help us explore that fiscal responsibility.

We are first going to have Jack Kemp, founder and chairman of Kemp Partners, and honorary co-chairman of the Free Enterprise Fund, who will discuss the potential effectiveness of the Gulf Opportunity Zone. He was a long-time member of Congress before becoming Secretary of HUD.

Then we are going to have the treasurer of Mississippi, already referred to by Senator Lott, Tate Reeves, to discuss the State's economic situation.

Next, Ms. Dianne Bolen, executive director, Mississippi Home Corporation, who will provide us insights on how tax relief will assist in addressing the current housing situation.

Then we will have Mr. Harry Connick, Jr., honorary chair, Operation Home Delivery, Habitat for Humanity International, who will provide us with insights on the housing situation of the impacted area.

Dr. Jane Gravelle, Senior Specialist in Economic Policy of the Congressional Research Service, will speak on enterprise zones.

Last, Mr. James Kelly, chief executive officer, Catholic Charities, Archdiocese of New Orleans, will give us a view as he sees it there.

We will start with Secretary Kemp.

**STATEMENT OF HON. JACK KEMP, FOUNDER AND CHAIRMAN,
KEMP PARTNERS, WASHINGTON, DC**

Mr. KEMP. Thank you, Mr. Chairman. I understand I have 5 minutes. I can go 5 minutes without using a verb. [Laughter.]

As usual, befitting Jack Kemp, I have a rather lengthy testimony that I would like to have included in the record, and I will just read two pages that will summarize the five points that I would like to make today.

First of all, it is a pleasure to be with you. Thank you so much, you and Senator Baucus, for holding these hearings. Thanks to Trent Lott, John Kyl, and Olympia Snowe, old friends from my days in the House of Representatives.

I was thrilled that President Bush announced that his father and President Clinton will lead the relief effort, pleased that Harry Connick, Jr., is leading an effort to put money into Habitat for Humanity, its Operation Home Delivery.

He and I were on the "Today" show a couple of weeks ago and made that announcement, and it is a tremendous effort. Twenty-five million dollars has been raised. But I will let Harry talk about that.

I truly believe this crisis, this catastrophe, is of Biblical proportions, but it has within it the seeds of a great opportunity for the Congress, on a bipartisan basis, to use progressive market-oriented solutions, not only that can work in this challenging moment in history, but will have applicability to similar problems of poverty, despair, and destitution wherever they are, or whenever they might occur in the future.

The huge problem I believe, Mr. Chairman, and members, is of such magnitude that it requires us to think in terms of Abraham Lincoln, and perhaps Franklin Delano Roosevelt, thinking about

the agenda of ownership and shareholder society, where access to education, access to capital, access to a job, access to home ownership is accessible to all people.

One is reminded of the Lincoln Homesteading Act of 1862, his Freedman's Bureau of 1864, Franklin Roosevelt's FHA and GI bill after World War II, and during World War II, actually.

They fit into, I believe, a strategy of combatting poverty and encouraging enterprise, expanding ownership opportunities, and using public/private partnerships, market-oriented solutions to the vexing problems of poverty and despair, particularly in the Gulf.

Keeping Lincoln and Roosevelt in mind, I want to suggest five things real quickly, and then open it up, I guess, to the other people to testify, and then we can answer some questions.

First, a 21st-century urban homesteading act would allow low-income families to homestead on Federally owned properties and those that are under eminent domain. I think that Federal agencies, number two, GSCs such as the Federal Home Loan Bank Board, Fannie Mae, Freddie Mac, FHA, could pool resources, 3 percent of their profits, 5 percent of the profits, to buy out low-income property owners and use these Federal properties available for low-income people to homestead.

Third, it would not be a Kemp testimony if I did not bring up investment capital and getting capital flowing into this green-lined area of our country, at least in the next 5 to 10 years.

President Bush has declared the entire delta, the entire Gulf Port region, an opportunity, empowerment, or enterprise zone, whichever you choose to declare it. We need to flesh out the idea, but here is how I think it might work.

I think, Mr. Chairman, instead of a tax credit—with all due respect, and I do support the New Market Tax Credits—I would eliminate the capital gains tax on any man or any woman who would put his or her surplus savings and capital into the Gulf Port region that would create jobs for people in the Gulf Port region of America.

All investment in new machinery, technology, equipment, and plant should be expensed. Why just do it for a very small business? Why not allow, for 10 years, all investment in the Gulf Port region to be expensed?

Fourth, Mr. Chairman, SBA, the Minority Business Development Agency, CDBG, and other Federal and State monies could be targeted to both urban and rural poverty-stricken areas to be green-lined for special development initiatives. I support the Bush New Market Tax Credits. It could be used for housing ownership, shelter, real estate, and business development.

Fifth, Mr. Chairman, in order to rise above some of the inter-agency turf competition, we might think of appointing proven leaders of national stature, like former Mayor Andy Young of Atlanta, former Mayor Mark Moriall, the president of the Urban League, Bruce Gordon of the NAACP, Colin Powell, Henry Cisneros, former Secretary of Housing. I am chairman of Speaker Hastert's Saving America's Cities task force. I would love to help in any way I can.

I would just make two last points. These are not new ideas. They are not Kemp's ideas. I stole them from Bobby Kennedy in Bedford-Stuyvesant in 1968. He took it from Abraham Lincoln's Home-

steading Act of 1862. Joe Lieberman, Trent Lott, Connie Mack, Eleanor Holmes Norton, Spencer Abraham, Charlie Rangel, Bobby Garcia. There are men and women on both sides of the aisle, Democrat and Republican, who have all advocated doing something extraordinarily big in urban America. Let us apply that to the Gulf Port.

And when it works—and I believe it will work—I think it will be a model for other ghettos and barrios in America where people are really hurting for jobs and access to capital. The single biggest problem for a minority businessman or woman is lack of access to available capital. Thank you very much.

The CHAIRMAN. Thank you, Jack.

[The prepared statement of Mr. Kemp appears in the appendix.]

The CHAIRMAN. Mr. Reeves?

**STATEMENT OF HON. TATE REEVES, STATE TREASURER,
STATE OF MISSISSIPPI, JACKSON, MS**

Mr. REEVES. Thank you, Chairman Grassley, Ranking Member Baucus. Let me begin by saying thank you for your bipartisan support of legislation that is already going to help the Mississippi Gulf Coast rebuild.

Thank you for giving me the opportunity to speak to you today regarding Federal tax policies that may be utilized to expedite the process of getting citizens of South Mississippi back to work, their kids back to school, and the economic engine that drove my State's economy back in gear.

The damage caused by Katrina's path is unimaginable, not just in our coastal counties, but throughout our State. Our infrastructure has been deeply damaged, but our fortitude has only strengthened.

I spent this past Monday with local officials in Harrison and Jackson Counties, the latter of which happens to be the home county of Senator Lott. These places are being led by true leaders, some of the finest men and women America has to offer.

They are not complaining. They are not deserting their constituents. They are simply working day and night to help rebuild their communities in what otherwise would be part-time jobs. They are ordinary people doing extraordinary things.

I do not come before you today asking for a hand-out. Mississippi simply needs a helping hand. While I recognize that this hearing is regarding taxation policy, I would be remiss if I did not ask you to consider the great challenge individuals face with respect to housing.

I would be remiss if I did not urge you to consider the consequences of those in the uninsured and under-insured categories. These people are our friends, our neighbors, our family. They are Americans in need of help from Congress.

I must remind you of the great need for State and local governments to receive direct fiscal aid to help them get through the weeks and months ahead. The State of Mississippi has created a loan program through the Mississippi Development Bank that will guarantee our local governments access to capital.

However, in lieu of direct fiscal relief from the government, the ability to repay those loans will be a major issue for many of our

political subdivisions which have lost a large percentage of their tax base.

I believe that an allowance for a second advance refunding would be crucial for our State and local governments in the intermediate term. The cost to the U.S. Treasury of such an act would be minuscule in comparison to the benefits derived for our local communities.

Generally, one would refinance their debt to achieve net present value savings. In this instance, our State and local governments should be allowed to restructure their debt, possibly delaying several years of principal and interest, until a reasonable time when their tax bases could be reestablished.

In addition, I would encourage you to consider relaxing certain limitations on tax-exempt financing for working capital needs.

While I appreciate the financial commitment that has been, or will be, made by the President, Congress, FEMA, and other Federal agencies, I believe the private sector is the key to Mississippi's renaissance.

For our Gulf Coast region to rebuild as the beautiful place it once was, we must work together to create an environment that encourages the private sector to invest in our communities.

One way to accomplish this goal is through the allowance of \$15 billion in tax-exempt private activity bonds that should be classified as bank-eligible with no limitations. I would encourage you to expand the types of eligible entities allowed under the Liberty Bond legislation.

I would also encourage Congress to consider a special allowance for accelerated depreciation up to 50 percent in the first year for capital investments made in the affected areas.

To fully understand this request and the justification behind it, one must take a step back and consider the types of industries that are located on the Mississippi Gulf Coast: oil refineries, ship building companies, utilities, tourism attractions, defense and aerospace companies, just to name a few.

While the jobs created by these employers are essential to my State's economy, their finished products are essential to keeping America safe. The one common theme within each of these industries is the extent to which they depend on capital investment. We must create incentives to encourage these capital-intensive industries to rebuild.

Many of the items I have outlined today have a precedent in Congress, some do not. An unprecedented disaster requires an unprecedented response.

My Governor, my U.S. Senators, the local elected officials, and most importantly the citizens of my State, have made me proud to be a Mississippian. We have shown resilience in the face of the worst natural disaster in our Nation's history.

We will rebuild our State 1 day at a time, no matter how long it takes. With your help, we will rebuild in a manner that will make all of you proud of what we accomplish together. Thank you.

The CHAIRMAN. Thank you.

[The prepared statement of Mr. Reeves appears in the appendix.]

The CHAIRMAN. Now we go to Ms. Bolen.

**STATEMENT OF DIANNE BOLEN, EXECUTIVE DIRECTOR,
MISSISSIPPI HOME CORPORATION, JACKSON, MS**

Ms. BOLEN. Thank you, Mr. Chairman, Senator Baucus, and distinguished members of the committee. My name is Dianne Bolen. I am the executive director of the Mississippi Home Corporation.

The Mississippi Home Corporation is the State's housing finance agency. Our mission is to provide the opportunity for safe, decent, and affordable housing. We accomplish this mission through the programs that we administer, such as the Mortgage Revenue Bond program, the Mortgage Credit Certificate program, and the Low-Income Housing Tax Credit program.

I appreciate this opportunity to appear before this committee to discuss the housing needs of Mississippi as a result of Hurricane Katrina, and how Congress can assist in the rebuilding of the Gulf Coast.

While over half the State felt the wrath of Katrina, the Gulf Coast suffered catastrophic damage. The 20- to 35-foot tidal surge covered 80 miles of coastal land, going as far inland as several miles.

Some towns were completely wiped off the map, such as Waveland, MS, with a population of 10,000. Infrastructure gone. Debris removal is a daunting task. What used to take a friend of mine 20 minutes to get to work now takes an hour and a half on a good day.

Access to the coast is very limited and restricted in certain areas. Many people lack basic services. Some are living in tents. We can conservatively estimate that a third of the housing stock on the coast was destroyed. Based on the 2000 census, that would come to 31,000 owner-occupied houses and 14,000 rental units. The majority of home owners did not have flood insurance.

Housing prices are going up as we speak. A house selling for \$100,000 before Katrina now sells for \$119,000. Labor to repair houses is in short supply. Mold is a big issue.

The need for housing is great. Mississippi needs more revenue bond cap and low-income housing tax credits, with greater flexibility. I have supplied a series of recommendations in my written testimony for your consideration.

The Mortgage Revenue Bond program and the Low-Income Housing Tax Credit programs are proven tools with a proven delivery system. They are a prime example of public and private partnerships that work. They have a system of accountability that is already in place. These tools are essential to the rebuilding of the Gulf Coast. Thank you so much.

The CHAIRMAN. Thank you very much.

[The prepared statement of Ms. Bolen appears in the appendix.]

The CHAIRMAN. Now we go to Mr. Connick.

STATEMENT OF HARRY CONNICK, JR., HONORARY CHAIR, OPERATION HOME DELIVERY, HABITAT FOR HUMANITY INTERNATIONAL, WASHINGTON, DC

Mr. CONNICK. Thank you, Mr. Chairman and members of the committee. I am honored to be here today to present testimony in hopes of trying to remedy one of the most difficult domestic situations I think we have ever faced as a Nation.

I am not an expert on development, I am not an expert on construction, and certainly not on tax policy, as you probably are already aware, but I am a native New Orleanian who is deeply concerned about the future of the city, and the other post-hurricane affected areas.

I have had the opportunity to visit my hometown. And by the way, I use New Orleans as sort of an example representing the whole Gulf Coast region, but New Orleans is the place I am most familiar with.

I had the opportunity to go there several times since Hurricane Katrina, the first of which was within 2 days of landfall. What I saw there were things that I hope to, but probably will never be able to, erase from my mind.

I saw babies who had not eaten or had anything to drink for days. I saw dead bodies. I saw senseless abandonment by government, desperation. These are things that, as a citizen of this country, you are supposed to see on an international news broadcast.

They are certainly not things that you are supposed to see in our country, much less in your own neighborhood. What profoundly confused me was that these people had the same accent that I have, they ate the same food, they listened to the same music.

Well, over the last few weeks my reason for involvement has become a lot more clear. I think a lot of people have a question as to whether the region should be rebuilt. My question is not whether we should rebuild the region, but rather how to rebuild it and do it in an economically effective and socially acceptable way.

Also, how can we protect this region from any future natural disasters, but at the same time responsibly and respectfully acknowledge the value of human life? In other words, I do not think money should be an object when it comes to keeping these people safe, just because they happen to live in a low-lying area.

I have been named the honorary chairman for Habitat for Humanity in the Gulf Coast relief efforts, which is a great honor for me. I think the Habitat home is a perfect model for the situation that we are in right now. Jack, you could go on and on about the low-cost mortgages, and the no-profit model, and all of that stuff.

What impresses me the most about it is that the people who are going to be occupying these homes are tax-paying, job-holding citizens who are going to help, through sweat equity, build their own houses.

I met a woman in Slidell just 2 days ago who is being presented with a new house. I would be proud to have this woman live next door to me in my neighborhood. I think a lot of people are real freaked out about that.

They are real scared about that. They are scared of the working class, the poor people, perhaps the black people. I have never quite understood that, being raised by parents who are color blind, but I think it is something that needs to be addressed.

I have three suggestions regarding how we can rebuild our community. The first, and this is probably the most confusing to me, is there are over 300,000 families that have been displaced. I guess there are over a million people.

That is the largest displacement in America since the Civil War. Three hundred thousand families. I am sure a great number of

members of those families would love to get back to work and rebuild their own communities.

I think that you all have the power to convey to other people in authority: give these people a chance to get the jobs first. Give them job training. Let them have the opportunities to rebuild their own communities as opposed to passing it off to people not only out of State, but out of the country. I do not understand that.

The second point I would like to make is, as you sit down to your negotiating table, there are a lot of chairs around that table. Pull up a few extra chairs for some local voices to be heard. These people are voiceless.

When I went to the Astrodome and sat down with as many people as I sat down with, they do not feel like they are being represented on this level of government. They feel abandoned. What are they thinking? I mean, they are sitting on a cot, they are sleeping in a stadium. They think they are going back home.

I went to the ninth ward and saw the first Habitat house I had anything to do with. It was called Harry's House on Music Street, because it was on Music Street, and a single mother and her children inhabited this house. It is probably going to have to be torn down, along with acres and blocks and miles of other neighborhoods.

What are these people in the Houston Astrodome thinking right now, and the other evacuees? What are they going to go back to? Who better knows the problems of our city and the patterns that need to be broken than the locals? Give them a chance to speak, too. I venture to say you would be pleasantly surprised at some of their ideas.

The last point is, I think it is important that these poor people are not priced out of these neighborhoods as they are rebuilt. I said before I would be proud to live next to these people. I truly believe that.

We need to start thinking in modern terms. We need to get away from this black/white thing, lower-class/higher-class thing. We need to start thinking in terms of, these are members of our community. These are taxpaying, good citizens.

When I walked into the convention center and I saw 15,000 predominantly black, angry, desperate, hungry people, I did not walk around with a shotgun and a bullet-proof vest. I walked in there and said, I am going to try to get this message out.

One guy even came up to me and said, can you get them to drop some water on us, please? I said, well, you must be so thirsty. He said, no, I want to clean the bathroom. We have a sense of pride here. It was so disgusting in that convention center. This guy just wanted to clean up. These are the types of people we have in New Orleans. They are responsible, good people.

Ironically, the convention center is the same place where we get ready to launch our Mardi Gras parade every year, Orpheus, which is the first interracial, intergender parade in Mardi Gras history. The same black people and white people, men and women that I want in my parade were sitting there in disgrace and humility for days and days and days. They were completely let down on so many levels.

I am not here to point fingers and blame. I just want to be a voice for these voiceless people and plead with you to help find a solution. Again, I am not an expert on all of the things that you know about. I sit here in great awe of you and the institution of government in this great country of ours.

I was in Barcelona for a press event not long ago. Every single journalist from Poland, to Greece, to Russia, to Italy, said, "What the hell happened in your country?" I was embarrassed.

Recently I sang the National Anthem at the Saints game. I am a diehard Saints fan. Do you know anything about football? [Laughter.] I am a diehard Saints fan. I sang the National Anthem. When I got to the line of, can you see the flag over the land of the free and the brave, I am saying, how brave are we right now? I was embarrassed and disgusted at that particular point.

My kids. I have three kids. I think about the Pledge of Allegiance, when they talk about "one Nation." Man, we are not acting like one Nation right now. We need to forget this. We need to treat people with dignity and respect and get these communities back together, black, white, rich, poor. I am proud to be associated with Habitat, and I hope that you will take that under consideration. Thank you.

The CHAIRMAN. Yes. Thank you, Mr. Connick.

[The prepared statement of Mr. Connick appears in the appendix.]

The CHAIRMAN. Now, Dr. Gravelle?

STATEMENT OF DR. JANE GRAVELLE, SENIOR SPECIALIST IN ECONOMIC POLICY, CONGRESSIONAL RESEARCH SERVICE, LIBRARY OF CONGRESS, WASHINGTON, DC

Dr. GRAVELLE. I would like to thank you for the opportunity to be here today.

Direct tax incentives for business have some advantages for rebuilding areas because they work through market mechanisms and therefore will induce the most productive additional investment.

But they are complicated. Because they cannot be received by individuals and firms with no tax liability, it may be difficult to publicize to less-sophisticated taxpayers and can complicate tax administration.

Now, most existing geographically targeted incentives have been directed to chronically depressed areas, often referred to as enterprise zones. The economic efficiency rationale for enterprise zones does not necessarily transfer through a Gulf Zone subsidy, which involves rebuilding a whole area.

The usual rationale that economists suggest for enterprise zone provisions really addresses a labor demand and supply imbalance. The poor areas of the city have unemployment, while businesses located in the suburban fringe have trouble finding employees, so these provisions are designed to encourage businesses to locate in the poor areas.

This philosophy is very different from the justification for rebuilding after a disaster. One argument for subsidies after a disaster is to spread the risk of extraordinary disasters to the country as a whole because imperfect insurance markets prevent firms

from insuring against the loss of business—the absence of customers, the absence of labor—while an area recovers.

Another argument for rebuilding is to preserve the unique cultural heritage of the area. Another is as part of a general social safety net.

A significant body of economic studies of the effects of enterprise zones, largely at the State level, actually has not indicated that enterprise zones have been very effective in inducing investment. Now, this is the evidence we have. It is not necessarily true that that evidence would transfer to rebuilding a whole area, like the Gulf Zone.

The justifications that I have suggested do provide some insight into how subsidies might be designed. The labor imbalance in enterprise zones would suggest that subsidies be made for hiring labor rather than investment. Indeed, investment subsidies, in theory, could actually reduce labor demand by encouraging investment in labor-saving devices.

If the rationale for the Gulf Opportunity Zone is instead insurance against catastrophic risk, the subsidies might appropriately include both labor and capital subsidies to deal with labor- and capital-intensive businesses.

The insurance argument also suggests that aid should be concentrated on preexisting businesses whose gross receipts were predominately in the disaster area. This would include, but not necessarily be limited to, small businesses.

The cultural preservation argument might suggest incentives for preserving or restoring buildings, and specifically for aiding the service industries.

There are two basic types of tax subsidies that might be considered: direct subsidies to firms and indirect subsidies through private activity taxes and bonds, such as the low-income housing credit whose target is really ultimately for renters and not business, and the New Markets Tax Credits.

Of the direct subsidies, investment subsidies tend to have the most bang for the buck compared to capital gains relief, for example. These investment subsidies can be provided through bonus depreciation or through investment credits.

Now, bonus depreciation is neutral if applied to all assets, and that is an important feature for permanent tax policy. But the magnitude for a short-run incentive of bonus depreciation is constrained by the present value of depreciation.

For most equipment investments, 50-percent bonus depreciation is equivalent to reduction of no more than 2 to 3 percent of the cost of the investment. It would be much larger, around 12 percent, for buildings. Section 179 expensing only applies to business equipment investment at the moment.

These tax subsidies provide immediate benefits only for those firms with current or recent tax liability. Now, since many of these firms may not do well this year or may not do well in future years, a possible revision is to extend the carry-back period for these firms or to allow firms to elect a longer carry-back period and a shorter carry-forward period for net operating losses.

The Work Opportunity Tax Credit has already been provided for small employers in the recent bill. That subsidy might be expanded

to larger employers who are already present in the area and derive most of their income from the area, a change that would be consistent with this insurance rationale.

Businesses and individuals without tax liability can benefit from indirect subsidies that are channeled through taxable investors, such as private activity taxes and bonds, low-income housing credits, and the New Markets Credits.

All of these provisions, however, have two very important limitations: they add to complexity and administration costs in structuring some of these investments, particularly, and they can produce windfall gains—indeed, very high gains, high returns—in some cases, for the taxable investors.

Thank you very much.

The CHAIRMAN. Thank you, Dr. Gravelle.

[The prepared statement of Dr. Gravelle appears in the appendix.]

The CHAIRMAN. Now, Mr. Kelly?

**STATEMENT OF JAMES R. KELLY, CHIEF EXECUTIVE OFFICER,
CATHOLIC CHARITIES, ARCHDIOCESE OF NEW ORLEANS,
NEW ORLEANS, LA**

Mr. KELLY. Thank you, Chairman Grassley, Ranking Member Baucus, Senator Bunning, for inviting me here today. I am humbled. Please know how much I appreciate all you are doing to assist us in this tremendous crisis. I come on behalf of the victims of Katrina and Rita, and also on behalf of the poor, both old and new.

Since 1727, the Catholic Church in Louisiana has been providing care to the poor and vulnerable. In fact, Catholic health, education and charities all trace their roots back to the Ninth Ward of New Orleans and the Ursuline nuns.

This past year, Catholic Charities' dedicated staff and volunteers provided services and care to over 125,000 people in the archdiocese in the greater New Orleans area.

Catholic Charities operates 30 programs and services, addressing such issues as hunger, poverty, unemployment, abuse, violence, homelessness, and mental illness. These are all issues and problems that have affected the hundreds of thousands of victims of Katrina, the poor of the past, together with the vulnerable of the present.

Let me tell you about Sherry Jackson, a records administrator, a mother of two, the wife of a New Orleans police officer, who just this past week moved into an apartment after having spent the past 5 weeks in a shelter.

She spent that opening week worrying about her two children and worrying about the safety of her husband. Finally, with the evacuation over, with the violence decreased, he was safe. But as any mother, she continued to worry about her children.

He was afforded a stay on the ships on the 5 nights that he would be working, but on the 2 days that he had off, he would come to Baton Rouge and live and sleep in the shelter with his family. Sherry, by the way, is an employee of Catholic Charities.

Prior to Katrina, we, along with church and city officials, urged folks to leave. Gordon Wadge, my partner in leadership, and I spent Saturday and Sunday helping our residential programs for

the homeless, for the abused, for the mentally ill, and for the mentally retarded, to climb on buses and to evacuate.

Then we decided, as Indians, not as chiefs, to go to the dome to be with the poor. The first 24 hours, we helped transport and administer to the medically fragile. The second 24 hours, we took care of missing and lost children. We waded out of the dome on Tuesday, realizing that we needed to change our roles and begin organizing a massive response and relief effort.

Thanks to our sister agency and Deborah Roe, in Baton Rouge, we were able to set up shop and to begin responding, at first sending counselors to minister to the frail and the sick in Armstrong Airport, reorganizing our Second Harvest Food Bank, and soon shipping 400,000 pounds a day, mobilizing a team of doctors, nurses, and professionals to care for first responders who were in trauma and shock: the police and the firefighters. Subsequently, that team moved on to other fragile populations in other shelters.

Of course, each morning people lined up at the door beginning at 2 or 3 o'clock in the morning, seeking whatever emergency assistance we can provide, like Mary from New Orleans who was flooded out, who was living in a house with 20 other people, four families, looking for a job and a place to live. Also, like Alan, who broke his arm fixing his roof and was laid off, and his wife Tracy, who lost her job at the Hyatt, the hotel without any windows.

Now they wonder how they will get by, how they will eat, how they will pay a mortgage. Hundreds of thousands of victims of Katrina and Rita are in need of a comprehensive array of housing, services, and assistance. FEMA, the Red Cross, the Salvation Army, churches, State, local government, we have all been overwhelmed by the sheer numbers.

Today, over 47,000 people are living in shelters in Louisiana, 35 days without privacy and without dignity. That does not count the thousands living with family, friends, and in motels.

How can we begin to help people put their lives back together—a job, child care, schooling for their kids, medical assistance, and the critical mental health assistance that is so desperately needed—if they do not have a place to call their own, if they do not have a place to begin healing?

They are in dire need of trailers, of waivers, of options. Their brave spirits cannot last another 35 days. I wanted to thank this committee for its development of the bipartisan Health Care Relief Act which provides streamlined access and temporary Medicaid benefits for Katrina's survivors, both inside and outside the region. The 100-percent federally funded provision is essential to covering the physical and mental health care so desperately needed.

I am delighted that you included childless adults, who often do not fit into one of the narrow Medicaid boxes or categories. I spent two hours the Monday night of the hurricane with a mentally ill woman who had become lost from her group, wandering the Superdome. I saw all of the Superdome that evening, for those two hours, and we never found her group.

In addition to housing and health care, there is a need for jobs and temporary assistance. The TANF and unemployment benefits in the hurricane States are among the lowest in the country, especially for people who have nothing left.

The additional TANF assistance and unemployment insurance in your bill will greatly assist, but by no means will be enough. Prior to the hurricane, 22 percent of our State's citizens lived below the poverty line, 30 percent of our children, 47 percent of African Americans. We had one of the highest rates of the uninsured. This was prior to Katrina.

Despite many approaches to create economic enterprise zones and increase employment through business tax credits, it is clear that the Gulf Coast region will need to receive much more Federal assistance to help us rebuild individual lives, families, and communities.

The hurricanes of the past month have reminded us that, in our Nation, too many Americans live in poverty, that tremendous inequalities still exist. The President has called us to reexamine these problems and to reconnect ourselves to finding solutions. While our safety net has some gaps and too many Americans lack economic and educational opportunities, we do have a critically important program that works.

May I end with prayer? But how to pay for all of this, I hope is not on the backs of the poor. The burden of financing and funding programs for the least should fall on those of us blessed with the most. It is not the hungry, the homeless, and the unemployed.

While the stories and photos paint a grim picture, their hopes rest in the faith in God, in our country, and in each one of us today. In Ephesians, we are called to come together to form one body, one spirit, one hope.

To be successful, we will need God's grace and God's speed, and a special spirit of humility, resulting in true collaboration and a real quantifiable success. I pray for your discernment, I pray for your success. I am certain that God will bless you, your families, and your staff for your efforts to help the good and the great people of the Gulf Coast. Thank you.

The CHAIRMAN. Thank you.

[The prepared statement of Mr. Kelly appears in the appendix.]

The CHAIRMAN. Mr. Connick, I had several questions I wanted to ask you. One, because you will be rebuilding homes, if you want to say how many that is, that was one of my questions. But the most important thing I wanted to get from you is, we are grappling with this policy of where to rebuild, and it is a very sensitive issue. So what is Habitat for Humanity's policy in regard to that?

Mr. CONNICK. Well, as far as how many homes are going to be rebuilt, it depends on how much money we raise.

The CHAIRMAN. All right.

Mr. CONNICK. I am very, very involved in raising as much money as we can. With regard to the issues that you are talking about, maybe we should take some cues from Holland when they had that flood in 1953. They said, you know what? We are not going to put a price tag on how important our citizens are. We are going to spend 25 years and \$8 billion to make sure that these people are safe.

I feel the same way about the people in the Ninth Ward. I went back to my house I grew up in Lake View, LA. I had not been in there since I was 12. The door was open, mold all over the place. They are going to have to tear it all down.

Will people want to move back to those neighborhoods? Of course they will. It is just a question of, how can you do it? Is there a scientific way to improve it? I do not know those answers.

The CHAIRMAN. In other words, your nonprofit organization is not dealing with that question now.

Mr. KEMP. Mr. Chairman, I am national chairman of Habitat for Humanity.

The CHAIRMAN. All right. Go ahead.

Mr. KEMP. More Than Houses campaign. We have raised a half-billion dollars in 5 years to build 100,000 homes in low-income communities. There are Habitat chapters in every low-income community and every city in the United States.

They do an assessment, they do their diligence, and they make sure that the family, the home, the property, the city all are involved in the decision as to where it goes, how it is built, and who becomes the taxpayer, as Harry pointed out. So they are on the ground right now, getting ready for the good work the campaign that Harry talked about is going to do for the Gulf Port region.

The CHAIRMAN. All right.

Then my question to you was, of all of the tax incentives we might be talking about, maybe one or two that you would put at the top of the list from your own personal point of view.

Mr. KEMP. Yes. Well, I think the greatest impediment to wealth creation and risk taking is to tax it directly, as in capital gains taxes. I am very disappointed that Dr. Gravelle suggests this is a tax subsidy.

That assumes that the government owns the profit and what it gives back as a lower tax rate on risk taking is a subsidy. I refuse to believe that. It is directly a tax on not the rich; the rich are already rich. It is the poor who cannot get rich on wages. You have to get rich, or richer, or create wealth and start an enterprise and hire people by earning, saving, and investing.

If you look at the low tax, low barrier to entry cities in the United States and in the world, they all point to the fact that enterprise zones, called empowerment zones in Harlem and enterprise zones in DC, supported by Mayor Williams, the Conference of Mayors, the Conference of Black Mayors, the Conference of Black Legislators, the National Governors Conference, all support the idea of a radical surgery on the tax code targeted towards the poorest of the poor to attract capital.

I frankly believe that it would cost absolutely very little because you are creating enterprise, jobs, and expanding the tax base as opposed to just subsidizing people.

The CHAIRMAN. All right.

Mr. Reeves, your use of the tax-exempt bonds. What would you see as the two or three greatest needs there for the use of those?

Mr. REEVES. With respect to the private activity bonds, as I mentioned in my testimony, if you look at the industry that really dots our landscape on the Gulf Coast, you are looking at capital-intensive industries, such as ship builders.

Our largest employer on the Gulf Coast is a major ship builder for the U.S. Government. Our tourism industry employs directly in the gaming industry 14,000 employees. The major ship builder employs 12,000. So, obviously those two areas.

Our oil refinery over in Senator Lott's hometown is another possibility, where the infrastructure of these privately owned facilities was destroyed. We must create an environment whereby we attract the private sector to rebuild their facilities so that we can get individuals back to work so that they can, quite frankly, start providing for the economic rebirth of the region.

The CHAIRMAN. All right. I had other questions, but there is a vote on. I am going to have to defer to Senator Baucus for his questioning, and then I will go vote. I will not come back, so I am saying thank you to all of you. When Senator Baucus gets done, the hearing will be adjourned.

Thank you all very much for your participation.

Senator BAUCUS. Thank you, Mr. Chairman.

I would like to focus on Habitat for Humanity. I have helped build two homes. I was very impressed with the program. Loved it. Working with people there, banging my thumb, everything that goes into building homes. Is there some way we could just build on that and radically expand that? Because I think it is a good model. It is something that is in place, that is working.

Mr. KEMP. Could I make a humble suggestion?

Senator BAUCUS. Yes. Sure.

Mr. KEMP. I have not discussed this with Harry, but as the GSE legislation moves through the House, you might consider allowing the secondary mortgage market to bring Habitat into its fold. Right now, Fannie, Freddie, and Federal Home Loan Bank cannot guarantee or buy down those mortgages.

How about amending the legislation to let Habitat for Humanity participate in the secondary mortgage market? That would be a huge process of liquefying their portfolio, which is close to a half-trillion dollars of mortgages. They then could use that for more homes, not only in the Gulf Port, but in other parts of this country.

Senator BAUCUS. That is an interesting idea. What else comes to mind, if we are going to build on the program?

Mr. KEMP. In my opinion, I was at HUD in 1989, I think, when we amended the Federal Home Loan Bank Board to require them to take 10 percent of their profits and put it into affordable housing. It is very controversial in the House of Representatives. Some of my conservative friends are very much opposed to it. They are afraid it will go to lobbying or something.

You can draw the restrictions at Fannie and at Freddie to make sure that the money does not go to lobbying or to consultants, but goes directly into affordable housing.

So, there is an attempt by Barney Frank of Massachusetts, and I think Mike Oxley of Ohio, to take 3 to 5 percent of Fannie and Freddie's profits and have it dedicated towards affordable housing. You can draw the restrictions in such a way as to make sure that it is free of the lobbying or consulting that everybody seems to be concerned about.

And what other purpose is there for Fannie and Freddie than to help low-income people get a shot at affordable housing? It would also help the banks with their Community Reinvestment Act points.

So, I would urge your staffs on both sides of the aisle, Senator, to look at the testimony here, to look at the Federal Home Loan

Bank Board, as a model of how we can treat Freddie and Fannie as they go through the GSE process.

Senator BAUCUS. Dr. Gravelle, with all due respect to the gentleman on your left who is a very strong advocate of incentives, could you just tell us, in your professional view, which ones work better than others, and what would you recommend from the point of view of efficiency?

Dr. GRAVELLE. Well, I think it is best if you can get the subsidy directly to the person who is going to make an investment, without intermediaries, if you can, so something like an investment credit or perhaps expanding bonus depreciation to structures, because a lot of the businesses in this area they are rebuilding will be done with buildings and not equipment. So, I would think a direct subsidy like that.

Bonus depreciation, as I say, is constrained by its own very nature, so as expensing it can be no better than the difference between present tax depreciation and expensing. So if you wanted to make something bigger, I think you would have to go to an investment credit, which the States actually like, too, because it does not change the taxable income base.

Senator BAUCUS. I do not have much time left here, but both of you from Mississippi, I appreciate your efforts in bonding authority. I was down in Pass Christian a couple, 3 weeks ago and personally saw there was nothing left, so I have some sense of what is happening there, and we very much want to help. But thank you for your efforts and testimony on additional bonding. I agree with you. We have to find some way to make that work.

Mr. Kelly, I want to thank you personally, too. I mean, it is a personal sacrifice you have gone through, clearly. I mean, you have not seen your family in how long?

Mr. KELLY. We were together this weekend.

Senator BAUCUS. Oh, good. Finally.

Mr. KELLY. And I took my son to school on Monday.

Senator BAUCUS. Well, good. I appreciate that. But you are a real servant. Thank you for doing all that you do.

And, Mr. Connick, thank you for speaking out. I just urge you to keep doing it, and maybe talk to some of your other friends in the industry and tell them how important it is, and pass it on. We think it helps a lot for you and others to keep doing what you are doing. So, thank you very, very much.

Mr. CONNICK. Thank you.

Senator BAUCUS. Thanks, everybody. The hearing is adjourned. [Whereupon, at 12:27 p.m., the hearing was concluded.]

A P P E N D I X

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

Testimony of Dianne Bolen

Mr. Chairman, Senator Baucus, and distinguished Members of the Committee:

My name is Dianne Bolen, Executive Director of the Mississippi Home Corporation (MHC). MHC was created by the State of Mississippi as a non-profit housing finance agency to provide the opportunity for safe, decent and affordable housing for all Mississippians. As Mississippi's housing finance agency, MHC administers federal, state and corporate programs relating to housing and furthering the mission of the Corporation.

I appreciate the opportunity to appear before this committee to discuss the housing needs in Mississippi as a result of Hurricane Katrina and how Congress can assist Mississippi in rebuilding the Gulf Coast. Hurricane Katrina struck the State of Mississippi on August 29, 2005. The storm wrought significant devastation not only to Mississippi's Gulf Coast communities, but also throughout other areas of the State. As a result of Katrina's incursion into Mississippi, many of the State's residents find themselves with homes completely destroyed or having sustained significant damage. Many of these residents had no flood insurance.

In the hardest-hit areas of the State, residents still lack water, power, telephone service and basic infrastructure. While debris removal efforts are underway and crews are attempting to restore basic services, the rebuilding process cannot begin immediately. By taking action now using some of the following recommendations, Congress would allow MHC to be ready to finance the construction and purchase of single and multifamily housing units when the Gulf Coast becomes ready to receive its residents.

As of October 2, 2005, 466,000 individuals and families have registered with FEMA, of which 321,000 have been referred for housing assistance. While this does not mean all will qualify for housing assistance, it does provide a preliminary estimate upon which we can base our expectations. More accurate damage assessments are unavailable at the present time. According to the 2000 Census, the total number of housing units of the three Gulf Coast Counties, Jackson, Hancock and Harrison, is 136,111. Of these units, 93,823 are single family owner-occupied houses and 42,288 are rental units. We can conservatively estimate that roughly one-third of the total housing inventory in these Gulf Coast counties—approximately 31,000 single family owner occupied units and approximately 14,000 rental units—have been completely destroyed.

MHC administers several federal programs at the State level, including the Mortgage Revenue Bond program, the Housing Tax Credit program and the Mortgage Credit Certificate program. Because of MHC's experience in affordable housing finance administration in Mississippi for the past twenty years, we are uniquely qualified to aid in the recovery process. In order to use our resources most effectively, we recommend making temporary changes to the Mortgage Revenue Bond program and the Housing Tax

Credit program in order be better prepared to meet the housing needs of the State's residents once they begin to return to the coast.

The following recommendations will allow the Mississippi Home Corporation to quickly and effectively act to meet the housing needs of the hurricane-affected areas of the State:

Housing Tax Credit

- Provide Mississippi with additional Housing Credit authority without reducing authority available to other states. Congress should triple Mississippi's annual per capita Housing Credit allocation for the next five years in order to encourage and accelerate rental housing development in hurricane-affected areas. Under the current \$1.85 annual per capita allocation, Mississippi receives \$5.4 million in Housing Credits annually, which produces about 600 rental units and satisfies only one-third of the state's demand for Credits.
- Designate all Mississippi counties Difficult to Develop Areas (DDAs) for the next five years. At a minimum, Mississippi counties eligible for FEMA Individual and Public Assistance should be granted DDA status. Housing Credit properties located in DDAs—areas with high construction, land, and utility costs relative to median income—are eligible for a 30 percent increase in eligible basis for the purpose of calculating their Credit awards, allowing development of properties that are otherwise financially infeasible. The National Association of Home Builders predicts a 20 percent increase in building costs in Hurricane Katrina-affected areas.
- Allow the award of additional Credits to properties in DDAs—beyond amounts necessary for their development—to provide rental assistance for very low- and extremely low-income families, administered by MHC.
- Allow MHC to amend, with the prior approval of the governor, its Qualified Allocation Plan, without undertaking a public hearing process, so MHC can respond quickly to changing needs and priorities.

Multifamily Bond Issuance

- Provide the Secretary of Treasury explicit authority to promulgate regulations suspending Housing Credit income requirements and occupancy rules in tax-exempt bond financed properties. Treasury and IRS have issued regulations suspending Housing Credit income and occupancy rules to allow Credit property owners to immediately house Katrina victims. However, Treasury says it lacks the authority to extend similar relief to tax-exempt bond-financed Housing Credit apartments.

Mortgage Revenue Bonds

- Substantially increase Mississippi's private activity bond volume cap in each of the next five years to respond to increased housing, industrial development, and

other demands. Based on Mississippi's Mortgage Revenue Bond Program for 2005, the average home price was \$98,000, which based on a \$100,000,000 Bond Issue would yield 1,021 homes. This does not take into account any rise in the cost of construction. The Mississippi Home Corporation (MHC) currently has approximately \$200,000,000 in carryforward private activity cap and another \$200,000,000 in Recycled bonds that it can use toward rebuilding the Coast. This amount would provide funding for the purchase of 4,084 homes. MHC typically issues between \$100,000,000 to \$125,000,000 in Mortgage Revenue Bonds on an annual basis.

- Expand and extend the MRB relief Congress provided in the recently enacted tax relief bill, H.R. 3768. That legislation waives the first-time home buyer requirement in Mississippi's disaster areas and for individuals whose homes Hurricane Katrina destroyed. It also raises the MRB home improvement loan limit to \$150,000 for the repair of residences damaged by Hurricane Katrina. These provisions, set to expire on January 1, 2008, should be extended through December 31, 2010. MHC also asks Congress to increase the MRB income limits to 120/140 percent of the greater of statewide or county median income (consider disaster counties target counties for income purposes) for homes financed in Mississippi's disaster areas for a period of five years, as the Finance Committee has proposed. At a minimum the increased income should apply to individuals whose homes were destroyed or damaged by water and were not covered by their Homeowners Insurance Policy and had no flood insurance because they were not in a flood plain. The increase in income limits would mean that for the three coast counties, the limits would go from a range of \$46,900 (one to two in family) to \$53,935 (Three or more in family) to a range of \$56,280 to \$65,660. The majority of the disaster counties would go from a range of \$40,700 to \$46,805 to \$48,840 to 56,980.
- Allow 100 percent financing on 203 (b) FHA-insured MRB loans. FHA generally requires 3 percent of the home's selling price as a down payment. FHA does have a 100 percent loan for disaster areas called the 203 (h). Lenders are not familiar with this loan product and its requirements. It would be more efficient and cost effective to allow 100 percent financing of the 203 (b) for a period of three to five years for the disaster areas.
- Exempt tax-exempt housing bonds issued by state or local housing finance agencies to support the rebuilding effort from the Alternative Minimum Tax (AMT). Current law provides that interest on private activity bonds is exempt from regular income tax but not the AMT. AMT relief will lower bond yields, allowing MHC to provide MRB mortgages at lower interest rates. By allowing bonds to be issued outside the AMT you also increase the pool of investors buying the bonds. The bonds would yield a 20 to 25 basis point reduction in price that would be passed on to the Home Buyer in the form of a lower mortgage loan rate of 20 to 25 basis points generating a savings over the life of the loan of

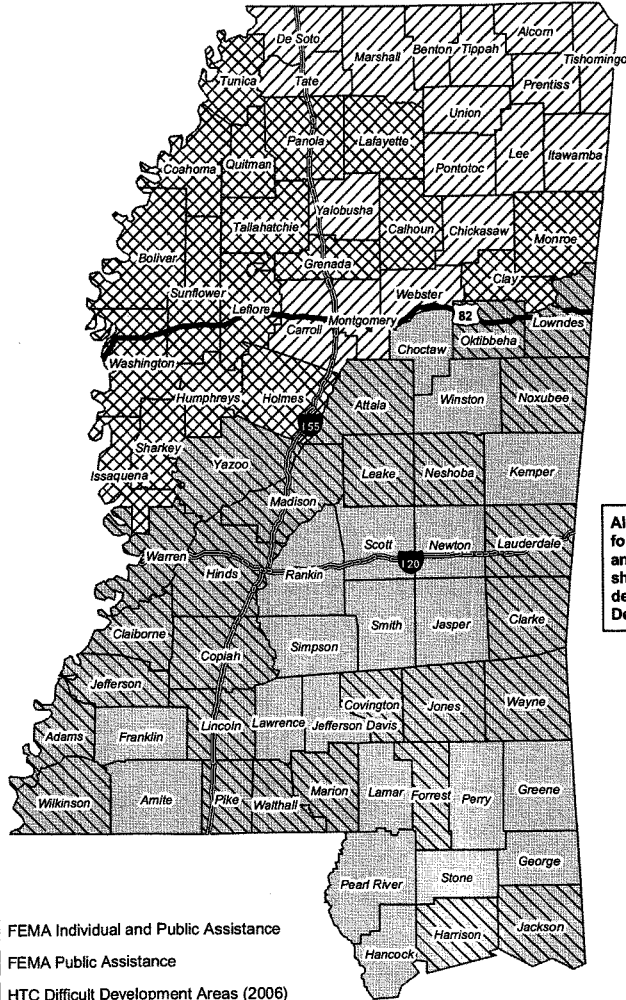
approximately \$6,000. For lower income Home Buyers this can also mean the difference in qualifying for the loan or not qualifying.

- Do not count tax-exempt bonds purchased by corporations in support of the rebuilding effort against their two percent (“de minimis”) safe harbor limit. Freddie Mac has agreed to buy one billion in Mortgage Revenue Bonds from Mississippi, Louisiana, and Alabama by as much as twenty-five basis points below market cost that translates into a twenty-five basis point lower mortgage loan rate to the Home Buyer. MHC is currently working with Freddie Mac on the purchase of our next Bond Issue. As a result of having a known buyer, MHC will be able to reduce the cost associated with Underwriter Fees.
- Direct the IRS to suspend temporarily Purchase Certification documents required to re-verify bond loan compliance in counties eligible for FEMA Individual and Public Assistance, while requiring these documents to be produced as soon as reasonably possible. These documents include the Lender’s Closing Certificate, Borrower’s Affidavit Part II, Affidavit of Seller, and a copy of the HUD-1. MHC is finding that many lenders and attorneys on the Coast have lost all their original documents due to the flooding.




Other Proposals

- Provide developers a single-family tax credit for building homes in FEMA Individual and Public Assistance designated counties for purchase by families with incomes of 120/140 percent (Target Area Requirements) of area median income or less.
- Make Housing Credit and Bond disaster relief permanent to expedite the housing response to future natural disasters.

Mississippi



All counties designated for FEMA Individual and Public Assistance should also be designated as Difficult Development Areas

-  FEMA Individual and Public Assistance
-  FEMA Public Assistance
-  HTC Difficult Development Areas (2006)

For explanations of FEMA assistance see:
<http://www.fema.gov/mm/inassist>
<http://www.fema.gov/mm/pa>

FEMA designations from FEMA Release HQ-05-178 and FEMA-3213-EM, FEMA-1604-DR.
 Map prepared by Mississippi Home Corporation

**Questions for the Record From Ms. Dianne Bolen
October 6, 2005**

From Senator Grassley:

1. Ms. Bolen, the Mortgage Credit Certificate program provides, as you know, a tax credit directly to the home owner.

I am interested in your view on whether the Mortgage Credit Certificate program is widely utilized and if not, are there any changes that you would suggest that would enhance the Mortgage Credit Certificate program so that its use would increase on par with any increases that you would like to see in the mortgage revenue bond financing and low income tax credit housing areas?

According to a 2003 survey conducted by the National Council of State Housing Agencies (NCSHA), only eight Housing Finance Agencies utilize the Mortgage Credit Certificate Program (MCC). As of September 30, the Mississippi Home Corporation (MHC) has originated 41 loans in 2005 with Mortgage Credit Certificates.

I do not know why other states do not utilize more MCC's, but in Mississippi the answer is tied primarily to the borrower's need for assistance with downpayment and closing costs. Borrowers who utilize the MCC program have the option to use MHC's Downpayment Assistance Program which provides downpayment and closing costs in the form of a second mortgage loan. The addition of the second mortgage loan increases the borrower's debt ratio to to a level which, in many cases, disqualifies that borrower from first mortgage loan.

Under the Mortgage Revenue Bond Program (MRB), MHC can provide the downpayment and closing cost assistance in the form of a cash advance as opposed to a loan. Since the cash advance is not a loan, it does not increase the borrower's debt ratio.

In order to enhance the MCC program as it relates to Hurricane Katrina, I suggest the Federal Disaster Areas be declared Target Areas for income purposes. There is a substantial number of displaced homeowners who need our assistance who would qualify for our programs if the disaster area were declared a Target Area.

MHC plans to increase the size of its 2006 MCC program in anticipation of increased demand from borrowers due to the recently enacted H.R. 3768 that provides first time homebuyer relief in the disaster counties.

2. Ms. Bolen, I understand that it may be difficult to predict the obstacles in home building for the gulf region in the coming months given the widespread destruction and the increased demand for supplies and skilled labor.

I would, however, like to get some idea of how long it would take from enactment of the provisions you have suggested to move-in day for the displaced citizens in your State. Could you provide us with some sense of the timing?

Homeownership: MHC's bond issuance process and procedures used by our participating lenders are well established. Originating mortgages can begin immediately for families that wish to buy or build homes in neighborhoods and communities where infrastructure is in place and operational. The size of the homes purchased by MHC borrowers generally require approximately 120 days to construct. The timeframe for families wanting to rebuild on existing lots will depend on when public infrastructure is fully restored. Our best guess would be nine to twelve months. In the most devastated areas along the coastline it could be potentially one to two years before home construction could begin.

Rental: According to MHC's preliminary estimates there are approximately 3,500 renter households from the three gulf coast counties alone that are in need of housing that are at or below 60% area median income for a four person household. Within this group, approximately 2,000 of these households are below 30% of area median income.

Based on our conversations with developers, a 150-unit development requires approximately 12 to 15 months from application submission to approval to construction to the time the first tenants move in. Again, in the most devastated areas on the coast, it could be potentially one to two years before construction could begin.

From Senator Rockefeller:

1. The Low Income Housing Tax Credit is an example of a public private partnership, and the LIHTC Program has been recognized as the most successful affordable housing program. Using Federal tax credits, the program brings private capital into an area that would not otherwise be marketable.

What role should public private partnerships such as the Low Income Housing Tax Credit play in the rebuilding effort?

We agree that the Low Income Housing Tax Credit (LIHTC) should play a key role in the rebuilding of affordable housing in Mississippi. The program has a proven track record of public private partnerships that work effectively. According to MHC's preliminary estimates there are approximately 3,500 renter households from the three gulf coast counties alone that are in need of housing that are at or below 60% area median income for a four person household. Within this group, approximately 2,000 of these households are below 30% of area median income. Assuming developments sized at 150 units, it will take 24 developments to meet the need.

MHC currently receives an annual Housing Tax Credit allocation of approximately \$5.4 million that generates 600 units; therefore, a total allocation of approximately \$32.4 million will be required.

We believe that our LIHTC proposals (increased annual authority, designation of additional Mississippi counties as "Difficult to Develop" areas, ability to amend QAP without public hearing process) will maximize the efforts of the public private partnerships in the rebuilding effort. Furthermore, the LIHTC is the program that best addresses the needs of low-income renters.

From Senator Lincoln:

Do you have an estimate for the affordable housing need in the state of Mississippi as a result of the hurricane? If so, I would like to know what role you believe the Low Income Housing Tax Credit should play in meeting that need.

FEMA has classified damage to homes in five categories: Catastrophic, Extensive, Moderate, Limited, and Flood. By our estimates, approximately 10,000 housing units occupied by families with incomes between \$25,000 and \$54,000 suffered catastrophic damage. The MRB program income maximum limit for this area is \$54,000 for three or more family members. This number represents approximately 65% of the total housing units occupied by this income level and does not include housing units which suffered extensive, flood, moderate or limited damage. In total, MHC estimates that just over

25,000 housing units in the three Gulf Coast counties alone suffered some kind of damage. In addition, MHC's preliminary estimates indicate there are approximately 3,500 renter households from the three gulf coast counties alone that are in need of housing that are at or below 60% area median income for a four person household. Within this group, approximately 2,000 of these households are below 30% of area median income. Assuming developments sized at 150 units, it will take 24 developments to meet the need.

We believe the Low Income Housing Tax Credit Program should play a key role in the rebuilding of affordable housing in the disaster areas for households at or below 60% of the area median income due to the number of renters in that income range who are without housing. The program has a proven track record and will maximize the efforts of the public private partnerships' rebuilding efforts.

**STATEMENT FOR SENATOR BUNNING
SENATE COMMITTEE ON FINANCE**

**“The Future of the Gulf Coast: Using Tax Policy To Help Rebuild
Businesses and Communities and Support Families After Disasters”**

6 October 2005

Thank you, Mr. Chairman.

As this committee considers further legislation to aid those affected by the hurricane disaster in the Gulf region, I am glad that we are taking time to hold this series of hearings.

While it is obviously important to move forward in a timely manner, it is also important to examine in detail the various ideas being presented to aid the region and the steps we have taken with regard to past disasters. I am pleased that efforts are being made to learn from our experiences with prior targeted relief bills, and I expect that the knowledge that we gain will influence any legislation that this committee will produce.

I look forward to hearing from our witnesses today, both the policy experts and those who have been on the ground in the Gulf region.

Thank you.

**STATEMENT OF
HARRY CONNICK, JR.
Honorary Chair, Habitat for Humanity's Operation Home Delivery**

**Before the
United States Senate Committee on Finance
on The Future of the Gulf Coast**

October 6, 2005

Mr. Chairman, members of the committee, thank you for inviting me. I am honored to present testimony which, I hope, will help you remedy one of the most difficult domestic crises we have encountered in my lifetime. I am here today not as an expert on development, construction or tax policy, but as a man, born and raised in New Orleans, who is deeply concerned about the future of his city and the other hurricane-affected areas of the Gulf Coast.

During my three trips to New Orleans after the storm, I experienced humanity as I never thought I would. From horrifying, nameless death to clinging, new life. From relentless suffering to inspirational heroism. From senseless abandonment to unbreakable human spirit. These are scenes I have seen in far away places - not in American neighborhoods, and certainly not in the place I grew up.

Over the past weeks, my reasons for involvement have become clear to me. I want to help restore a sense of community and security among the citizens of New Orleans and the Gulf Coast. My question is not whether the region should be rebuilt; but rather what is the most economically effective, socially acceptable way of rebuilding? How can we make our region safe, while responsibly and respectfully addressing the incalculable worth of human life?

Working with Habitat for Humanity as the honorary Chair of Operation Home Delivery

provides me an avenue to channel this incredible sadness that has devoured my soul. This program is getting people back into homes, back on their feet and on with their lives. Last week, through an amazing outpouring of volunteer support in New York City; Los Angeles and Jackson, Mississippi, Habitat for Humanity built 60 houses in a box for folks in need throughout the Gulf Region.

This past Monday, the first, post-Katrina house was erected in Louisiana. And many more are on their way.

Why are these Habitat houses so important? For many reasons. A house is security, safety and the beginning of stability for the families who have lost so much. But more than that, these houses are the foundations of their new lives and of new, vibrant communities. And it is important to note that these are not trailers or transitional places, but permanent, beautiful homes that people can be proud of. I will never forget the incredible joy and the gleaming smiles I saw on the faces of the single mom and her kids when I handed them the keys to a house I built with Habitat many years ago in New Orleans. Hurricanes destroyed the structures, but it did not destroy the spirit of New Orleans or the other Gulf Coast towns. The people can and will return, and the unique culture and vibrancy will re-emerge. But we must provide the means to rebuild.

I firmly believe that the Habitat for Humanity model is the right one for these circumstances - just as it is for people in need of affordable housing around the country and around the world. Habitat offers low-cost mortgages at no-profit, and asks people to contribute to the building of their own homes through sweat equity. When the homes are completed, the families are secure in the knowledge that this is their home. It is a hand up, not a hand out. And it is the first step to a life of financial and emotional stability.

But Habitat for Humanity offers just one part of the larger rebuilding effort. This effort requires the long-term commitment of the government, corporations, and other non-profit organizations working together toward a renewed and revitalized Gulf Region.

There are more than 300,000 families in the Gulf Region who lost their homes and are waiting for that peace of mind. The hurricane exposed the sad reality of poverty in America. We saw, in all its horrific detail, the vulnerabilities of living in inadequate housing and the heartbreak of losing one's home. There are many ways the government can help right these wrongs. Here are a few ideas:

(1) Habitat's experience proves that peoples' lives are changed for the better when they take part in the building effort. Many of the 300,000 families in need of homes are eager to find work and be part of the rebuilding of their community. You can insure that the people of the region are given priority in the rebuilding jobs, and the training necessary to do the job, as part of restoring their dignity.

(2) Rebuilding New Orleans and the Gulf Coast will involve many decisions that will affect the lives of the people of this devastated area for years to come. No one knows better what was wrong with the old patterns, and what will make life in New Orleans better, for example, than the people who have lived there all their lives. It would only compound the suffering that has already gone on to see homes, parks, schools, and all the other elements of the city rebuilt without the meaningful voice of its citizens at the table. Part of the healing and recovery will be giving the displaced a way to participate in what happens next.

(3) In many cities around the country, when a neighborhood is improved, it is the poor and working people who are the first to be priced out. We already see the first evidence of that in New Orleans as prices are rising in the portions of the city that were less badly flooded. You need to make sure that the rebuilding effort includes enough lower cost homes and apartments for the tens of thousands of New Orleanians with limited income who want to go home. We at Habitat can do much but we cannot meet the need alone.

New Orleans is my essence, my soul, my muse. I will do everything within my power to ease the suffering of my city and ensure she one day recaptures her glory.

I come to you with hope. I have no doubt that the government of this great nation will work with its people to lead New Orleans and the Gulf Coast back to an enlightened, proud, safe part of the world.

Thank you very much for allowing me to share my thoughts. I implore you to make it right, to make us proud.

Statement of Senator Chuck Grassley, Chairman
Finance Committee Hearing, "The Future of the Gulf Coast: Using Tax Policy
to Help Rebuild Businesses and Communities and Support Families after Disasters"
Thursday, Oct. 6, 2005

I'm pleased to call to order this hearing. A little over one week ago, the Senate Finance Committee focused on our second phase of tax relief efforts with respect to the aftermath of Hurricane Katrina. The Finance Committee has responded quickly and decisively to the hurricane. A week and a half ago, President Bush signed into law the immediate tax relief package worked out by the House and Senate. I thank Senator Lott for his input as well as that of Senators Landrieu, Vitter, Cochran, Shelby and members of this Committee. We hope to pass the immediate health care and income security package as well. Unfortunately, we've run into a Senate speed bump on that front. A few senators are blocking the bipartisan Finance Committee immediate health care and income security package. If they were lone rangers, we'd have cleared the package by now. Unfortunately, my guess is our friends at the other end of Pennsylvania Avenue are also involved. Senator Baucus and I are working together on these packages and will continue to do so.

I appreciate the determination and focus Senator Baucus has put into moving the two immediate packages. He has heard from the Gulf Coast region folks. So have I. What they are saying is, move quickly. They especially want us to move quickly on this next package of tax relief. As the governors said last week, time is a-wasting. We can't dilly-dally on Capitol Hill as people in the region face real-world decisions on whether to relocate or not.

So, to the people of the Gulf Coast region, I promise you we will move expeditiously. I'm directing my staff to ready the next Finance Committee package for our return from the Columbus Day recess. We intend to continue to work on this package in a bipartisan manner. So, I promise to expeditiously on the package. At the same time, I want to promise to move with an eye toward the best use of the federal taxpayers' dollar. As I said last week, we need to marry up our compassion for the displaced persons and damaged communities with our attention to fiscal discipline. We need to find the most efficient and effective ways to use the federal resources under this committee's jurisdiction to carry out the overall policy of rebuilding the region. I would like to reiterate four principles designed to guide our consideration of the next phase of hurricane relief.

Principle number one: market forces are going to have to be the prime mover in getting the region back on its feet. Whatever policy initiatives we look at should be designed to speed up market forces that are already in play.

Principle number two: ascertain and deal only with uninsured losses. The taxpayers should not be bailing out insurance companies or underwriters. This principle is a corollary to the first principle. That is, market forces ought to work their will and

losses ought to be borne by those who undertook the risk. That is the capitalist system, after all.

Principle number three: within the category of uninsured losses, we should focus limited federal resources on those who are in most need. We should focus on small businesses. In the Gulf Coast region, like that of the rest of America, small business creates most of the new jobs. It doesn't mean that large multinational corporations should not be considered in our proposals. It does mean the incentives and loss recovery should not be designed to duplicate what multinational businesses are otherwise predisposed to do.

Principle number four: the incentives and loss recovery should be front-loaded and time-sensitive. That is, we should send signals to business and others to move aggressively and quickly back to the region. There should be a distinct beginning and end to the policy the Finance Committee is considering. This principle is important for fiscal discipline as well.

In recent days, reports of mismanagement and excessive payments have continued to come from the relief effort. American taxpayers are compassionate, but rightly expect their hard-earned tax dollars to be spent wisely. Congress hastily approved an open-ended appropriation in excess of \$60 billion. That well-meaning, but quickly-approved open-ended appropriation has produced a lot of tales of wild and wasteful spending. That bill wasn't in this committee's jurisdiction. It wasn't under this committee's watch. It doesn't mean, from this committee's standpoint, the federal Treasury door should be swung wide open for every conceivable tax cut or spending proposal related to the Gulf Coast region. I hope I hear assurances from Secretary Snow on this point.



Statement of Jane G. Gravelle
Senior Specialist in Economic Policy
Congressional Research Service

Before

The Committee on Finance
United States Senate

October 6, 2005

on

Tax Incentives in the Aftermath of Hurricane Katrina

Mr. Chairman and Members of the Committee, I am Jane G. Gravelle, a Senior Specialist in Economic Policy in the Congressional Research Service of the Library of Congress. I would like to thank you for the invitation to appear before you today to discuss tax proposals for economic rebuilding in the aftermath of Hurricane Katrina. Although I discuss options and approaches, please note that the Congressional Research Service takes no position on legislative options.

I would like to discuss the following issues. First, what potential assistance can the federal government offer, and what past examples of geographically targeted incentives exist? Second, what is the economic efficiency rationale for U.S. government involvement in the aftermath of Katrina? Third, what evidence exists for the success of geographically targeted programs, and is this evidence relevant to Katrina? Fourth, what are the implications of the efficiency rationale for the design of tax incentives? And finally, what role can tax incentives play, and how might they be designed to be most effective?

Alternative Approaches to Providing Assistance

Government assistance for rebuilding may involve two types of policies. One is grant assistance. This assistance can be provided to public entities to rebuild the public infrastructure (roads, schools, etc.) which might include port facilities that were formerly privately owned and might include reconstruction of low income housing. Grants, or other assistance, such as credit subsidies, could also be provided to private individuals and businesses. An alternative policy is to provide tax subsidies for private firms. Tax subsidies could also be provided to individuals, for example, to rebuild their homes. Mortgage revenue bonds are an example of tax subsidies directed at homeowners rather than

businesses. Expansion of some of these provisions has already been enacted in the recent tax legislation.

Tax incentives have the advantage of working via market processes, so that the individual additional investment is the most productive of the investments that otherwise would not be made. If subsidies are directed at a specific market “failure,”¹ however, the lack of specific control by the government may be a disadvantage. Other problems with tax subsidies are their potential lack of availability to firms and individuals without tax liability, the difficulty in making less sophisticated firms and individuals aware of the provisions, and the additional administrative complexity in the tax code. Grants or loan subsidies can be targeted to specific uses and might be appropriate for addressing certain types of external effects. A disadvantage of grants and loan subsidies is the bureaucratic process required and the lack of information available to government officials about optimal investments. In both cases, lag time can be a problem.

Current Geographically Targeted Tax Provisions

In his address on September 15, the President’s proposals included a proposal for a Gulf Opportunity Zone that would provide tax subsidies to businesses. Such provisions might be modeled on current enterprise zone provisions.

The main examples of past tax legislation to address disasters are the Liberty Zone provisions adopted in 2002 for the area in lower Manhattan that was affected by the terrorist attacks. These provisions included expansion of the Work Opportunity Tax Credit (WOTC) for small employers, accelerated depreciation for equipment investments and leasehold improvements, increased private activity bonds (which are generally limited by a state cap) and favorable treatment of capital gains realized from the replacement of property. These provisions were originally made available for a few years (varying by incentive), but were extended in most cases through 2010.

Current tax law contains other geographically targeted provisions often referred to as enterprise zones. (Many states have enterprise zone programs as well.) They comprise 40 empowerment zones (30 urban and 10 rural), 95 enterprise communities (65 urban and 30 rural), and 40 renewal communities. Tax incentives for empowerment zones include a 20% employer wage credit for the first \$15,000 of wages for zone residents who work in the zone, an additional \$35,000 (above the \$100,000 generally allowed) in expensing of equipment investments of qualified zone businesses, and expanded tax exempt financing for certain zone facilities. Renewal communities are allowed a 15% wage credit on the first \$10,000 of wages, the additional \$35,000 in capital expensing, and partial expensing of qualified buildings. Enterprise communities receive tax exempt financing benefits. Schools in enterprise communities and empowerment zones are also eligible for qualified zone academy bonds, where the federal government effectively pays the interest on the bonds. These areas are also eligible for special benefits for cleaning up environmentally contaminated areas (brownfields). There are also special provisions for Indian reservations and the District of Columbia. There is also a new markets tax credit for investors, equal to 5% of the original

¹ Market failure is a common term in economics and it refers to circumstances where markets do not work with full efficiency, or where there are external costs and benefits that are not priced. An example is the negative effects of pollution.

investment and for the next two anniversary dates, and a 6% credit for the following four anniversary dates, along with capital gains tax benefits for investors.

New Orleans already has a renewal community designated area, the New Orleans/Jefferson area, on the Mississippi River west of the French Quarter, but it is only a part of the city. There is also a renewal community in Mobile, Alabama. The Treasury has announced that it will give additional consideration to approving new markets coverage for organizations that target their investments to the disaster areas.

These measures indicate the types of geographically targeted tax incentives that have been and are now being allowed: wage credits, accelerated depreciation, tax exempt bond expansion and tax subsidized bonds. There are other options, however, that might include an expansion of the tax credit for rehabilitation of older buildings. This type of provision might be more appropriate for a city with a significant tourism business like New Orleans, whereas lower Manhattan was primarily a financial center.

States adopted enterprise zones well before the federal government did so in 1993. The enterprise zone idea began in the U.K. and many states have since adopted enterprise zones. The earliest state programs began in Florida and Louisiana.²

The recent tax relief bill, H.R. 3768 (The Katrina Emergency Tax Relief Act of 2005, P. L. 109-73), signed by the President on September 23, already contains some measures of these types. It allows a WOTC for individuals affected by the hurricane (through 2005 for employers outside the area and through August of 2007 for employers inside the disaster area), along with an employee retention credit, but limited to firms with no more than 200 employees. It also includes a number of provisions providing benefits to property owners. It allows tax exempt mortgage revenue bond financing for current homeowners (these bonds are currently only available to renters) and increases the limit from \$15,000 to \$150,000 for home improvement loans. It excludes income from the cancellation of indebtedness. The two most significant items (based on revenue costs) are the elimination of casualty loss deduction floors and allowing an extended period of time to avoid gain recognition for involuntary conversions.³

Justification for Subsidies

There is a considerable economic literature discussing both the justifications for geographically targeted subsidies to private business and assessing the effectiveness of these subsidies. In general, economic theory suggests that private market incentives in most cases make subsidies unnecessary or not efficient. Private rebuilding should occur in the absence of tax subsidies, although government construction of essential public infrastructure, such as roads, is vital to any area's recovery. The issue is what speed or magnitude of rebuilding is desirable. Normally the need for subsidies would occur either to achieve distributional

² See Margaret G. Wilder and Barry M. Rubin, "Rhetoric versus Reality: A Review of Studies on State Enterprise Zone Programs." *Journal of the American Planning Association*, Vol. 62, Autumn, 1996, pp. 473-490.

³ Other provisions included charitable giving incentives, tax free withdrawals from IRAs and pension plans, exemptions for sheltering victims, and qualifying for the earned income and child credits based on 2004 income.

objectives or because of market failures — circumstances where an efficient allocation of investment does not occur because of unpriced costs.

The issue often addressed in the economics literature, reflecting the normal goal of enterprise zones and similar policies, is not about rebuilding a devastated area, but about encouraging development in areas that are chronically depressed. There are two efficiency reasons that are commonly given for this intervention. One is that there is a mismatch between available labor supply, and the businesses that need employees — an argument that in general would apply to urban areas, not rural ones. For example, businesses in some outlying areas of the city may find it difficult to locate employees, while unemployment in the inner city may be high. This mismatch causes lower income in the city as a whole and a lower tax base. If transportation costs or lack of knowledge creates a barrier to mobility around the city, one approach is to try to develop the inner city to create jobs for residents. There are, of course, alternative policies, such as providing job matching services and subsidized mass transit for residents of low income areas, or providing low-income housing in areas of the city that are more prosperous. For a variety of reasons these alternatives may not be accepted by the city residents. In addition, city transit systems may not be designed to transport workers out of the central city. Thus, the option of trying to stimulate development in the depressed area may be chosen.

A second efficiency argument is that depressed areas tend to breed more crime which imposes costs on society (both from being a victim of crime and from paying for the resources such as police and prisons needed to deal with crime). This argument might apply to both rural and urban areas.

In either of these cases, the objective is to provide jobs for residents of depressed areas. That rationale suggests that tax subsidies provided should be in the form of wage subsidies, which are more likely than subsidies for investment to produce jobs. Under certain circumstances capital subsidies could actually decrease employment by encouraging labor saving investments. Yet many of the subsidies provided in these geographically targeted areas are subsidies for capital investment.

There is also a concern that the resources drawn into the enterprise zones will be those from a contiguous area that also tends to be poor, since the closest substitutes for businesses within an enterprise zone are the businesses that are located in close proximity.

A second objective is redistributive — to help poor people. The difficulty with this argument is that there is no obvious reason to concentrate government help on poor people who live in the poorest neighborhoods and exclude equally poor people who do not.

There is also the issue of whether intervention should be provided by the federal government or the state government. If the motive is efficiency then the source of funds might depend on who is bearing the costs of that inefficiency, and in the case of revenue base and crime may include both taxpayers in the states and localities and taxpayers across the national in general. If the motive is distributional, then there is more of a case for a national effort, particularly in the case of Hurricane Katrina since the states and localities involved have lost much of their revenue base as well.

In the case of the rebuilding of areas devastated by Hurricane Katrina, the question is whether the standard arguments for enterprise zones can be applied to rebuilding areas that

are not (at least in their entirety) chronically depressed, but have been destroyed by a natural disaster. It is not clear that they can be. Rather, the principal justification for intervention may be largely distributional — the desire to help people who have faced a significant loss to reclaim their lives.

A different efficiency objective may also be invoked in the case of major disasters: aid to devastated areas by the federal government may be viewed as an implicit form of insurance — the country as a whole acts to spread the risk of the cost of natural disasters. If there are imperfect markets for catastrophic insurance, then aid in rebuilding is needed to achieve an efficient allocation of resources. In particular, the cost to businesses in a catastrophe exceeds the loss of property (which can be covered by insurance) because the business also loses its customer base and work force, and it is difficult for private insurance markets to provide coverage for this type of loss due to problems such as moral hazard⁴ (behavioral response on the part of the insured) and adverse selection (since insurance companies are not as fully informed about the health of the companies as the companies themselves, they would expect the companies with inferior prospects to constitute more of their customers and price the insurance too high for the average firm).

Providing relief to businesses affected by disasters by the government can also, however, create its own moral hazard if provided in cases where firms could have been insured (e.g. property insurance). Viewed from this perspective, relief should be limited to extraordinary disasters.

Another potential rationale for rebuilding, especially in New Orleans, is the value of the unique cultural heritage embodied in the city. The existence of a unique city can be said to provide benefits to the country as a whole, even those who may not visit, much as the presence of the Grand Canyon or national parks. It provides value in the option for visiting and a cultural backdrop for novels, movies, and other entertainment media.

Finally, relief may be provided to the region as a part of the risk spreading (across time and across individuals) that is part of the general social safety net, similar to the justifications for Social Security.

Evidence on the Effectiveness of Geographically Targeted Incentive Provisions

State and local zone programs have been around for a longer period of time than have federal programs, and provide most of the basis for empirical studies. While they provide subsidies to both labor and capital, most of these programs tend to rely more heavily on investment subsidies.⁵ They have also commonly tended to provide subsidies for zones in urban areas.

⁴ Moral hazard is another common term used in economic analysis and is a common insurance problem. A standard example is not allowing fire insurance for more than the value of the property, which provides an economic benefit to destroying one's own property. There are more common examples, however, such as unnecessary visits to the doctor when an individual has extensive health insurance.

⁵ See Leslie Papke, "Enterprise Zones," in *The Encyclopedia of Taxation and Tax Policy*, ed. Joseph J. Cordes, Robert W. Ebel, and Jane G. Gravelle (Washington, D.C.: The Urban Institute, forthcoming 2005). An earlier version is available in the 1999 edition of the encyclopedia.

Evidence on the effectiveness of subsidies is unclear. There is a significant body of empirical studies focused mainly on state enterprise zones; in general, most of these studies have not found evidence of effects on growth or employment.⁶ These results do not necessarily mean that there are no positive effects, but rather that the effects are small and difficult to detect statistically. Specific evidence of the empirical effect of federal programs is virtually non-existent and although some studies have found effects, there are some reservations about their methodology.⁷

The U.K., which began the enterprise zone approach (but focused on industrial zones rather than communities), is now allowing the zones to expire after concluding that the source of new activity was relocation from other areas.⁸

The studies, largely from state enterprise zones, constitute the body of empirical evidence available to assess effectiveness. These results, however, may not be very meaningful for measuring the potential effect of aid to rebuild the disaster area. For example, it is possible that depressed areas are so unattractive for business entry that subsidies cannot exceed the threshold to entice new business in, while a subsidy for a less depressed area may do so.

One difference for rebuilding of larger areas of cities, or entire cities, is that it is less likely that any induced investment or growth would come at the expense of other poor communities, since these incentives are not specifically targeted at chronically distressed areas. Rather the investment would be diverted from other uses in general.

Moreover, to the extent that the risk sharing rationale is the argument for providing assistance, the aid may serve its purpose even if it does not induce additional investment. The most important effect might be to lead to a more efficient allocation of investment in the country in general because the expectation of assistance in the event of a major disaster offsets the lack of an actuarially fair insurance market.

⁶ For a brief review, see Leslie Papke, "Enterprise Zones," op. cit. See also Robert T. Greenbaum and John B. Engberg, "The Impact of State Enterprise Zones on Urban Manufacturing Establishments," *Journal of Policy Analysis and Management*, Spring 2004, Vol. 23, pp. 315-339, for a review of the evidence. The authors in this study found very little average effect, but a positive effect on new establishments and a negative effect on existing ones. A more positive outcome was found in a new study of Mississippi enterprise zones. See Jim F. Couch, Keith E. Atkinson, and Lewis H. Smith, "The Impact of Enterprise Zones on Job Creation in Mississippi," *Contemporary Economic Policy*, Vol. 23, April, 2005, pp. 255-260. A more detailed review of some earlier studies can be found in Wilder and Rubin, "Rhetoric versus Reality: A Review of Studies on State Enterprise Zone Programs," op. cit. Other reviews include Don Hirasuna and Joel Michel, "Enterprise Zones: A Review of the Economic theory and Empirical Evidence," Policy Brief, Minnesota House of Representatives Research Department, January 2005; Cynthia L. Rogers and Jill L. Tao, "Quasi-Experimental analysis of Targeted Economic Development Programs: Lessons from Florida," *Economic Development Quarterly*, Vol. 18, August 2004, pp. 269-285; Daniele Bondino and Robert T. Greenbaum, "Decomposing the Impacts: Lessons from a Multistate Analysis of Enterprise Zone Programs," John Glenn Working Paper Series, The Ohio State University, Working Paper, June 2005.

⁷ See General Accounting Office, *Community Development: Federal Revitalization Programs Are Being Implemented, but Data on the Use of Tax Benefits Are Limited*, GAO-04-306, March 2004.

⁸ See Leslie Papke, "Enterprise Zones," op. cit.

There is some very limited evidence on the WOTC in general. A concern about the program has been the possibility of churning employees to repeat the credit. There are some reasons to believe this churning problem is not serious, but there is also some limited information that suggests the WOTC does not have much effect on hiring decisions.⁹

Implications of the Efficiency Rationale for General Focus of Tax Incentives

The design of tax incentives depends partly on the justifications for rebuilding. The traditional enterprise zone focused on creating jobs and increasing labor demand in depressed areas of the city would, at least in theory, be most likely to expand employment if labor subsidies are used. There is no particular reason to limit the incentives to firms that are already present in the area, as attracting new firms may be as important as expanding old ones. Nor is there a particularly reason to focus on small businesses as opposed to large ones.

If the rationale is, instead, to spread the risk caused by localized disasters to the country as a whole, and to focus that risk spreading on the businesses most affected by the disaster, the implications for design are quite different. First, to address the concerns of a range of different types of businesses, some of which are labor intensive and some of which are capital intensive, a range of subsidies might be more appropriate. The subsidies might be particularly focused on businesses that existed prior to the disaster, and also on businesses whose activities (measured, for example, by gross receipts) are concentrated in the disaster area. This design implication suggests that small businesses would be more likely to qualify since such businesses would, by their nature, tend to have more of the receipts concentrated in a single area. Nevertheless, the rationale would not preclude including larger businesses with more employees or a larger asset base. In addition, since the problem with an area wide disaster for business activity extends beyond property damage to the loss of a customer base and a labor force, subsidies to address issues such as housing may also be appropriate.

Based on the rationale of the preservation of the cultural heritage, especially in the New Orleans area, subsidies might be directed towards the construction or reconstruction of historic buildings, which would be accomplished via several mechanisms. It may also suggest that subsidies directed at the service sector might be appropriate.

The Specific Design Issues

Tax subsidies can be provided directly to the target, as in the form of investment subsidies, general tax relief, and wage subsidies for businesses to rebuild. They can also be provided indirectly through private activity tax exempt bonds and programs like the low income housing credit, whose target is not the business itself, but renters, and the new markets credit. They should, of course, have a time limit, but it is difficult to determine what that time period should be.

There are several important observations that might be made about specific design issues.

⁹ See the discussion of the WOTC in U.S. Congress, Committee on the Budget, United States Senate, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, Senate Report 108-54, Washington, DC, U.S. Government Printing Office, Dec. 2004, p. 493.

Direct Investment Subsidies

Investment subsidies reduce the cost of investing. These can be provided through programs such as bonus depreciation and investment credits. It is important, however, to be aware of the magnitude of effects. The value of provisions such as expensing and bonus depreciation depend on the standard depreciation rules. Bonus depreciation is neutral across assets as it proportionally lowers the required rate of return to be a desirable investment. But its magnitude can be small in some cases because the return for short lived property is not a large fraction of the cost. Fifty percent bonus depreciation, for example, is the equivalent, at a tax rate of 35%, to a 2% price reduction for five-year property and a 3% price reduction for seven year property. (The benefits of expensing would be twice as large). The magnitude of benefits is relatively small because the present value of standard depreciation deductions is large and the speed up's value is small relative to asset cost. If 50% bonus depreciation were extended to structures or structural repairs, the benefit would be 12%. If a larger subsidy is desired, an investment credit might be employed.

For capital subsidies, the largest "bang for the buck" tends to come from investment subsidies, rather than tax relief for the return to existing capital (such as lower capital gains rates).

Tax subsidies, in the absence of refundability, benefit only those firms with tax liability. Firms may also not benefit if they have significant carryovers of past losses or credits. Since these firms may not do well in the current or future tax years, a possible revision is to extend the loss carryback period. This extension could be either a simple increase, or an option to elect a longer carryback period and a shorter carryforward period.

Wage Subsidies

The WOTC has already been provided for small employers in the recent tax bill. One important issue is whether the subsidy should be expanded to larger employers who were already present in the area and derived most of their income from the area, a change that is consistent with the insurance rationale.

Indirect Subsidies

Businesses that do not have tax liability can benefit from indirect subsidies that are channeled through taxable investors. There are three types of provisions that might be considered: private activity tax exempt bonds, low income housing credits, and new market tax credits.

One provision that can funnel subsidies to businesses without tax liability is an expansion of private activity tax exempt bonds. Tax exempt bond financing is generally available to State and local governments for financing public capital such as schools and roads. Private activity bonds involve borrowing by the state and local governments and then providing the proceeds to private investors, without a general obligation to pay interest and redeem the bonds if the project fails. Essentially this activity produces a tax subsidy (in the form of lower interest rates); without limits it could become an unlimited subsidy for all private investment. As a result, Congress has limited these private activity bonds to specific uses and to small issues, with volume caps applied by state.

However, providing subsidies through private activity bonds involves a certain degree of inefficiency as they involve intermediaries (which may make them less efficient and can produce windfall gains to high income investors). The exemption of tax on the bond interest allows states to provide funds at a lower rate, but it also tends to create excess returns to high tax rate investors. An alternative to expanded tax exempt bonds, although not a tax program, is to provide direct low cost loans.

Private activity bonds also essentially use federal funds but allow control to rest in the hands of state and local authorities, an outcome that may or may not be desirable.

If additional authority is allowed, it is not clear what the magnitude should be or how long it should be allowed. New York City has not been able to use all of its bond authority. The bond authority might be tied to the needs, but it may also be informative to consider the general magnitude of ongoing activity. According to the latest census data for 2001-2002, the state and local governments of Louisiana had approximately \$21 billion in total outstanding debt, and \$7.5 billion for private purposes. The state and local governments of Mississippi had approximately \$10 billion of debt, with \$2.6 billion for private purposes. The state and local governments of Alabama have \$19 billion of debt and \$3.9 billion in private activity bonds.

A second type of tax provision that provides indirect benefits to those who do not have tax liability is the low income housing credit, which provides significant credits to investors for property when a certain fraction is rented to lower income individuals. As with tax exempt bonds, the state and local governments exercise control. There has been a lively debate in the economics literature about the efficiency of this provision, particularly as compared to alternatives such as rent vouchers.¹⁰ In the short run, rent vouchers may simply bid up housing prices but in the long run, direct construction or supply subsidies may displace housing that would otherwise exist. As in the case of tax exempt bonds, one problem with the subsidy is that the projects are complicated to organize and there may be significant overhead costs. Another is that the investors may receive windfall benefits. Some critics charge that the low income housing credit is part of the corporate tax shelter problem and that investors receive very high returns. Some studies have suggested that states lack complete information on a significant fraction of projects.

Another type of tax benefit that does not directly provide benefits to businesses in the area is the new markets tax credit, which allows investors to receive credits for investments in community development authorities in poor areas. The new markets tax credit is so new that little information is available, but it is likely to suffer from similar problems to the indirect mechanisms above: the possibility of excess returns to investors as well as administrative overhead.

In general these indirect mechanisms involve a tradeoff: they can potentially direct funds to recipients who could not receive tax benefits directly and they use private market

¹⁰ The following discussion is based on Leonard E. Burman and Alastair McFarlane, "Low-Income Housing Credit, in *The Encyclopedia of Taxation and Tax Policy*, ed. Joseph J. Cordes, Robert W. Ebel, and Jane G. Gravelle (Washington, D.C.: The Urban Institute, forthcoming 2005). An earlier version is available in the 1999 edition of the encyclopedia.

mechanisms to some extent, but they also involve administrative overhead and may compensate private investors excessively.

Conclusion

Tax subsidies may play a role in rebuilding the Gulf area and may be justified on several grounds, all of which suggest a range of possible types (for labor and for capital). Evidence from state experience with empowerment zones does not support significant effects, but this evidence, relating to investment in chronically depressed areas, may not be relevant for rebuilding after a disaster. One of the significant challenges with tax policy, particularly in an economically devastated area, is that many of the businesses may not have adequate tax liability to benefit from the provisions. There are some ways of overcoming this problem. One is to extend the loss carryback period. There are also some novel approaches (such as allowing refundable credits, or offsetting payroll taxes) but these approaches have generally not been used in the income tax system and there may be concern about setting precedents. The other approaches, of allowing indirect subsidies (such as private activity bonds) may circumvent this problem, but may also involve significant administrative costs and windfall benefits to investors.



Memorandum

October 21, 2005

TO: Senate Finance Committee
Attention: Nick Wyatt

FROM: Jane G. Gravelle
Senior Specialist in Economic Policy
Government and Finance Division

SUBJECT: Follow-up Questions from Testimony

This memorandum responds to your request for answers to follow-up questions related to the October 6 Senate Finance Committee hearing on “The Future of the Gulf Coast: Using Tax Policy to Help Rebuild Businesses and Communities and Support Families After the Disaster.”

From Senator Grassley:

Dr. Gravelle, I understand there has been some debate about the efficiency of the low income housing tax credit. Could you please comment on that for us?

Any tax subsidy that requires third party investors introduces two inefficiencies relative to direct grants. The first is the cost of collecting the funds from the third party participants. The second is that some of the benefit may accrue to the investors. The low income housing credit appears to have both problems.¹ When individuals are involved, the cost of syndicating the investment is relatively high. Returns to investors were initially extremely high but appear to have fallen over time (although one would expect nominal returns to fall because of the decline in inflation). Corporate investors, especially banks, have been more involved recently, and although these entities do not have the high syndication costs, they have tended to have very large returns; the latest information indicated returns of 15% to 25% in the early 1990s. These returns are very high, especially given the low inflation rates of the time.

¹ The issues discussed in this reply are covered in greater detail in Leonard E. Burman and Alastair McFarlane, “Low-Income Housing Credit, in *The Encyclopedia of Taxation and Tax Policy*, ed. Joseph J. Cordes, Robert W. Ebel, and Jane G. Gravelle (Washington, D.C.: The Urban Institute, forthcoming October 2005) and “Low Income Housing Credit,” in U.S. Senate, Committee on the Budget, *Tax Expenditures: Compendium of Background Material on Individual Provisions*, Committee Print 108-54, Dec. 2004. An earlier version of the encyclopedia article is available in the 1999 edition.

From Senator Santorum:

Could you expand further on the use of current New Market Tax Credits funds for the Gulf Opportunity Zone? How would the logistics of this work? How might this affect current long-term recovery projects in other areas of the U.S.?

The New Market Tax Credits provides credits of 5% for the first three years and 6% for the next four years to investors who invest in Community Development Entities (CDEs) in designated low income areas. The credits are allocated through a competitive application process and are subject to a ceiling. The Treasury indicated on September 9 that it would provide additional consideration to applications from the disaster area and an extension of time to file an application. If funds are allocated to the disaster area and the cap is binding, shifting credits to the disaster area will reduce credits available to other parts of the country. To avoid this effect, one option is to increase the ceiling or provide a separate special ceiling for the disaster area; the latter approach would also have the effect of channeling a specific tax benefit to the area. The current ceiling for 2005 is \$2 billion, rising to \$3.5 billion in 2006 and 2007; at that point the provision expires.

At last week's hearing, George Yin from Joint Tax mentioned bonus depreciation as an incentive for the Gulf Opportunity Zone. Do you agree with his recommendation? If so, in your opinion, what range of depreciation would be necessary to make it a worthwhile investment?

Bonus depreciation should induce additional investment and it has advantages as a long term tax subsidy because it is neutral and cannot lead to negative tax rates. But for a temporary subsidy, neutrality is not important, and a drawback of the provision is that the magnitude is controlled by the present value of depreciation. I estimate that the benefit for equipment investment, where depreciation is relatively rapid, for 50% bonus depreciation, is equivalent to a 2% price reduction in the cost of an asset for five year property and 3% for seven year property, for a taxpayer in the 35% bracket. It is smaller for lower tax brackets and zero for firms without tax liability and the inability to carry deductions backward and forward. Almost all of equipment investment falls into one of these two categories. The effect would be larger for longer lived equipment assets and especially for buildings, where depreciation is much smaller (leading to a 12% price reduction for commercial and industrial buildings). Bonus depreciation was not applied, in the past, to structures, but it could be in this case.

How much investment is induced depends on the responsiveness of investment to a tax subsidy, a value which is difficult to measure. Most empirical studies of structures have not been able to detect an effect, and those for equipment indicate a price elasticity that is relatively small, around -0.25 to -0.66. (These behavioral responses are very difficult to estimate, however, given the lags in investment response). That elasticity means that, for example, with the -0.25 elasticity, a 10% fall in the cost of the investment will lead to a 2.5% increase in investment. For 50% bonus depreciation, therefore, even assuming all firms could use it and assuming a 35% tax rate, for five year property the effect would range from ½ of 1% (for the -0.25 elasticity) to 1.33% (for the -0.66 elasticity) for five year property, and 0.75% to 2% for seven year property. With lower tax rates or for firms that do not have the ability to utilize the deductions immediately because of a lack of taxable income, the effects would be smaller. The effect on cost would be larger for structures but we have very little evidence on these elasticities. There is almost certainly an effect, but, as noted earlier

these effects are very difficult to estimate. The effect during the period should be larger for a temporary incentive.

A second problem with bonus depreciation or most other tax incentives is that the value diminishes (or disappears) for firms without current or prior tax liability. This effect could be remedied, however, by extending the carryback period for net operating losses.

More flexibility might be available with a credit, which could be set to any level desired; the credit would also need to be allowed a carryback period to address firms without tax liability.

We have seen the amazing role charities have played in the relief effort. How do you see their role in the rebuilding effort? What should we be doing here on Capitol Hill to increase giving?

Individuals respond to crises by increasing charitable giving, as we have seen with several recent disasters, and charities are an important part of that response. Using tax incentives to encourage charitable giving and to direct it at the rebuilding effort, however, presents several challenges. The tax system can affect charitable giving by reducing the price of giving, as is currently the case for itemizers who can deduct charitable contributions. Proposals have been made to allow a deduction for non-itemizers as well. One can measure the effectiveness of these incentives by determining the price elasticity. If it is above one, a dollar of tax revenue loss stimulates more than a dollar of charitable contributions; if it is below one, a dollar of loss stimulates less than a dollar and it would be more efficient to provide grants to charities. While earlier estimates of charitable giving had found evidence of elasticities above one, a more recent study that controlled for timing effects found lower elasticities, of around -0.5^2 . If this elasticity is correct, a dollar of revenue loss would generate \$0.50 of contributions.

This low elasticity may simply mean that actions reflecting charitable motives are less sensitive to price than is the case with other types of transactions. There are no estimates of the responsiveness of corporations to price incentives although it is possible those responses could be larger.

A second problem with using general charitable contributions incentives for the rebuilding effort in the Gulf area is that only a small part of charitable giving would likely be funneled to that area unless any additional incentive were made contingent on contributing to that area. Charitable contributions go to many different uses. For example, excluding foundations (which are intermediaries), according to Giving USA less than 10% of giving in 2004 went to human services. While other recipients of charitable funds provide human services and related benefits (such as health and education), only a fraction is likely to go to the purposes envisioned. In addition, charitable contributions benefit all areas of the country and thus only a small fraction of general giving would be expected to go to the disaster area.

There are two ways to increase the efficiency of any additional charitable incentive. The first is to allow only charitable deductions or any other incentive (such as a credit) over a floor, which could either be a dollar floor or a percentage of income. The latter would

² Randolph, William C., "Dynamic Income, Progressive Taxes, and the Timing of Charitable Contributions," *Journal of Political Economy*. vol. 103, Aug. 1995, pp. 709-38.

probably be a more efficient floor since contributions rise with income. The second is to make any additional benefit contingent on spending for specific purposes in the Gulf area. (Some changes have already been made with in H.R. 3768, the recent Katrina tax relief bill with the latter restriction in mind). Both modifications, and especially the second one, would present some administrative problems.

From Senator Baucus

You have testified that capital subsidies can actually decrease employment but capital subsidies seem to be the tool most often used in these targeted zones. Could you explain the difference between capital and labor subsidies? And, what are the capital subsidies in the President's GO Zone proposal and are there sufficient offsetting labor subsidies?

Capital subsidies reduce the cost of acquiring equipment and/or structures and include provisions such as expensing of investments, bonus depreciation, capital gains reductions, and indirect subsidies such as expanded private activity tax exempt bonds. While they increase investment and output, they can also reduce the demand for labor by encouraging businesses to substitute capital for labor. Labor subsidies include provisions that reduce the cost of hiring labor, usually by providing a wage credit. The recent Katrina tax relief bill (H.R. 3768) included a limited wage subsidy, an expansion of the Work Opportunity Tax Credit (WOTC) to former residents of the disaster area, to extend through 2007. Current geographically targeted tax provisions include, along with capital subsidies, wage credits (in the case of enterprise zones and renewal communities).

The President's GO Zone proposal includes only capital subsidies: an increase in expensing for small businesses, 50% bonus depreciation (apparently for equipment), and some type of unspecified provision for structures.

You've identified as a significant challenge the fact that many of the businesses in the disaster zone may not have adequate tax liability to benefit from some incentives. What incentives are you referring to that may go under-utilized or wasted?

Any direct provision to the firms may be of limited use to some firms because of the restrictions on the carryback and carryforward of losses. If the benefits are large relative to income, as may be the case with a significant investment program and if the firms experience significant current and short term losses, even previously profitable firms may not have enough tax liability to use these provisions. Moreover, benefits of provisions such as accelerated depreciation depend on timing. Examples of these types of benefits that may not be used by many firms include expensing, bonus depreciation, and any type of direct tax credit or benefit; these types of provisions are included in the President's GO Zone proposals. Wage subsidies would also be unused by firms without profitability (although it might be possible to offset those against payroll taxes if allowed as a credit).

We have heard testimony in support of a zero rate on capital gains in the Gulf region. Some have raised concerns that not taxing capital gains will provide easy and simple ways to devise opportunities for tax arbitrage and sheltering. Are you aware of these concerns and do you have proposals that would ensure against such tax evasion? Of all the options for business investment incentives, how does the zero rate on capital gains compare?

The assessment of the zero capital gains rate depends on what assets are allowed the exclusion. Are residents of the zone to be allowed a zero capital gains tax rate regardless of where investments are made? Are investments in the zone to be allowed a zero capital gains tax rate, regardless of who owns them? In the first case, there may be little benefit to investment in the region, since capital gains on stocks, which normally account for the majority of gains, would reflect gains on investments in the U.S. as a whole (and in foreign countries as well). (Mr. Kemp's proposal does exempt gains of individuals either working or living in the zone.)

There are much more serious opportunities for tax sheltering under a proposal that allows individuals living or working in the zone to exclude gains. Individuals could shift their residence or, in some cases, work location, to the zone temporarily to realize a large gain.

The rest of this discussion assumes that the capital gains relief applies to assets in the zone, rather than to individuals who reside or work in the zone.

There are a variety of ways that a zero rate on capital gains could be used for tax sheltering and arbitrage in the case of application to assets in the zone. A more fundamental problem, however, with allowing a zero rate on capital gains is that a general capital gains exclusion will also apply to gains that accrue to existing investment in the area, especially as the disaster area itself includes some existing property not destroyed or even seriously damaged. Moreover, gains from land would also be included in the tax benefits. Because of this effect, a capital gains exclusion is not nearly as efficient, in terms of inducing investment per dollar of revenue loss, as subsidies that are attached only to new investment. In addition, even if the benefit were restricted to new investments in the zone, the gain associated with land would be part of the gain and would be difficult to separate from other investments.

In addition to the potential for windfall benefits on existing property and land, there are ways in which a capital gains exemption can be used for tax sheltering. The magnitude of this sheltering would depend on the specific type of exclusion enacted. For example, there are recapture rules that tax gain in the amount of prior depreciation deductions at higher rates, which reduces the scope for tax sheltering. Without such a provision, depreciation may be deducted at high rates and taxed when recovered at low rates, so that income could be earned on property with no actual productive use. At the same time, requiring depreciation to be recaptured and taxed at ordinary rates would limit the benefit of the zero rate for depreciable assets. (Currently, gain to the extent of previous depreciation is taxed at ordinary rates, although the amount arising from straight line depreciation for structures is capped at 25%.) Of physical assets, the asset that would benefit the most in these circumstances is probably land, for which no investment inducement is needed; that would be entirely a windfall.

There are probably many potential shelter opportunities that would eventually be developed by tax lawyers and these experts are the best source of information on potential shelters. This discussion can identify only the more obvious ones. One example of a shelter mechanism is a like-kind exchange of property, where the property with substantial accrued gain outside the zone is swapped for property with limited gains in the zero gains area. Absent some restrictions, this gain accrued outside the zone would then be tax exempt. Another mechanism, although one with limited scope, is for an individual to perform much of the rehabilitation of a property and, with a capital gains exclusion, income which is essentially labor income, will never be taxed. And, of course, a standard arbitrage approach

is for a high tax rate investor to borrow to purchase or construct an asset that will largely produce gain; because interest continues to be deducted, the taxpayer will receive a significant net subsidy from the government. Increasingly, such interest may be largely not taxed to borrowers, as a large fraction is exempt via pension plans, IRAs, and imputed income from banking services. There are also complex business arrangements, primarily through partnerships which have considerable flexibility, that may present opportunities to shift otherwise taxable, and now exempt, gain to high tax rate participants.

If relief were extended to businesses that operate partly within the zone and partly outside the zone, the taxpayer would have an incentive to allocate as much of the gain as possible to the zone.

It is very difficult to address some of these tax shelters. If benefits are granted on the basis of residency or work location, allowing benefits only for taxpayers with a significant period of residency or work location would limit abuses. Like-kind exchange shelters can be addressed by requiring a longer holding period for property before it is eligible for a zero tax, or retaining the accumulated untaxed gain and taxing it upon sale. Recapture and taxation of depreciation also reduces sheltering operations as does the existing passive loss restrictions.

From Senator Rockefeller

The Low Income Housing Tax Credit is an example of a public private partnership, and the LIHTC Program has been recognized as the most successful affordable housing program. Using federal tax credits, the program brings private capital into an area that would not otherwise be marketable.

What role should public private partnerships such as the Low Income Housing Tax Credit play in the rebuilding effort?

The low income housing credit has critics and supporters. The critics suggest that low income housing subsidies might be more efficiently provided through grants and loan subsidies due to overhead costs and excess returns to investors. Many economists also suggest that housing assistance should be provided directly to the tenants, whose increased ability to pay rents will lead to an increased supply of housing. On the other hand, a significant amount of lower income housing has been provided through the credit; over one fifth of all new multifamily construction from 1995-2001 is credit property.³ And the credit operates through the private sector which may be more efficient in constructing housing than the government is. The magnitude of the role of the low income housing tax credit depends on how those benefits and costs are traded off, a difficult question to answer.

To increase the role of the credit, an expansion of the caps for the affected states could be allowed. The credit rate could also be increased. The projects would also become more attractive if the income limits for tenants were raised, but this change would also likely have the effect of displacing potential lower income tenants.

³ See Leonard E. Burman and Alastair McFarlane, "Low-Income Housing Credit, in *The Encyclopedia of Taxation and Tax Policy*, ed. Joseph J. Cordes, Robert W. Ebel, and Jane G. Gravelle (Washington, D.C.: The Urban Institute, forthcoming October 2005).

From Senator Kerry:

You heard Mr. Kemp testify about his super-charged enterprise zone. Do you think the benefits will outweigh the costs? Do you think a more direct approach would be to offer grants and loan subsidies?

The broad tax relief proposed by Mr. Kemp could create tax administration problems. Allowing lower taxes on wage income and exempting capital income for those who live or work in the zone would induce wealthy taxpayers to establish principal residences or temporary work environments in the zone. This problem is particularly serious with capital gains relief, since the realization of gain can be controlled by the taxpayer.

Moreover, it would provide benefits to taxpayers based on their place of residence or work even if in some cases those taxpayers have very high incomes and were not harmed by the disaster. There could also be serious horizontal inequities. A taxpayer living on one side of a county line would continue to pay lower taxes than a neighbor on the other side of the county line. Geographically targeted tax benefits inevitably confront problems of abuse and inequity. They could also induce residents or jobs to move across the geographic boundaries.

Companies that operate in multiple jurisdictions, if included in the exemption, would also have an incentive to shift profits to the favored jurisdiction. Excluding these companies would address that problem but would greatly limit the scope of investment incentives.

In addition, imposing a simple low tax rate that can be filed on a post card is actually very difficult to devise, as one can see by examining a 1040 tax return and considering the reason for each line on the form. The tax return is used to claim refundable tax credits such as the earned income tax credit, to target the appropriate social security contributions, and to deal with a variety of complicated circumstances such as taxation of annuities and pensions, itemized deductions and other provisions. Simplifying the tax is very difficult. For example, deducting uninsured casualty losses, a provision that most would agree is helpful to individuals with property experiencing a disaster loss, could not be accommodated on a postcard.

The business provisions proposed would create significant negative tax rates, especially for debt financed investments, negative tax rates that would benefit existing capital as well as new investments. If continued indefinitely, such provisions would reallocate capital from other parts of the country and cause economic inefficiency.

Broad tax relief of this nature is likely to be less efficient at inducing new investment and rebuilding than targeted grants, loan subsidies, and some types of tax incentives, because broad relief produces windfall gains for other types of capital.

In a recent report, you raised concerns about the stimulus benefit of extending the tax cuts. Can you share your views on this?

Tax cuts only stimulate the economy if they lead to spending. There are two reasons that extending the tax cuts would be unlikely to increase spending much. The first is that extending the tax cuts will not provide an actual increase in disposable income until the tax cuts expire, which for most of them is not until 2011. There are economic theories that indicate that the expectation of a future tax cut can lead to additional spending now, but the

empirical evidence does not seem to support this view strongly; current income seems to exert a stronger influence. And even if a future tax cut did increase income, it would have no effect to the extent that it is already anticipated. Secondly, evidence also suggests that lower income individuals are more likely to spend, and relatively little of the benefit of the 2001-2003 tax cuts accrued to lower income individuals. If one were choosing among tax cuts for short run stimulative purposes, this approach would likely rank very low, after current tax cuts and tax cuts directed at lower income individuals.

Do you think strengthening the EITC would provide some stimulus benefits?

The EITC has the advantage of directing benefits to lower income individuals which might make it more likely to be translated into spending. One problem with the EITC is that most individuals receive it as a lump sum at the time they file their tax returns. Thus there would be some delay in receiving it and perhaps a delay in spending it. This delay would be less important for a tax cut enacted late in the year, as tax returns can be filed early in the next year and there is a lag at that point with any type of tax cut because other tax cuts cannot be provided through withholding either. Thus, a retroactive EITC increase for 2005, given that we are near the end of October, would translate relatively quickly into disposable income.

If the EITC credit amount was increased for families with 3 or more children would this help more families have income above the poverty level?

Larger families require larger amounts of income to exceed the poverty line. Thus, expanding the EITC for families with three or more children would have a greater effect per dollar of revenue loss than a more general EITC change in reducing the number of families that fall under the poverty line. A recent CRS report illustrates the effects for 2003 for a family with two workers earnings about \$20,000 (which is approximately full-time minimum wage work for both).⁴ In that case, a family with two children has income after the current EITC at about 120% of the poverty level, a family with three children is approximately at the poverty level, and a family with four children has only about 90% of the poverty level.

⁴ See CRS Report RS21477, *The Earned Income Tax Credit (EITC): Policy and Legislative Issues*, by Christine Scott, for a discussion of the effects on different family sizes of the EITC.

Testimony of James R. Kelly
Chief Executive Officer
Catholic Charities
of the Archdiocese of New Orleans

**The Future of the Gulf Coast: Using Tax Policy to Help Rebuild
Businesses & Community and Support Families After the Disaster**

Before the United States Senate Committee on Finance

October 6, 2005

Thank you, Mr. Chairman and members of the Committee, for the opportunity to testify before you today on matters of concern that impact and address the needs of survivors along the Gulf Coast. We are grateful to the Committee for convening this hearing to focus on the Gulf Coast and the importance of a comprehensive strategy that strengthens the nation's "safety net" through bi-partisan action.

In 1727, Ursuline nuns stepped onto Louisiana soil in the area known as the Ninth Ward of New Orleans to care for the citizens of Louisiana. In September 2005, some areas of the Ninth Ward resembled its earlier incarnation – devoid of housing, vegetation and population – thanks to Hurricane Katrina. Although nearly three centuries have passed, the legacy of the Ursuline nuns continues through "Catholic Charities" and its mission to care for those in need. Incorporated in 1938, Catholic Charities Archdiocese of New Orleans, offers life-giving programs, advocates for the voiceless and empowers the most vulnerable to foster a more just society.

Prior to Hurricane Katrina many services were still located in the Ninth Ward. Catholic Charities operated more than 30 programs addressing such issues as hunger, poverty, unemployment, domestic violence, education and the needs of the mentally ill, low-income seniors and at-risk children. Today, Catholic Charities serves those whose lives have been changed forever by Hurricane Katrina, in addition to many of those we served before.

Catholic Charities is an effective and efficient organization serving over 150,000 people annually with an administrative rate of just 7 percent. Over 92 cents of every donated dollar goes to direct services.

Today, as we help rebuild the New Orleans metropolitan area, Catholic Charities is committed to continuing its tradition of excellence in service to the community. As we respond, recover and rebuild, we are Ministry in Motion for all who need our assistance. Because at Catholic Charities, people are the heart of the matter.

Post Katrina

A few weeks ago our offices in New Orleans were under ten feet of water, and are not completely operable today. However, we were called upon to serve survivors in the initial days of the disaster. And just as the many families throughout Louisiana and the South are hosting family, friends, and even strangers who otherwise would have no roof over their heads, the Diocese of Baton Rouge is serving as our host family.

Because of the hospitality offered by the Diocese of Baton Rouge, our staff is working around the clock to serve those in need. We are able to provide hundreds of thousands of pounds of food to the hungry and poor. In addition, the New Orleans agency is providing care to New Orleans firemen and policemen. The agency has taken over operation of a medical and respite care center in Baton Rouge where first responders who are working on the ground in New Orleans can get crisis and trauma counseling, medical attention, and other support services before returning to duty.

The people that we served prior to Hurricane Katrina are now in shelters, cars, with family members or perhaps lost their lives before we could get help to them. The businesses that employed folks are gone and unless creative strategies to give them new life are implemented soon, many of them may never be rebuilt.

Despite the recent announcement from FEMA implementing a housing assistance program for those who lost their homes because of the disaster, 47,000 people are still without temporary housing and are being housed in temporary emergency shelters. You need to know that major policy changes should be made so that these families can get out of shelters and into decent affordable housing in order to begin to rebuild their lives.

As both a victim myself and a service provider, I make the following suggestions as you continue to respond to the needs of our region:

My first and foremost suggestion is to do no harm. The committee should ensure that no cuts are made to basic safety-net programs like Medicaid at this time of devastation in our country. Even before the hurricane in my state of Louisiana, the lack of health insurance was one of the major problems facing our community. Medicaid and the SCHIP program provide basic coverage to the poorest pregnant women, children, seniors and severely disabled persons.

The proposals to force the poorest and most vulnerable people in our society to pay more for their healthcare are difficult to justify in this richest country in the world. It is important to ensure that the needs of the survivors are not met by cutting benefits to others currently in need outside of the affected area.

I applaud the efforts of this committee for its development of the bipartisan bill, S.1716, the "Emergency Health Care Relief Act of 2005," which would provide for streamlined access to temporary Medicaid benefits for Katrina survivors both inside and outside the declared disaster area.

Your inclusion of poor childless adults in this temporary Medicaid program is an act of great wisdom that we urge you to continue to advocate for. Many of the survivors and evacuees we are seeing in Baton Rouge are childless adults who lost what limited access they had to health care when the hurricane damaged or destroyed clinics and outpatient departments in their communities. Now as they live in shelters or the remains of their homes, their previous chronic health illnesses have become acute, and they are suffering from new diseases.

As you know, the economies of Louisiana, Mississippi and Alabama will need many years to begin to recover. While the Grassley/Baucus bill would be a wonderful down payment, I urge you to begin to consider how the federal government can help to rebuild the health care financing and delivery systems in the Gulf region, which were woefully deficient to begin with and are now totally beyond their capacity to serve the needs of our people.

I urge this committee to develop ways to provide temporary income to Katrina survivors who have not yet and will not find work immediately who have virtually no income or liquid assets. There are at least three programs under the jurisdiction of this committee that could be adapted for this purpose: the TANF program, unemployment insurance, and the Earned Income Tax Credit (EITC).

I salute Senators Grassley and Baucus and other supporters for the provisions in S. 1716 which would provide 14 months of TANF assistance to eligible Katrina survivors and 13 weeks of additional unemployment insurance benefits.

TANF and unemployment benefits in the hurricane states are among the lowest in the nation, but they are essential to provide some basic sustenance and dignity to people who have lost everything and have few prospects in the coming months. But TANF and unemployment benefits can help only a fraction of the dispossessed people who have been evacuated or left behind to try to survive in the flooded shambles of their homes.

Many survived before the hurricanes with very modest incomes with 84 percent of the jobs in the region originating from the service industry. Many that we see now cannot work for the same employers again—at least not for years. The jobs in reconstruction should go to survivors who lived in the region.

Their families, neighbors, and churches have also been wiped out. Some way must be found to provide some basic income support for these people until communities are rebuilt and jobs become available. We cannot maintain people in shelters much longer, and without income, they cannot survive. The federal government should make available resources to help the affected states to cope with this situation. The safety net had huge holes that many of the survivors had already fallen through pre-Katrina. To only repair and strengthen the net for survivors does not address the fundamental flaws nor does it provide long term solutions for the future. First, the holes cannot be made bigger not for the survivors nor for other people living in poverty across this country.

Even before the hurricane we had incredible, intractable poverty in our region. It is important for Congress to begin to develop a pro-active, anti-poverty policy with many tools.

Prior to Katrina, Louisiana was among the poorest states in the nation, and the city of New Orleans tied for the sixth poorest large city in the United States. According to a recent report from the Center on Budget and Policy Priorities that looked at recent census data, the city of New Orleans itself had a very high poverty rate – 28 percent of the population lived in poverty. Many of the poor in New Orleans, 54 percent, did not have a car, truck or van. Sixty-five percent of poor elderly household did not have a private means of transportation, thereby making it more difficult for them to escape the impending storm. In addition, affordable housing was scarce for New Orleans residents – almost non-existent. Many lived in extremely poor housing conditions in areas that have now been completely wiped out.

Despite many approaches to create enterprise zones and increase employment through tax credits for businesses it is clear that the state of Louisiana and the Gulf Coast region will need more direct federal assistance to prosper in the future.

I have been greatly troubled by voices urging Congress to cut even deeper into domestic programs, even programs serving the poor, to pay for reconstruction in the Gulf Coast region. In our Catholic social teaching, we are taught that the burden of financing the government should fall on those best able to pay. It is not the poor, the hungry, the disabled, or sick who should pay for this terrible disaster.

Survivors, the poor and the vulnerable do not care about the philosophy – the red and the blue and the political divide – what they care about is finding a way to live – day to day-week to week. While the stories and pictures of the complete disaster that followed in the wake of Hurricane Katrina paint a very grim picture of the magnitude of human suffering, and a sense of overwhelming loss, survivors continue to have hope. Hope: that they will have food, shelter and dignity; that they can care for and keep their families, that their communities will together be reconstructed, and that their fellow Americans, their brothers and sisters and their government will not forget or abandon them.

Thanks you for this opportunity. We will work with you and others to get this important work done.

Answers to Questions for the Record
Mr. James R. Kelly
Catholic Charities USA

Questions from Senator Santorum

Question: We have seen the amazing role charities have played in the relief effort. How do you see their role in the rebuilding effort?

Answer: Historically, in response to most disasters in our nation, charities agencies have been able to mobilize quickly to provide individual assistance to survivors.

In the wake of Katrina and Rita, Catholic Charities agencies faced challenges which included the loss of entire office facilities, staff and volunteers who themselves were displaced and homeless. In spite of these tremendous barriers, Catholic Charities USA and our network of agencies quickly reestablished our operations along the Gulf Coast. Our dedicated staff, themselves survivors, were on the job taking care of those who so desperately needed our services. Catholic Charities USA and the Catholic Charities network quickly reestablished our operations, and our staff and volunteers, who are also survivors, were there to help others who needed us.

Within three days of Hurricane Katrina, the seven Catholic Charities Agencies of Florida had organized and deployed teams of relief works to the most ravaged areas of Mississippi. Despite the damage to Catholic Charities in the two Mississippi dioceses, the Florida teams were able to set up relief centers in one of the surviving parish halls from which they organized church volunteers to distribute donated food, water, clothing and bleach for weeks before FEMA appeared.

Catholic Charities of Baton Rouge has provided space and support to evacuated staff of Catholic Charities of New Orleans who were quickly able to reopen our food distribution program which is distributing 400,000 pounds of food every day.

Catholic Charities of Albany, New York sent a team of social and health workers to Baton Rouge to assist staff of Catholic Charities Baton Rouge.

And now teams of professional staff and volunteers from our member agencies across the country are rotating in to support our operations on a bi-weekly basis.

In addition, Catholic Charities USA in the early days of the disaster developed a housing response known as "Home Away from Home" which is linking housing resources identified by member agencies across the country with those needing housing identified by agencies in the primarily impacted and secondarily impacted areas.

None of this is meant to disparage the wonderful work of small charitable organizations and churches in organizing and delivering aid to hurricane survivors. However with a

disaster of this magnitude, charities with national networks and connections and trained, experienced staff are needed.

Question: What should we be doing on Capitol Hill to encourage giving?

Answer: The newly introduced S. 1780, the CARE Act, would be a good start. The provisions that would be most helpful are:

1. Restoration of the charitable tax deduction for the two-thirds of U.S. taxpayers who do not itemize deductions on their federal tax returns; and restoration of \$1 billion in funding for the Social Services Block Grant which states use for grants and contracts for faith- and community-based groups to aid poor families, seniors and persons with disabilities.
2. In addition, many experts are convinced that further cuts in the estate tax are likely to reduce incentives for charitable giving by affluent families.
3. Charities typically have to pick up the burden of serving the poor and the sick after government budget cuts in programs like Medicaid, Food Stamps and housing assistance. When groups like Catholic Charities have to seek additional donations to provide emergency food and shelter for families that cannot get the government help they need, our capacity is diminished to help disaster victims and others to rebuild their lives.

Question from Senator Kerry

Question: You mention some troubling statistics in your testimony about poverty in Louisiana and that 28% of the population in New Orleans lives in poverty. Would you agree that one of the best things we can do from a tax policy standpoint is to strengthen the EITC?

Answer: Yes. Experts agree that the expansion of the EITC in the 1990s was a major factor in reduction in the child poverty rate in those years. The EITC makes a huge difference in Louisiana where such a large percentage of parents support children on wages at or just above the minimum wage.

An increase in the EITC and providing a higher benefit to families with more than two children would be the single best policy initiative to reduce child poverty among the working poor.

A RENAISSANCE STRATEGY FOR
THE GULF REGION
TESTIMONY BEFORE THE U.S. SENATE
COMMITTEE ON FINANCE
OCTOBER 6, 2005
BY
JACK KEMP

Hurricanes Katrina and Rita produced a national calamity of biblical proportions, or as David Brooks of the New York Times put it, of "Hobbesian" proportions. Picking up the pieces provides Congress an unprecedented opportunity to implement proven policies that have been on the drawing boards since the late 1970s, indeed they have their roots back to Abraham Lincoln and FDR.

This huge problem requires "big ideas," such as those identified with Presidents Lincoln and Roosevelt, and it is clear from his words and actions that President George W. Bush understands this and understands the magnitude of this tragedy and the scale of the opportunity.

Thinking about the agenda of an ownership and shareholder society where access to education, access to capital and access to homeownership is available to all, one is reminded of Lincoln's Homesteading Act of 1862 and FDR's FHA and GI Bill. They fit into a strategy of how to combat poverty, encourage enterprise, expand ownership opportunities and devise public-private partnership and market solutions to vexing problems of poverty and despair.

Thus, the need to rebuild the Gulf Coast provides Congress and state legislatures with the opportunity to implement big ideas that not only can rebuild in a rational and efficient manner but also could provide a model for beginning to transform the rest of the United States. **We have a golden opportunity to "green line" the Delta and Gulf Coast with government policies that facilitate and empower the private sector and private citizens, and in the process prove these policies also will work in the rest of the country.**

As we think about the government's role in assisting people to get back on their feet after Katrina and Rita, we should be thinking about how to expand private property rights and business ownership, particularly in the minority community, in order to create jobs and greater opportunity for those most severely impacted by these hurricanes. We should create rational and reasonable incentives to build a new Gulf Coast and Delta Region unencumbered by bureaucratic rules and strictures. We have an enormous opportunity to replace outmoded government programs and bureaucracies with public-private partnerships and new private institutions that are built upon the foundation of individual ownership, private property rights, personal responsibility and social justice that a stakeholder society brings.

President Bush is on the right course in calling for an opportunity zone for the entire Gulf region. His proposal was greeted recently by a Washington Post editorial labeling it a "Go Go Zone." Apparently no good deed goes unpunished.

I applaud the President's approach and agree that tax incentives should be available across the board to all legitimate businesses willing to invest the capital to rebuild.

The Post opined, inexplicably, that tax incentives offer breaks for investment but not for job creation. Did the Post editorialist ever take a look at the renaissance going on in Harlem, thanks to President Clinton's Empowerment Zone (a modified Enterprise Zone)? Have they looked at the low-tax industrial zones (maquiladoras) along the Tijuana-San Diego border? Have they noticed how low-tax, pro-business cities like Shanghai, Shenzhen, Pudong and Hong Kong are doing in China? Or the city of Dublin, Ireland, or the city of Dubai, UAE? There are many other examples and empirical evidence that show that while the president's opportunity zones need tweaking, they will work using similar incentives.

Congress recently passed legislation extending limited tax relief to the victims of hurricanes Katrina and Rita. Congress should enact follow-on legislation adding more "juice" to the president's opportunity zone idea of "green-lining" the entire Gulf Coast region as an enterprise zone with powerful tax and regulatory incentives to restore robust economic activity and jobs with homeownership and housing as key components.

In fact, we already have a bipartisan consensus on enterprise zones that formed back in 1995 around an enhanced enterprise zones bill that was supported by Spencer Abraham, J.C. Watts, Peter King, Jim Talent, Joe Lieberman, Carol Moseley Braun, John Breaux, Eleanor Holmes-Norton, among others, which was based on the old Kemp-Rangel Enterprise Zone bill of the 1980s. You also have a contemporary example from which to work in the Brownback-Fortuno-Ryan National Enterprise Zone Act of 2005.

The fundamental idea behind these bills is that private enterprise, not government, is the source of economic and social development. The failure to recognize this fact was, in my opinion, a flaw in President Clinton's Empowerment Zones. While a sincere effort, Empowerment Zones fell far short of what was needed to spawn a rebirth of economic vitality and entrepreneurship in our distressed areas.

Empowerment Zones had only limited tax incentives, including a small increase in expensing for plant and equipment, and they were driven by a kind of Great-Society mentality with some \$280 million in social services block grants. Social Services block grants are based on the failed notion that government can create jobs and prosperity. As I have said repeatedly, we must get away from this "big-brother" mentality. Government does not and cannot create wealth. The best it can do is unleash citizens' drive and initiative to succeed in the market economy. We need to free up capital and the entrepreneurial spirit, and that is what a super-charged enterprise zone in the Gulf Coast region can do.

During the next decade, Congress should allow individuals and companies in the zone or anyone outside the zone investing in it to pay federal taxes under a simplified, pro-growth tax system.

Individuals living or working in the zone should be allowed to:

- pay a simple, low, single-rate tax that can be filed on a postcard;
- with no tax on capital gains;
- with no tax on income saved and invested; and
- no tax on low-income workers up to 180 percent of the poverty level.

Companies and home builders doing business in the zone should be allowed to:

- pay federal taxes under a streamlined federal tax system;
- allow full, immediate write-off of all investment expenditures and inventory purchases;
- a full deduction for all dividends paid; and
- no tax on capital gains.

I also would support another idea contained in the 1995 version of national enterprise zones act which is to allow all individuals and companies to deduct the purchase of qualified “enterprise-zone stock” (and I would suggest interest on bonds as well) from their income up to some generous limit, say \$250,000 a year and a million dollars in their lifetime.

In addition to tax provisions such as these, Congress should enact broad regulatory relief to companies doing business in the hurricane enterprise zone. The President already has suspended some federal regulations for purposes of rebuilding but more is required than a piecemeal approach. What is required is temporarily holding federal environmental, labor and other economic regulations in abeyance, leaving it to state and local governments to determine which regulations are so essential to public health and safety that they should be enforced during the life of the zone.

Where education and homebuilding are concerned, wider use of education and housing vouchers are also tools that can be used. Congress should authorize education vouchers for the children living in or displaced from the hurricane region, which should be redeemable at any public or private school or go toward the education-related expenses of home-schooled children.

Congress also should take immediate action to preserve the Historically Black Colleges and Universities in the region, which include Dillard University, Xavier University of Louisiana and Southern New Orleans University. It is estimated that these schools have lost 20 percent of their student bodies. Congress should follow the suggestion of Howard University’s President, Pat Swygert and make an emergency appropriation to make up the lost tuition and fees.

Finally, it is absolutely essential that Congress use this opportunity to create the president’s urban homesteading program to give displaced and otherwise low-income

people an opportunity to own homes. Thanks to the "Today" show on NBC, Warner Records and my friend Tim Blixseth, \$25 million has been raised for Habitat for Humanity in just two weeks. "Operation Home Delivery" will send homes to the region in several weeks down the Mississippi River to the Gulf Region.

One idea would be for Federal agencies and GSEs, such as the Federal Home Loan Bank, Fannie Mae and Freddie Mac, along with FHA, to pool resources to buy out low-income property owners, and then these newly acquired federal properties would be available for low-income people to "homestead." The money provided by the buy-out, along with perhaps, a Section 8 voucher, could be used to relocate or re-invest in property (when it makes sense to rebuild on the old site) or as a down payment on a new home. Obviously there would have to be guidelines and income limits but the homesteading idea would be an asset-based welfare and anti-poverty idea where the poor could then create the "live capital" outlined so well in Hernando de Soto's "Mystery of Capital."

Another matter where housing is concerned: Habitat for Humanity is one of the most cost effective ways to provide housing/homeownership for the most needy in our society. Because the secondary mortgage market (Fannie Mae and Freddie Mac) is prohibited from purchasing non-interest bearing mortgages, the GSEs cannot provide liquidity to Habitat for Humanity as it does for the rest of the housing market. I urge Congress to consider amending the pending GSE legislation or attaching this proposal to emergency Katrina and Rita relief legislation.

Other important ideas that should be considered are President Bush's "new markets" tax credit program, which could be targeted for homeownership, shelter, real estate and business development. New Market Tax Credits is an existing Treasury program that does just what the President is calling for and, with some minor changes, this program can be a leading catalyst for private sector reinvestment in the affected areas of the Gulf. If Congress would extend the definition of distressed areas to the parishes and counties affected by Hurricanes Katrina and Rita, raise the incentive percentage for small business equity investments and dedicate a pool of money available for the affected areas, then this program would go a long way toward increasing the private sector role in the rebuilding effort and decreasing dependency on the government. In addition, the Brownfields legislation proposed by Congressman Michael Turner of Ohio could provide a useful approach that could be tailored and adapted to the Gulf Coast to deal with environmental liability exposure, which will emerge as the rebuilding proceeds.

Many of my Republican friends are wringing their hands about the cost of undertaking these efforts. I agree that much of the cost could be paid for by reducing other nonessential discretionary federal spending - starting with repeal of the 6,000-plus pork-barrel projects contained in the recently enacted transportation bill - which has gotten completely out of control. I endorse the idea of across-the-board spending cuts on nonsecurity and nonentitlement accounts being proposed by congressional conservatives.

The Republican Study Committee should be commended for coming up with "Operation Offset," which identifies some \$50 billion in corporate pork and \$300 billion in overall discretionary spending that should be delayed, if not eliminated outright.

Is \$100 billion to \$150 billion a lot of money? Of course it is. But as my colleague at the Free Enterprise Fund, Larry Kudlow, points out, it is an amount that easily can be shouldered by our economy which will be \$13 trillion in 2006 and is projected to grow to \$20 trillion during the coming decade.

As Kudlow points out, "Yes, the budget deficit will rise for a year or two, from roughly 2.5 percent of GDP to perhaps 4 percent. Big deal. The very bond markets that actually do the financing have shrugged the spending off, with Treasury issues continuing to trade around 4.25 percent. There was no 'spiking up' of long-run interest rates that might suggest a financial crisis. The stock markets, meanwhile, just registered their best third quarter in seven years."

Kudlow also points out that family net wealth — which includes the value of our nation's businesses, bonds, stocks, and real estate — just hit an all-time high of \$50 trillion. A great figure but the pie needs to be "democratized," not by redistributing the pieces of the pie among the poor but by giving the poor the access to capital, which will allow them to get a larger share of an even faster growing pie.

The fact is, Mr. Chairman, enterprise zones for the Gulf Coast will be relatively inexpensive and very cost effective. Every new job means a new taxpayer and a broader tax base. The 1995 nation-wide enterprise zone proposal was estimated, on the high side, to cost \$2 to \$3 billion over five years. The Brownback-Fortuno-Ryan National Enterprise Zones are expected to "cost" \$26 billion over ten years. Clearly the cost of a Gulf Region enterprise zone would constitute a mere drop in the bucket compared to the total cost of rebuilding.

Moreover, we know the kinds of tax reforms contained in enterprise zones will work. For example, between 1977 and 1982, when the capital gains tax was reduced from 49 percent to 20 percent, the number of small company start-ups exploded by nearly 50 percent. More recently, as a result of the accelerated write-off provision (so-called "expensing") enacted in 2003, firms' retained earnings reached an estimated four percent of potential GDP during 2004, a share not matched since the 1960s.

Even under the fairly tepid Clinton Empowerment Zones, 35 states and the District of Columbia have produced hundreds of thousands of new jobs and scores of billions of dollars of new capital investment. And, the concept has long been endorsed by the National Governors' Association, the Conference of Black Mayors, the Council of Black State legislators and the U.S. Conference of Mayors. There is a tremendous bi-partisan coalition just waiting to be built around this concept.

Finally, in order to rise above some of the inter-agency turf competition that invariably will arise, I have urged the White House to think about appointing proven leaders of

national stature like Ambassador Andrew Young, Urban League President Marc Morial, Mayor Anthony Williams and former HUD Secretary Henry Cisneros to help consolidate a bipartisan consensus. I too would be willing to contribute in anyway that might be useful and productive. As Chair of Speaker Hastert's "Saving America's Cities" Working Group, I recently have re-intensified the thinking and the work I have been doing on these issues for nearly thirty years.

In the aftermath of this national tragedy, we have an unprecedented opportunity to combat poverty and democratize capitalism so as to help people put their lives and family back together. Combating poverty with education, home ownership, jobs and democratic capitalism is the vision for a true renaissance for the Gulf Coast and indeed the entire nation.

Thank you, Mr. Chairman.

**STATEMENT FOR THE RECORD
HABITAT FOR HUMANITY INTERNATIONAL**

Submitted by Jonathan T.M. Reckford, CEO

**United States Senate
Finance Committee**

October 6, 2005

Dear Chairman Grassley, Ranking Member Baucus, and Members of the Committee:

Thank you for the opportunity to provide a Statement for the Record on behalf of Habitat for Humanity International. Habitat for Humanity, established in 1976, seeks to eliminate poverty housing and homelessness from the world, and to make decent shelter a matter of conscience and action. Since our founding, we have built more than 200,000 houses around the world providing more than one million people with a place to call home.

Yet the lack of decent, affordable housing remains a serious problem, both in the United States and around the world. For too long, this problem has not been given the attention it deserves. According to UN-Habitat, in 2001, 924 million people lived in urban slums around the world. They estimate the number of people without housing or in primitive housing could be as high as 1.5 billion by 2020. In the United States, one of the richest countries in the world, more than fourteen million families have critical housing needs, meaning they pay more than half of their income for housing or live in severely substandard conditions.

Decent, affordable housing options are important for strong, healthy communities. Affordable housing allows people to live where they work and helps to create a diverse and vibrant community. Having a stable, decent living environment has been shown to increase children's school attendance, improve health, and increase job retention among adults. In addition, affordable homeownership opportunities give families the chance to create invest their hard-earned money and save for the future.

Even before the storms, much of the affected area already suffered from a lack of affordable housing. Now, after the devastating hurricanes and floods, the need for affordable housing in the Gulf Coast and New Orleans is tremendous. The National Low Income Housing Coalition estimates that more than 300,000 housing units were lost to the hurricane and subsequent floods. The Enterprise Foundation's estimates are even higher - 455,000 homes in these areas must be rebuilt entirely and another 475,000 will need some form of major or minor repairs. Of these homes, the Enterprise Foundation believes more than 280,000 were occupied by families and individuals earning \$20,000 or less, and another 197,000 homes were occupied by families and individuals earning

between \$20,000 and \$50,000. The devastation caused by the hurricanes has only compounded an existing burden on these families who struggle each day just to keep a roof over their heads.

The task of rebuilding the Gulf Coast and New Orleans will be monumental. Habitat for Humanity offers a positive and successful option, as our staff and volunteers work alongside homeowner families to build new homes throughout the affected region. As always, we will offer low-cost mortgages at no-profit, and ask people to contribute to the building of their own homes by contributing "sweat equity." We are committed to rebuilding the nearly 100 Habitat homes that were destroyed in the storms, but we will not stop there. The number of homes we will build will be limited only by the amount of money we raise and the capacity of our staff and volunteers to build safe, decent affordable shelters.

Habitat for Humanity has named our rebuilding effort "Operation Home Delivery." In the first phase of this program, we are building component parts of homes around the country with our local Habitat affiliates, as a way to engage our vast volunteer network and to begin work immediately. To date, we have had over 20,000 volunteers sign up on our website. Last week, the first 65 house frames were constructed in New York, California, and Mississippi. And on Monday, walls for the first house were raised in Slidell, Louisiana. The rebuilding has already begun, a more detailed explanation of our Operation Home Delivery program is included with this statement.

Habitat for Humanity offers just one part of a larger rebuilding effort. A truly successful rebuilding effort will require government, corporations and nonprofit organizations working together. We hope to join with others in the housing industry in a collaborative effort to rebuild the Gulf Coast. While we will continue to provide homeownership opportunities for low income families, we know it is important for us to work together to develop diverse communities with a mix of housing options, including rental housing opportunities.

There are many ways the government can help. A home ownership tax credit for affordable housing development would enable the development of affordable for-sale housing for low income people, a necessary component in the rebuilding of the hurricane-affected areas. New home construction costs can often exceed the amount that low-income families in many areas can afford to pay. Without resources to fill the gap between development cost and market value, developers may be reluctant to focus on affordable new homes. A home ownership tax credit would provide a resource to fill that gap.

A community contribution tax credit program, like the one that currently exists in Florida, could also help. This tax credit provides an incentive to encourage corporations to make donations toward community development and low-income housing projects. The program allows any corporation paying corporate income tax or insurance premium tax to receive a tax credit equal to 50 percent of their donation to an approved community

development or historic preservation project. Habitat for Humanity, and programs like ours, have benefited greatly from this program.

Habitat for Humanity looks forward to working alongside volunteers and homeowner families in the Gulf Coast to build new homes. We hope that you will support us, and other organizations like ours, while we work to ensure decent, affordable housing is available throughout this region.

Thank you for this opportunity to submit a Statement for the Record. We look forward to working with Congress, as well as others in the housing industry, to ensure that the people of the Gulf Coast are able to return home.

Habitat for Humanity's Operation Home Delivery

On-site construction on the first of what eventually will be hundreds, if not thousands, of Operation Home Delivery houses began on Oct. 3 - five weeks to the day after Katrina devastated the homes and lives of so many families in Alabama, Mississippi and Louisiana.

The first three Operation Home Delivery houses will be built in Covington, La., with St. Tammany West Habitat for Humanity.

By year's end, construction of Operation Home Delivery houses with Katrina-affected families will be well under way in each of the affected states, providing simple, decent, affordable homes to those who would not qualify for conventional lending programs but are willing to help build their own home and then pay for it through a no-profit, no-interest loan. Their house payments will be recycled to help build even more Habitat homes.

In this first phase of encouragement and support, Habitat affiliates around the country will be asked to produce about 250 of the containerized homes for shipment to at least six affiliates in the affected region.

The houses will be built as properties can be acquired and made ready and partner families selected.

Most of the initial homes will go to New Orleans and Covington, La., for rapid recovery efforts and then to Mississippi and Alabama as the infrastructure there comes online.

Our staff is strategizing with experts to build homes that are suited in style and functionality for each area and we are researching the best possible construction methodologies. This will ensure that our work is appropriate and sustainable for community and neighborhood development.

Based on the effectiveness of the initial launch program, we will identify target locations in the United States to produce additional Operation Home Delivery solutions so that we can scale up to meet the need.

To make this major building program possible, Habitat for Humanity International has acquired warehouse space, and is seeking more where materials can be stored and assembled to facilitate the on-site building process.

With that initial warehouse space now secured, we have tremendous need for both equipment and building supplies as we move forward with this undertaking of unprecedented scope in the United States. Donations from corporate partners are being solicited. House-building materials of all types will be needed, as will be heavy equipment and hand tools.

While the need for housing is immense in the hurricane-affected region, nearly every

community across the country needs decent, affordable housing. For every dollar donated to Katrina recovery efforts, nothing would please us more than to see another dollar go to Habitat affiliate efforts in the donor's home community.

Habitat's Disaster Response Office has completed its first-level assessment of Katrina's impact on Habitat for Humanity affiliates in the Gulf Coast region and on Habitat homes. The first-level assessment indicated that 17 affiliates across Alabama, Mississippi and Louisiana were directly impacted by Hurricane Katrina. Of the 925 Habitat homes built by these affiliates, 246 sustained damage at various levels.

Long after relief efforts have ended and the spotlight has faded, Habitat for Humanity will remain hard at work in affected communities, building long-term housing solutions.

Operation Home Delivery will follow Habitat's guiding principles of providing a hand up, not a hand out.

Habitat will not and cannot be the answer to all low-income housing needs created by Hurricane Katrina, but we do expect to assist thousands of families and just as importantly, to serve as a catalyst in bringing others to the rebuilding process that will be required. For example, rental units, group homes and short-term housing units will be needed, but do not fall within Habitat's mission. We will work with others to ensure that such needs are met.

Habitat will use experiences learned during our work in previous disaster responses, during Hurricanes Frances, Charley and Ivan last year, and Dennis earlier this year, as well as lessons learned following last year's tsunami in the Indian Ocean basin and earthquakes in Iran and Afghanistan. All of these have helped us prepare better to respond in a situation such as this.

“The Future of the Gulf Coast: Using Tax Policy to Help Rebuild Businesses and Communities and Support Families After Disasters.”

**Tate Reeves
State Treasurer of Mississippi
October 6, 2005**

Thank you for giving me the opportunity to speak to you today regarding Federal tax policies that may be utilized to expedite the process of getting citizens of south Mississippi back to work, their kids back to school, and the economic engine that drove my state’s economy back in gear.

The damage caused by Katrina’s path is unimaginable – not just in our coastal counties, but throughout our State. Our infrastructure has been deeply damaged, but our fortitude has only strengthened.

I spent this past Monday meeting with local officials in Harrison and Jackson counties – the latter of which happens to be Senator Lott’s home county. These places are being led by true leaders... some of the finest men and women America has to offer. They are not complaining, they are not deserting their constituents, they are simply working day and night to help rebuild their communities in what otherwise would be part time jobs. They are ordinary people doing extraordinary things!

I do not come before you today asking for a handout... Mississippi simply needs a helping hand. While I recognize that this hearing is regarding taxation policy, I would be remiss if I didn’t ask you to consider the great challenge individuals face with respect to housing. I would be remiss if I didn’t urge you to consider the consequences of those in the uninsured and underinsured categories. These people are our friends, our neighbors, our family... they are Americans in need of help from Congress.

I must remind you of the great need for state and local governments to receive direct fiscal aid to help them get through the weeks and months ahead. The State of Mississippi has created a loan program through the Mississippi Development Bank that will guarantee our local governments access to capital. However, in lieu of direct fiscal relief from the federal government, the ability

to repay those loans will be a major issue for many of our political subdivisions which have lost a large percentage of their tax base.

I believe that an allowance for a second advance refunding would be crucial for our state and local governments in the intermediate term. The cost to the U.S. Treasury of such an act would be miniscule in comparison to the benefits derived for our local communities. Generally, one would refinance their debt to achieve net present value savings. In this instance, our State and local governments should be allowed to restructure their debt, possibly delaying several years of principle and interest, until a reasonable time when their tax bases could be reestablished. In addition, I would encourage you to consider relaxing certain limitations on tax-exempt financing for working capital needs.

While I appreciate the financial commitment that has been, or will be, made by the President, the Congress, FEMA, and other federal agencies, I believe the private sector is the key to Mississippi's renaissance. For our gulf coast region to rebuild as the beautiful place it once was, we must work together to create an environment that encourages the private sector to invest in our communities. One way to accomplish this goal is through the allowance of \$15 billion in tax-exempt private activity bonds that should be classified as "bank eligible" with no limitations (total exemption from Code Section 265). I would encourage you to expand the types of eligible entities under the Liberty Bond legislation. I would also encourage Congress to consider a special allowance for accelerated depreciation up to 50% in the first year for capital investments made in the affected areas.

To fully understand this request, and the justification behind it, one must take a step back and consider the types of industry that are located on the Mississippi Gulf Coast. Oil refineries, shipbuilding companies, utilities, tourism attractions, and the defense and aerospace industry, just to name a few. While the jobs created by these employers are essential to my state's economy, their finished products are essential to keeping America safe. The one common theme within each of these industries is the extent to which they depend on capital investment. We must create incentives to encourage these capital intensive industries to rebuild.

Many of the items I have outlined today have a precedent in Congress. Some do not. An unprecedented disaster requires an unprecedented response.

My governor, my United State Senators, the local elected officials, and most importantly, the citizens of my state have made me proud to be a Mississippian. We have shown resilience in the face of the worst natural disaster in our nation's history. We will rebuild our State one day at a time – no matter how long it takes.

With your help, we will rebuild in a manner that will make all of you proud of what we accomplish together.

**Questions for the Record From Hon. J. Tate Reeves, CFA
October 6, 2005**

From Senator Santorum:

Question: You mention in your testimony that the private sector will be the real key to the rebuilding effort. What provisions in the President's plan will help the private sector in this process?

Answer: We know we are going to see a large amount of federal money flowing into our state. We also know that we will see a large amount of insurance proceeds flowing into South Mississippi. However, for us to experience the renaissance, the rebuilding bigger and better, we must create an environment that encourages the private sector to re-invest in South Mississippi. The private sector is the key component to creating jobs to jump-start the local economies. If people do not have a job to return to, they have little incentive to move their family back to the devastated region.

The incentives offered under the Gulf Opportunity Zone proposals – specifically, the accelerated depreciation for new capital investments and the increased allocation for private activity bonds – are key components of creating the environment in Mississippi that will encourage the private sector to invest capital.

Question: What proposals in the President's Gulf Opportunity Zone proposal will give the biggest boost to small businesses? To rural and more urban areas?

Answer: The most effective incentive in the GO Zone proposals for small businesses and rural areas is the accelerated depreciation incentive. Any taxpayer can take advantage of the depreciation irrespective of the size of the investment.

The major beneficiaries of the accelerated depreciation incentives could vary significantly and include businesses such as: a heating and air conditioning company that needs to buy a new piece of equipment, a lady who owns a barber shop that is currently renting space but would like to construct a new building, and any companies that had expansions in their 10-year plan that may now be expedited. The accelerated depreciation incentives could help these small business owners make decisions to make capital investments in the affected region.

After all, it is the small businesses that create the majority of jobs in our country.

Question: In last week's hearing in which Governor Barbour participated, Louisiana Governor Blanco mentioned the need to help not just businesses, but individuals as well. What benefits might Individual Development Accounts or KIDS accounts have for the

low-income individuals who are victims of Katrina? What other asset-building provisions have you explored that might benefit individuals and families?

Answer: Individual Development Accounts or KIDS accounts could play a significant role in helping low-income individuals who are victims of Katrina. However, it is important to remember that Katrina didn't discriminate among the rich and the poor, nor did it discriminate based on race, sex, or gender. Katrina was a storm that affected all residents of South Mississippi. We must review issues surrounding the affordability and accessibility of insurance to ensure that a viable private-sector market continues to exist. We also must find ways to reduce the effects of potential huge increases in rates for customers of our investor-owned utilities.

Question: We have seen the amazing role charities have played in the relief effort. How do you see their role in the rebuilding effort? What should we be doing here on Capitol Hill to increase giving?

Answer: There were many heroes in the aftermath of Katrina, but without the help from the charitable organizations and in particular those faith-based groups that continue to operate in Mississippi, I am not sure how much worse things might be. Many of these organizations plan to continue to operate in my state for many years, and they will play a major role in the rebuilding process.

I would like to see Congress look at ways through additional tax deductions and/or credits for contributions to charitable organizations that operate specifically in relief efforts following natural disasters.

From Senator Smith:

Question: Recently, there has been a fair amount of discussion about authorizing a second advance refunding for tax-exempt bonds in the Gulf States. I understand that advance refunding would allow you and other state and local officials the opportunity to reduce your debt service costs or restructure outstanding debt. This has been an issue of particular interest to me, as I have previously sponsored legislation that would permit a second advance refunding for governmental and 501(c)3 bonds. Some bonds, however, like certain airports and port facilities, don't qualify for any advance refunding under current law.

Treasurer Reeves, what do you think about allowing advance refund private-activity airport and port bonds in the areas affected by Hurricane Katrina?

Answer: I strongly support allowing advance refunding for private-activity airport and port bonds in the areas affected by Hurricane Katrina. Under normal circumstances, the benefits derived by our local ports and airports by allowing an advance refunding are far greater than any potential loss in revenue for the federal government.

Under today's circumstances, the allowance of an advance refunding creates maximum flexibility for our ports and airports to restructure their debt burdens to more closely match their expected revenues in a post-Katrina environment. In fact, an advance refunding may help ensure that there are no defaults by any of our ports and airports.

In addition, I believe Congress should allow a second advance refunding for all state and local issuers. My reason for supporting such a provision is identical to the aforementioned benefits to our ports and airports.

From Senator Rockefeller:

Question: Please describe the extent of the damage to school buildings and your estimates of the cost of repairs necessary to reopen the schools in your areas.

What is the greatest need for school facility assistance? Are state and local resources available to provide that assistance?

Is it still reasonable to expect local communities to find a 10-percent match for the tax credit bond program or should the match be eliminated?

In past natural disaster situations, such as the Northridge earthquake in California, FEMA provided funds for the reconstruction of schools. The Department of Education also worked closely with FEMA to make sure efforts to rebuild schools and to reestablish school programs were coordinated with the local school districts. Is this happening yet in your communities?

Recognizing the importance of schools to a community as it tries to reestablish its stability is very important. Schools need to reopen as quickly as possible. But the schools that we rebuild and repair should be schools that reflect today's education needs and programs, not the just replacing the same buildings built 30 years ago. In past disasters FEMA's expectation has been to expect a building to be replaced as it was. How can we make sure that there is enough flexibility in the rebuilding programs to allow local communities to rebuild their schools so they meet today's standards and tomorrow's educational needs?

Answer: The October 19th facility impact from our Department of Education provides a preliminary estimate of 263 schools with damage – 24 of which could be categorized as severe – with 16 totally destroyed. In addition, 159 school buses must be replaced.

The total cost of estimate for repair/reconstruction is \$321 million, replacement of furniture, equipment, technology and textbooks is \$102.5 million, and total replacement cost for instructional materials is \$235 million.

In aggregate, that would suggest a grand total of \$668 million in public school facility and operational losses.

Congress has been generous in the appropriations process, and the U.S. Department of Education has been extremely helpful in creating the environment which allowed all of our schools to get open by the first week in November.

However, as we look at the financial picture of many of our local governments in the Gulf South region, it may not be realistic to expect them to be able to come up with their portion of the 10-percent local match. The reality is that many of the local governmental units in the region have very little tax base left following Katrina. In Mississippi, we have monitored our local government's finances closely and are searching for ways to help those communities as they recover from the worst natural disaster in American history.

STATEMENT OF SENATOR ROCKEFELLER
SENATE FINANCE COMMITTEE HEARING
TAX RELIEF FOR REDEVELOPMENT AFTER HURRICANES
OCTOBER 6, 2005

Mr. Chairman, thank you very much for holding this hearing. We have all been shocked and horrified at the devastation resulting from Hurricanes Katrina and Rita. I am certain that every member of this committee is eager to explore how the federal government can be helpful in alleviating the suffering of the victims and restoring vitality to the affected areas.

For my part, today, I would like to focus on three elements crucial to a vital community: health care, housing, and schooling.

I have been extremely disappointed that the administration has rejected efforts to provide appropriate Medicaid assistance for the victims and the states that have welcomed displaced victims. While it's too late to provide this relief in a timely manner, I am still hopeful that we can reach an agreement to provide essential health care services for our neediest neighbors.

I look forward to working with this committee and the administration to enact tax incentives that can play a role in revitalizing Gulf coast communities. I believe that tax policy can be particularly effective in trying to solve the housing and educational needs faced by families returning to the devastated areas.

Our goal must be the construction of livable communities. We have an opportunity to correct the development mistakes of the past that resulted, for example, in the extreme concentration of poverty in the lower 9th ward. The Low-Income Housing Tax Credit and the Mortgage Revenue Bond program seem to me especially promising in efforts to establish mixed income communities. I am interested in hearing from the witnesses today how we can create healthy, livable communities that will draw Louisianans and Mississippians back to their hometowns.

And we know that families cannot resettle a community if their children cannot be educated there. To rebuild and revitalize these communities, we must repair the damaged schools or construct new schools. Before the hurricanes struck, the National Center for Education Statistics estimated that school construction needs nationwide were \$127 billion – and now it is more.

We have limited school construction bonds that offer tax incentives, but I believe this must be expanded to cover the disaster areas, and even provided nationwide. The need is very clear – in Louisiana, Mississippi, Alabama and beyond. Given that the average age of a school is 41 years old, we really should promote school construction in

every state. I have a bill, America's Better Classroom Act, that would invest \$25 billion in school construction nationwide. We should target aid to the disaster areas, but we should also help every state because aging school buildings are a serious problem in many communities. This effort would improve our schools, and create jobs that boost the local economy.

I understand that the needs of the Gulf communities are not limited to health care, housing, and education. For example, I am very interested in ways that the New Markets Tax Credit program can spur business investment in the devastated communities. However, I am focused first and foremost on the people who will be the employees for these businesses. We need to make their communities habitable again. I hope that this hearing will be the first step in a successful dialogue about how we can help these devastated areas recover.

Senator Gordon H. Smith

**Senate Finance Committee Hearing
“The Future of the Gulf Coast: Using Tax Policy to Help Rebuild Businesses and
Communities and Support Families after Disasters”**

October 6, 2005

Thank you, Chairman Grassley and Senator Baucus, for convening today’s hearing. The devastation caused by Hurricanes Katrina and Rita is a national tragedy and my thoughts and prayers go out to all of those who suffered a loss. It is critical that the businesses and communities impacted by these hurricanes get back on their feet again and their employees can get back to work as soon as possible. Providing targeted tax incentives is integral to helping with this endeavor.

Specifically, I’d like to highlight two tax proposals that I believe will stimulate economic growth in the affected region.

The first proposal is bonus depreciation. I was one of the original authors during the 107th Congress of the bonus depreciation legislation that was enacted to stimulate our economy after the September 11th attacks. Bonus depreciation provided companies with an additional first year depreciation deduction for property placed in service between September 11, 2001 and January 1, 2005. Bonus depreciation reduced the cost of capital investment, and encouraged companies to purchase the latest technology in order to boost their productivity and become more competitive.

Bonus depreciation had a tremendous impact on our economy. Beginning in mid-2000 and throughout 2001, manufacturers’ shipments of non-defense capital goods slumped severely and then began a modest pickup after 30% bonus depreciation was enacted in the Spring of 2002. However, when bonus depreciation was increased to 50% in May 2003, shipment of equipment sharply increased throughout 2003 and 2004. For example, in January 2003, manufacturers’ shipments of non-defense capital goods was 9% below the previous quarter and had barely revived from the severe downturn of 2001. From May 2003 through December 2004, however, the annual rate of such shipments never fell below 5% – and reached as high as 20%.

In light of the recent natural disasters, I introduced a bill earlier this month, S. 1632, allowing for bonus depreciation for a three year period beginning on August 29, 2005. Bonus depreciation has a proven track record of encouraging capital investment and thus, growing our economy. Therefore, I hope that the tax package that is currently being developed will include bonus depreciation so that businesses in the affected areas will be able to afford the new productive equipment they will need to recover and grow.

The second proposal that I’d like to highlight, S. 965, will provide relief to small businesses that are S corporations to ensure that now, more than ever, they continue to be the driving force of our economy.

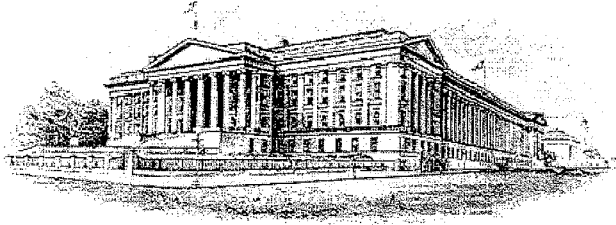
Currently, small businesses that changed their tax status (from C corp to S corp) cannot sell off assets for ten years without being double taxed (a regular tax plus a built-in gains tax). The double tax leads companies to hold unproductive assets much longer than they otherwise would just so they do not have this double tax. This directly affects their cash flow by locking up their assets.

It is estimated that there are 400,000 small businesses across the country that are stymied by this double tax. Taking away this double tax is not just important for those small businesses in the Gulf Coast region that want to rebuild. Businesses across the country may be looking to site facilities in that area. My proposal would make it easier for these companies to sell off unproductive assets and use that cash to rebuild, newly build, and create jobs in an economically devastated region.

We need to help small businesses restart their engines and that is exactly what my proposal would do.

As the Committee continues to consider tax incentives to assist the victims of the recent hurricanes and rebuild the Gulf Coast region, I hope the Committee will consider supporting both of these important proposals.

Thank you.



**DEPARTMENT OF THE TREASURY
OFFICE OF PUBLIC AFFAIRS**

Embargoed Until 10 a.m. EDT
October 6th, 2005

CONTACT: Tony Fratto
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**Testimony of the Honorable John W. Snow
Before the Committee on Finance
U.S. Senate**

Chairman Grassley, Ranking Member Baucus and Members of the Committee, thank you for the work you have done and are doing to help the people of the Gulf Coast region survive and recover. And thank you for inviting me to appear before this committee to explore the ways that Congress and the Administration can assist in the long-term rebuilding of the Gulf Coast region.

As a nation, we continue to grieve over the losses experienced by our fellow Americans who made the Gulf Coast region their home. There was a heartrending loss of life and extensive loss of possessions and property. For many survivors, there is nothing left.

The devastation of Katrina and the repeated misery brought by Rita left a scar on this nation. But America is a strong nation and Americans are profoundly resilient. And many are already rebuilding their communities or are anxiously waiting to start. We intend to help them.

People in the region must rebuild their infrastructure, their homes and their businesses. The overriding goal must be that everyone has an opportunity to build a better life for themselves and their families. We look forward to a time when victims can make their own future. Nothing less is acceptable.

It is critically important – and the President has made this clear – that as we help the region, we do so in a fiscally responsible way. The President called upon Congress this week to pay for as much of hurricane relief as possible by cutting spending. And we will work with you to identify offsets that will free up money for the reconstruction efforts.

Economic Background

We have a strong, vibrant economy, and that is going to be critical as we pursue rebuilding efforts. While there is clearly no “good time” to be hit by a devastating natural disaster, we were fortunate to be standing on very solid economic ground, with robust underlying fundamentals, when these terrible storms struck. Our economic strength undoubtedly enhances our ability to deal with this disaster.

With a strong economy, we can better afford to meet any challenge. I know that this committee is keenly aware of that fact, and I appreciate your work to make our economy the strongest and most adaptive in the world. The work that Congress did to pass economy-invigorating tax cuts in 2001, 2002 and 2003 is one of the reasons we are standing on solid economic ground today.

While the President’s tax cuts were designed for the good of the American people in terms of economic growth and job creation, we are reminded today that a strong economy can also serve as a type of shelter against storms – natural or economic – that are beyond our control.

Over the short term, our economy will feel the impact of Katrina and Rita, as jobs, property, and businesses have been lost, and gas prices have edged higher. High fuel prices are a burden on businesses and family budgets.

These terrible storms likely took away from economic wealth in the third quarter, but I am optimistic that rebuilding efforts will restore lost GDP by the first quarter of next year.

We can encourage this rebound even further by preserving the tax cuts that gave our economy the opportunity to grow and put us on the solid footing we enjoy today. Let me be clear on this point: now is not the time to increase the tax burden on the American people. Lower tax burdens encourage innovation, economic growth and job creation – all the things we need to help hurricane-ravaged communities recover and rebuild.

Treasury and IRS Action in the Wake of the Hurricanes

As the topic of this hearing recognizes, well-tailored fiscal policy is an effective tool during times of disaster recovery. In the wake of both Katrina and Rita, the Treasury Department and the IRS took immediate action to provide tax relief to hurricane victims, and also to encourage the charitable giving that is so important to both short and long-term recovery efforts.

We appreciate that the last thing people in the devastated areas needed to worry about, in the days following these terrible storms, is taxes. So we granted tax filing and payment relief to all affected taxpayers. We also waived certain requirements for developers to receive the low-income housing tax credit so that displaced victims, regardless of financial status, could have access to that housing during this time of great need.

In the aftermath of Katrina, it quickly became clear that diesel fuel was needed for rescue and relief efforts. Treasury has therefore provided relief from penalties for highway use of dyed diesel fuel – a type of fuel that had been limited to certain uses for tax purposes – in order to increase availability of diesel fuel.

We've also announced that we'll be providing additional help for business development by giving a priority to applicants from the Gulf region for New Markets Tax Credits. This step will help encourage businesses and investors to come back to the region quickly to create commerce and jobs.

The IRS also assigned thousands of employees to augment the FEMA hurricane victim registration effort and established its own dedicated toll-free disaster number and a special section of their internet web site. So far IRS employees have answered well over 760,000 registration calls for FEMA. They have answered more than 30,000 calls on the special IRS toll-free line for affected taxpayers, and they have filled orders for nearly 180,000 Disaster Relief Kits.

Commissioner Everson and the terrific employees of the IRS have done an outstanding job. I applaud their dedication and thank them for their excellent service to the American people.

At Treasury, we are also making sure that hurricane survivors have access to the financial resources they need, starting with the checks they receive from the government, like Social Security, unemployment payments, and direct disaster assistance. This is an area where cooperation and support from private industry is also helping us get the job done.

We also worked closely with banking regulators, who have asked the institutions they oversee to consider all reasonable and prudent steps to assist their customers' cash and financial needs in areas affected by Katrina and Rita.

Rebuilding: Higher, Better, Responsibly

As the President said in his September 15th address to the nation, the task of rebuilding “will require the creative skill and generosity of a united country” and our vision of the future is not just to rebuild, but to rebuild “higher and better.”

The Administration is committed to helping the region re-build – and we should do so in a manner that is fiscally responsible.

The relief and reconstruction efforts will be costly and are likely to have a short-term impact on the deficit. But these will be one-time costs. And they can be met while also meeting the President's commitment to halve the deficit by 2009.

I appreciated the story that the President told, in his September 15th speech, about a man in New Orleans who had lost his home. When asked by a reporter if he would relocate, the man said, "No, I will rebuild – but I'll build higher."

Every party involved in the rebuilding and revitalization of the region – from individuals to businesses to government – must embrace the attitude of that man, an individual who has lost so much but will prevail because he lives by a code of common sense and responsibility as well as all-American optimism.

To spend taxpayer dollars on anything that does not "build higher," that does not provide essential relief or generate real progress, or that can be washed away by the next storm, would be irresponsible.

While it is impossible, at this point, to assign a dollar figure to the federal rebuilding efforts, we are committed to principled, disciplined spending that is commensurate with the needs of the region.

We must approach this task with a number of clear goals and be mindful of avoiding moral hazard.

First, we must minimize the exposure of individuals to harm from future disasters. Clearly, the physical disaster protection needs of the region must be met.

Second, redevelopment plans must minimize the future exposure of all taxpayers, in recognition of the fact that the federal government is effectively often the insurer of last resort in large-scale disasters. In other words, we should not set a precedent that the taxpayer is the first-dollar insurer in all disasters.

Finally, redevelopment must tap the resources of the private sector and all of the efficiency and innovation that it brings.

Federal Action to Date

As you well know, over \$60 billion has been appropriated to the FEMA Disaster Relief Fund by Congress for the Katrina emergency response. As of last week, \$19.1 billion of the Disaster Relief Fund has been allocated for programs consistent with the Stafford Act and past practice, namely human services (mostly housing assistance), infrastructure, mitigation, operations and administration.

You have also passed tax relief to assist the victims and encourage rebuilding, and I applaud you for these actions. The people of the region are appreciative to the members of this Committee for acting quickly and decisively, and in a bipartisan manner. We look forward to working with you and hope the same spirit and cooperation will produce a second tax bill in the coming weeks.

The President's Proposals

The President has proposed a number of initiatives to spur rebuilding – and a better life – in the Gulf Coast. We look forward to working with the members of this Committee to bring these proposals to fruition, and I'd like to outline their basic purpose for you today.

A Gulf Opportunity Zone, or GO Zone, would help local economies devastated by Hurricane Katrina by providing tax relief and loans for businesses and entrepreneurs who invest in the region and create jobs. Small businesses in the GO Zone would be able to double their business expensing from \$100,000 to \$200,000 for investments in new equipment, take advantage of a 50 percent bonus depreciation, and receive tax relief for the building of new structures.

The GO Zone would also make available more funding for loans and loan guarantees for small businesses, including minority-owned enterprises, to get them up and running again.

The Gulf Coast hurricanes were specific and devastating events. But there is an American truism that will apply to the recovery of the area just as it has applied to the incredible growth and success of our country since its inception: entrepreneurship will create jobs and opportunity and help break the cycle of poverty. GO Zones are designed to facilitate that power of entrepreneurship and small business to the Gulf Coast.

The President has also proposed worker recovery accounts to help those who need extra help finding a job – a key to independence and a better life.

Finally, the President has proposed an urban homesteading initiative to provide a new beginning, in the form of a new home, for lower-income hurricane evacuees. Homeownership is one of the great strengths of any community, and it must be a central part of our vision for the revival of this region.

The Federal Role: Getting the Right Balance

The size and the scope of hurricane damage is unprecedented in our history. On an individual level, losses came in the form of homes, jobs and loved ones. Economically, lost income and infrastructure damage have national significance.

That said, it is essential that the Federal government play an appropriate role, but it should avoid taking steps that are excessive. We must tailor our response appropriately.

No one can say with certainty how much it will take to rebuild the region. The Federal government is still assessing the cost of lost infrastructure, for example. State and local governments are still grappling with the most immediate needs; they and community leaders will need time to plan.

How can we draw the lines? Much of that has yet to be determined. We must first be sure we understand the nature of the losses, some of which will be covered by insurance and reserves.

The Administration is seeking a backstop for local and municipal governments, to the extent traditional forms of support such as their own tax base, borrowing capacity, and state aid prove insufficient to provide essential services. We will work with the Congress to make sure this aid is effective.

For instance, some have proposed guarantees or other backstops of local and municipal bond issuance. In this area, I want to be very clear: while relief is needed, federal assumption or guarantees of localities' debt is highly undesirable and something Treasury would oppose. A federal bailout in the form of Treasury guaranteeing municipal securities could result in a risk premium on Treasury issuance going forward.

Providing a guarantee – a government-sponsored protection of investors – would be an intrusion in the private markets, disrupting the assessment of risk, which is essential to the proper function of markets. More importantly, such a guarantee would do little to put actual money in the hands of those who need it most - the individual victims. We cannot support that.

The Task Ahead

The task ahead is not simple, but America is no stranger to struggle, nor to solutions. We picked ourselves up after 9/11 and other disasters, and we have the will and the resources and the resolve to do so again. It is the spirit of Americans to pick themselves up, to rebuild and to be stronger than ever before.

Let me close by laying out a course of action that I believe will translate to the fiscally responsible rebuilding that I believe we are all committed to:

- Build infrastructure that mitigates the future exposure to storm damage.
- Avoid moral hazard by taking steps to promote and encourage prudent future planning including the appropriate role of insurance.
- Avoid damaging the national economy and our financial system.

Thank you, we look forward to working with you, and I look forward to taking your questions.

Questions for the Record
The Honorable John Snow
October 13, 2005

From Senator Santorum:

1. What proposals in the President's Gulf Opportunity Zone proposal will give the biggest boost to small businesses? To rural and more urban areas?

Answer:

The President's Gulf Opportunity Zone ("GO Zone") proposal includes several incentives to assist small businesses affected by Hurricane Katrina. The proposal allows an additional first-year depreciation deduction equal to 50 percent of the cost of new investment in the GO Zone, before application of the regular depreciation rules. This depreciation deduction applies to investments in equipment and certain other structures placed in service prior to the end of 2007, and to investments in buildings and land improvements placed in service before the end of 2008.

The GO Zone proposal also expands an expensing provision now available to small businesses. Current law allows small businesses generally to deduct up to \$100,000 (indexed for inflation after 2003 and before 2008) of the cost of certain tangible depreciable property. Investment in property in excess of \$400,000 (again indexed for inflation after 2003 and before 2008) reduces the expensing limit dollar for dollar, so that this provision does not apply to larger taxpayers that have investments in property in excess of roughly \$500,000. The President has proposed increasing the small business expensing limit by up to \$100,000 (indexed for inflation after 2003) for qualifying property placed in service in the GO Zone before 2008. In addition, unlike current law, the President has proposed allowing similar expensing of investments in real property placed in service before 2009, up to an annual limit of \$200,000 (indexed for inflation after 2003). Both expensing limits will be reduced by 50 cents for each dollar of new qualified GO Zone property above specified amounts.

These incentives will provide immediate relief to small businesses by substantially lowering the cost of replacing depreciable property destroyed by Hurricane Katrina, and should greatly assist in rebuilding the economy in the affected region. This relief will be available even in cases where taxpayers temporarily have no taxable income, as tax losses may be carried back to prior profitable tax years, generating an immediate carryback refund. In addition, because the President's proposal extends the bonus depreciation and expensing provisions to all new depreciable investment, it will be an unbiased tax incentive. This will encourage sustainable growth and help to ensure that the private sector, not the government,

will determine where, how much, and what type of private sector investments are made in the disaster area.

The expensing provision gives a greater incentive to small business than does the more generally available bonus depreciation proposal, although both are needed to assist economic recovery in the region affected by Hurricane Katrina. The provisions make no distinction between urban and rural locations, so both areas should benefit. The President's GO Zone proposal will aid equally in the replacement and reconstruction of damaged business property in both rural Mississippi and the city of New Orleans, and will not create a bias towards one area or the other.

2. In last week's hearing, Governor Blanco mentioned the need to help not just businesses, but individuals as well. What benefits might Individual Development Accounts or KIDS accounts have for the low-income individuals who are victims of Katrina? What other asset building provisions have you explored that might benefit individuals and families?

Answer:

The Administration supports expanding the existing Treasury Individual Development Account (IDA) programs and funding the expanded programs with tax credits rather than solely with grants. Withdrawals could be made from the IDAs for certain higher education expenses, first-time home purchases, and small business capitalization. Many Katrina victims need funds for these purposes and could have benefited from IDAs. Individuals with some savings are generally better able to deal with catastrophes like Katrina than are people without such a cushion. In its budget proposals last year, the Administration included a comprehensive expansion and simplification of the tax incentives for saving that, if adopted, would go a long way to providing relief in the event of future natural disasters.

3. We have seen the amazing role charities have played in the relief effort. How do you see their role in the rebuilding effort?

We applaud the role of charities in the hurricane relief effort. Charities have a long tradition of helping Americans in need and play a critical role in helping disaster victims to rebuild their lives in the aftermath of natural disasters. That role is recognized in the Federal disaster relief statute (42 U.S.C. § 5152), which authorizes the President to work with disaster assistance organizations in distributing needed medicine, food, supplies, or other items, and in restoring essential community services and facilities. We welcome the continued assistance of charities and their dedicated workers in the rebuilding effort. We applaud the Congress for enacting legislation to promote charitable contributions to charities involved in delivering assistance to victims and in rebuilding devastated communities.

4. Senator Lieberman and I recently introduced the CARE Act, S. 1780, to increase charitable giving. I also recently sent a letter requesting the full support of this Administration for that bill. Will the Administration put its full resources behind this bill?

The Administration strongly supports efforts to expand charitable giving and to provide support to charitable organizations that help serve Americans in need. The CARE bill includes many provisions that are consistent with the Administration's goal of promoting charitable giving across the Nation. For example, the Administration has proposed removing a significant barrier to charitable contributions by allowing individuals over age 65 to make tax-free distributions from their Individual Retirement Accounts directly to charity. The Administration also has proposed new incentives for businesses to donate food inventory to help the needy. We applaud Congress for including a similar food donation provision in the recent Hurricane Katrina relief bill.

The Administration supports many provisions in the CARE bill and looks forward to working with Congress to ensure that these provisions are consistent with the President's Budget proposals. The Administration is concerned about certain provisions that would unnecessarily complicate the U.S. tax code and would raise significant policy concerns. We look forward to working with Congress to develop alternatives to these proposals.

From Senator Baucus:

1. Under the terms of the vacation donation program Treasury set up after Katrina, employees donate their vacation time tax-free and employers convert the time into cash and donate it to a charity. I appears Treasury is using administrative guidance to change tax law since the rules regarding taxable income, including vacation pay, are well established.
 - a. Please explain how Treasury has the authority to override established tax law with respect to this guidance.

Answer:

Following the September 11, 2001 terrorist attacks on the World Trade Center and the Pentagon, we learned that employers were taking the position that employer charitable contributions made on account of employees giving up leave constitute a business expense deduction under Code section 162 rather than a charitable contribution deduction under section 170. As a result, the Treasury Department and the IRS decided to study the issue. On October 24, 2001, we issued Notice 2001-69 stating that, for a limited time, the IRS would not assert that payments made by an employer to an organization described in section 170(c) in exchange for leave

that employees elect to forgo result in constructive receipt of gross income or wages for the employees.

Although IRS and Treasury sunsetted Notice 2001-69 as of January 1, 2003, we believe that the displacement of tens of thousands of Americans and the tremendous destruction caused by Hurricane Katrina is not an appropriate time to take a technical enforcement position on this issue, especially where the impact on a taxpayer's liability would not be significant. Thus, in response to numerous public and Congressional requests, we issued Notice 2005-68 providing similar administrative relief to that provided after September 11. As with Notice 2001-69, the administrative relief is provided only for a limited period of time. We note that, unlike the notice issued following September 11, the current notice is more limited in that it only applies to charities that are providing relief to the victims of Hurricane Katrina.

- b. In general, what criteria does Treasury use to determine whether it has administrative authority or whether it legislative action is necessary?

Answer:

The Treasury Department and the IRS continually strive to interpret the Internal Revenue Code as enacted by Congress. If the facts of a particular situation are not addressed directly by the unambiguous words of the statute, however, we seek to apply rules that we believe reflect the intent of Congress, as expressed in the legislative history of the applicable statute. If the intent of Congress is not clear from the legislative history, we seek to provide rules that are consistent with both the wording of the statute and good public policy. If the Internal Revenue Code is clear, but a different result is appropriate under the circumstances, the Treasury Department and IRS will seek a legislative change by Congress.

2. Staff touring the Gulf Coast area visited FEMA sites and the IRS presence at those sites. In the Baton Rouge FEMA location, the IRS employees have only 1 computer and 2 phone lines. In Lafayette, they don't have any computer. Taxpayers need transcripts and other information to apply for SBA loans and to get their affairs in order. Where there is no computer, they have to fill out a paper form and wait for it to be mailed to them.
 - a. Do you consider this to be acceptable service for taxpayers who need information quickly and may not have a reliable permanent address or transportation?

Answer:

As FEMA sites were opened, the IRS immediately began to initiate procedures to properly staff the sites. Equipment needs generally vary at the sites which are operated by FEMA. As equipment needs are identified, requests were made to the

IRS Modernization & Information Technology Services (MITS) and filled. Recently, the IRS has contacted FEMA about establishing a minimum level of service at each DRC to be a phone and fax line that will become a standard requirement now and in the future. As a result of the IRS request, the minimum requirements will become standard for all future FEMA Disaster Recovery Sites (DCR).

Cell phones have been provided to IRS staff deployed to Katrina/Rita FEMA field DCRs. Additional fax machines have also been ordered. Additionally, the IRS is working with MITS to develop a long-term strategy for additional technology enhancements relative to disaster relief assistance programs.

- b. What is Treasury doing to monitor these sites and to make sure IRS has the equipment and infrastructure it needs to give taxpayers the help they need?

Answer:

IRS closely monitors the equipment needs specific to each of the disaster assistance sites. Additional equipment is placed where needs are identified (i.e. tent sites, mobile sites vs. permanent ones).

- c. The IRS Taxpayer Advocate brought the phone line shortage in Houston to your attention. What did you do after she told you about it? Did you ask FEMA for more phone lines?

Answer:

The issue involving phone line needs at one of the Houston sites has been resolved.

- 3. FEMA is going to pay Carnival Cruise Lines \$236 million to use 3 cruise ships for 6 months to house evacuees and relief workers. This works out to over \$30,000 per person, about double the going rate for a cruise. The terms of the contract include reimbursement for taxes. However, despite these generous terms, I also understand that Treasury is considering granting a waiver to Carnival that would exempt this income from US tax.
 - a. What is the status of this matter? Has Treasury made a decision?
 - b. Since the law appears quite clear that this income should not be exempt from US tax, do you think that Treasury has the authority to grant this waiver? Was Treasury involved in the contract negotiations? Were any promises or representations made to Carnival that it would receive this special treatment as part of the deal?
 - c. Do you think it is good policy for Treasury to even consider granting special relief in this situation? It's not like Carnival is going to be harmed without it – the contract already covers payments for taxes. Is it really in the best interest of the public for Treasury to interfere in this process by exceeding its authority to give Carnival this huge tax break?

Answer:

The Treasury Department cannot comment on its position with respect to requests for guidance by individual taxpayers. However, Treasury does have a fair amount of leeway under the relevant Code provision to interpret the types of activities that are so closely related to the international operation of ships that they should not be regarded as a separate source of income and thus, may qualify for an exemption from U.S. taxation as income that is incidental to the international operation of ships. In exercising this regulatory authority, the Treasury Department considers the treatment by other countries of U.S. shippers engaging in such activities because the exemption for income from the international operation of ships is a reciprocal one. Nevertheless, the Treasury Department does not feel there is a need for any additional Katrina-related shipping guidance.

4. The Small Business Development Corporation (SBDC) uses IRS transcripts to verify the tax history of applicants who do not have copies of their tax returns. In response to a joint letter from the Senate Finance Committee and the Small Business Subcommittee, Commissioner Everson stated that a process had been worked out between IRS and SBDC to expedite the delivery of the transcripts, but the process was not described.
 - a. Please provide a detailed, step-by-step, description of the process.

Answer:

Obtaining IRS Transcripts

Guidance for Small Business Development Centers

IRS transcripts are useful to taxpayers affected by Hurricanes Katrina and Rita for assistance in reconstructing financial records and completing loan applications and can be obtained through several methods. Clients who make appointments for assistance at SBDC sites can obtain transcripts to bring to their appointment using the following options:

- Call the IRS Disaster Hotline at 1-866-562-5227 to request transcripts be mailed to the address of record. If the address has changed, the operator will change the address and send the transcript to the new address.
- Fax or mail a Form 4506-T, Request for Transcript of Tax Return to the appropriate number or address listed on the form. Indicate "Hurricane Katrina" or "Rita" at the top and the request will be worked within 24 hours.
- If visiting a FEMA site staffed by IRS personnel, the IRS employee can obtain a copy by fax for the taxpayer.
- If near an IRS Taxpayer Assistance Center, transcripts can be printed for taxpayers while they wait.

For clients in SBDC sites obtaining assistance who have not previously secured copies of IRS transcripts, special procedures have been established:

- Have the taxpayer complete a Form 4506-T, Request for Transcript of Tax Return.
- Request they enter the SBDC site location and fax number in item 5.
- Write "SBDC – Disaster Hardship Relief Assistance" on the top of the form.
- Fax the completed form to the appropriate number shown below:
 - Alabama and Mississippi (866) 297-3199
 - If questions, call (877) 826-7104
 - Louisiana – (866) 895-2847
 - If questions, call (866) 499-7830
 - Texas – (713) 209-3708
 - If questions, call (713) 209-3660.
- Requests received between 8:00 and 4:00 Monday through Friday will be worked and faxed back within one hour.

- b. What is the time frame between the request for the transcript and the time it is received by SBDC?

Answer:

Transcripts are being provided within 1 hour.

- c. You stated during questioning that you supposed there could be IRS people at the SBDC sites. Would physical IRS presence at the SBDC sites, assuming adequate computers, phone lines and other equipment, expedite or in any way facilitate the process? Are IRS personnel at these sites now? If not, why not?

Answer:

Both IRS and the SBDC's agree that co-location of IRS employees at their sites is not the most effective or time efficient way to provide expedited transcript service to the SBDC's since one hour turn around is currently being provided. Also, we will continue our long standing partnership with the SBDC's to provide disaster relief seminars and other outreach and education materials.

- d. Has the SBDC expressed any concerns with the present arrangements?
What are you basing this answer on?

Answer:

IRS has contacted the SBDC State Directors to discuss the expedited transcript process and convey IRS support for any additional needs they may have. At this time, no concerns have been expressed.

- 5. The Katrina tax legislation already passed has a multi-billion dollar price tag. Any subsequent Katrina legislation obviously will add significantly to the cost.
 - a. Do you think offsets should be used in Katrina legislation?

Answer:

The Administration does not favor increasing tax rates on other income sources to offset the cost of further tax relief related to Hurricane Katrina. The President has indicated that, to the extent possible, hurricane relief should be paid for by reducing spending.

- b. What offsets to you think should be used to pay for this legislation?

Answer:

We will work with Congress to identify spending reductions that will free up money for hurricane reconstruction efforts. I applaud the efforts of the Senate Republican Leadership and Budget Chairman Gregg, who have requested Committee Chairmen to find additional savings to pay for the costs of Katrina. They asked Committee Chairmen who received reconciliation instructions to go above and beyond their savings targets and also asked non-reconciled committees to review policies and programs to find savings.

- c. To what extent does Treasury consider shutting down corporate loopholes and abusive transactions to be a tax increase?

Answer:

Ensuring that taxpayers do not apply the tax laws in ways that Congress never intended is not a tax increase. Similarly, ensuring that taxpayers are not able to engage in abusive transactions to avoid paying their full tax liability permits the government to collect the tax due under existing law, and is not a tax increase.

- d. Please explain how permanentizing tax cuts, including capital gains and dividends, will help pay for Katrina relief, as you have stated.

Answer:

A healthy national economy is a vital component of promoting economic recovery in the area devastated by Hurricane Katrina. The American economy has grown at a strong and steady pace since passage of the dividend and capital gains tax cuts in 2003. This has led to growing tax revenues, including a 15 percent increase in individual income tax revenues for fiscal year 2005 over 2004. Increasing the tax rates on dividends and capital gains would reduce the incentives for Americans to invest in the new business opportunities that create jobs. This would hurt the continuation of the current economic expansion and negatively impact hurricane recovery efforts.

While there is never a good time to be hit by a devastating natural disaster, we are fortunate to have a strong and growing economy that will facilitate efforts to quickly rebuild the areas affected by the hurricane. Lower tax burdens encourage innovation, economic growth and job creation – all the things we need to help hurricane-ravaged communities recover and rebuild.

6. What impact will Katrina related efforts have on effective tax administration, including:
 - a. The 2005 filing season
 - b. Call centers diverted to FEMA assistance
 - c. Ability to implement legislative changes timely

Answer:

RESPONSE (a): Hurricane Katrina-related efforts will have an effect on the filing season due to the impact on affected taxpayers of forms and publication, processing and programming changes required by the Katrina Emergency Tax Relief Act. IRS Toll-Free, walk-in and volunteer income tax assistance programs must also make changes for the FY 2006 Filing Season in order to assist taxpayers. For example, in the Taxpayer Assistance Centers (TAC), efforts are underway to train all frontline employees to handle the expected increase in Katrina-related contacts. The IRS is also taking steps to ensure taxpayers dispersed across the country as a result of the disaster will receive needed assistance at any TAC. While there were several TACs

initially closed because of the disaster, all are open except for Gulfport and New Orleans and these locations will open on or before November 1, 2005.

In addition, the IRS is working with their local and national volunteer partners to support the availability of volunteer services in the disaster areas. To address this issue, the Stakeholder Partnerships, Education and Communication (SPEC) organization is engaged in discussion and planning with these partners to determine ways to assist them and the evacuees. Engagement activities include contacting partners to determine impact to sites located in the disaster area and implementing updated policy, guidance and training relative to operational issues and legislative changes.

RESPONSE (b): In accordance with an existing Interagency Memorandum of Understanding, the IRS began supporting FEMA with 650 IRS employees answering Katrina-related telephone calls on August 29th. By September 26th, there were approximately 4,100 IRS employees answering FEMA calls related to Hurricanes Katrina and Rita in four locations which were modified to accept FEMA call traffic and count call activity. In addition to responding to FEMA calls, IRS operates a distinct disaster assistance telephone line where tax-related information is provided to victims of Hurricane Katrina. From August 29th through October 14th, IRS has answered 785,934 FEMA calls and 42,984 calls on the IRS Special Services Disaster Hotline.

The IRS was able to accomplish this level of FEMA support while simultaneously maintaining regular Toll-Free tax assistance services. Although four Toll-free sites were devoted to providing FEMA services and daily performance did decline, the overall impact to normal Toll-free operations was minimal. For the fiscal year, prior to the beginning of FEMA support, CSR LOS was 83%. Through September 30th, CSR LOS dropped slightly to 82.6%. Average Speed of Answer (ASA) has increased through the same period from 250 seconds to 258 seconds.

RESPONSE (c): The Service's ability to adequately implement legislative changes is largely dependent on making necessary changes to forms, publications and programming in time for the affected filing season. If no other legislation passes, the 2005 Form 1040 and its related products will be approved for printing and released to the contractor on November 15, 2005. This will allow the IRS to make necessary changes for the Katrina Emergency Tax Relief Act of 2005 and meet the originally scheduled shipping dates for the 1040 packages at an additional cost of \$250,000.

However, if additional KETRA legislation is passed, it may seriously impact the 2005 filing season. The Service may not be able to timely issue all tax packages or timely process tax returns if new changes are effective for 2005. It may also impact the number of returns that can be filed electronically. Additional contractor and postal costs would also be associated with the delays.

7. Do you think that nominees seeking Senate confirmation have a duty and responsibility to assure the public that they are complying with our tax laws and paying their fair share of the Nation's revenue needs?

Answer:

All citizens have a solemn duty to comply with the tax laws of the United States, including Presidential nominees seeking Senate confirmation. We should strive to attract highly qualified people to serve in responsible positions overseeing our tax system.

8. A study released last week found that almost one-third of American children are in families that do not qualify for the full child tax credit because their earnings are too low. This study found that almost half of African American children and 46% of Hispanic children qualified for less than the full credit. The former House Republican Speaker, Newt Gingrich, expressed concern with these findings and suggested changes should be made as part of any broader post-Katrina plan. Do you agree with him?

Answer:

I believe you are referring to a study published by the Tax Policy Center. The study was informative, but missed several important points. The study did not take into account the earned income tax credit. When the refundable child tax credit was expanded in 2001, it was designed to offset the work disincentives caused by the phase-out of the earned income tax credit. Indeed, the refundable child tax credit begins to phase in just as the earned income tax credit peaks. Thus, many low-income working families who are not receiving the full amount of the child tax credit are, in fact, entitled to a fairly large earned income tax credit.

As the study found, many of the families who are not eligible for the refundable child tax credit do not have any earned income. Expanding eligibility to include these individuals would change the fundamental nature of the current child tax credit, changing it from a work subsidy to an assistance program that could discourage – not encourage – work. The study notes that the IRS could not easily administer such a subsidy program. Moreover, many nonworking families currently do not file tax returns, but would be forced to do so solely to obtain the child tax credit if eligibility was expanded to families that do not have any earned income.

Finally, expanding eligibility of the child tax credit would be costly. We should be focusing our limited resources on providing assistance to individuals directly impacted by Hurricane Katrina.

9. We have read that the city of New Orleans laid off half of its workforce this week (about 3,000 workers). This could mean a huge drop in city services, although at

present, officials have promised it will not affect emergency services. As a former businessman, you must understand that businesses will be hesitant to move back to a city under such dire circumstances. Your testimony states, however, that you oppose any sort of federal guarantee or backstop for municipal debt. What is the President's plan for providing fiscal relief to these local governments so they can operate for the protection of their citizens and businesses?

Answer:

- **The best way to provide fiscal relief to these governments is to get these local economies back on their feet, with rebuilding, retail sales, and business activity generating revenue. That's what everybody, including local government officials, wants.**
- **But we know there's more to do. That's why the President signed into law the "Community Disaster Loan Act of 2005," which authorizes funds for community disaster loans to assist local governments that suffer substantial revenue loss as a result of a major disaster. That kind of help is more cost-effective than providing a blanket backstop to municipal debt.**
- **Providing a guarantee would disrupt the very thing financial markets do best – assess and price risk. In this case, more importantly, a guarantee won't put money in the hands of those who need it most - the individual victims.**
- **Federal guarantees of municipal bonds are an inefficient method of providing relief to affected states and local governments because a portion of the benefits would be realized by bond holders and not the issuing states and local governments. The benefits of the guarantee would be shared between bondholders and local governments. Grants are far superior method of assistance.**
- **With respect to community health and safety, Louisiana is still in a state of emergency in which the federal government aids state and local response efforts. In particular, FEMA is to coordinate all disaster relief efforts to alleviate the hardship and suffering. Further, though, FEMA is authorized to provide appropriate assistance for required emergency measures, under Title V of the Stafford Act, to save lives, protect property and public health and safety.**
- **In addition to the numerous existing disaster relief programs currently in use in affected areas, the President has also proposed several new programs to provide relief to businesses and individuals. The President's Gulf Opportunity Zone (GO Zone) proposal would provide immediate incentives for job-creating investment, tax relief for small businesses, incentives to companies that create jobs, and loans and loan guarantees for small businesses, to get them up and running again. The GO Zone proposal will double small business expensing from \$100,000 to**

\$200,000 for investments in new equipment, provide a 50 percent bonus depreciation for all businesses, and extend tax relief to the building of new structures. Worker recovery accounts will also help those who need extra help finding a job. Homesteading will provide a new beginning and a new home to lower-income evacuees.

10. Last month, the President spoke from Jackson Square and cited “deep, persistent poverty,” which has “cut off generations from the opportunity of America” and led to a “legacy of inequality.” Clearly, how we go about rebuilding the city of New Orleans and the Gulf region will determine if we are successful in overcoming these problems. Can you detail the plan you have worked on with Secretary Jackson for rebuilding these communities? How will you integrate the local citizens in these decisions? Can you assure this Committee that your tax incentives won’t simply re-concentrate poverty?

Answer:

The Administration is leading an effort to assess the total devastation in the Gulf region in order to determine where it is viable to rebuild and where it is not. The Treasury Department and the Department of Housing and Urban Development look forward to working with Congress, as well as state and local officials, to apply tools like the Gulf Opportunity Zone (GO Zone) proposals and the President's homesteading initiative as we craft comprehensive short-term and long-term plans for housing and economic development in the affected states.

The objective of both GO Zones and homesteading is to rekindle hope in distressed areas – whether those areas are distressed because of neglect and persistent poverty or through causes of nature, like a hurricane.

Like existing Renewal Communities (RCs), the GO Zone proposals include a requirement that their beneficiaries be residents of, or do business in, the affected areas. In the case of the RCs, there is a statutory resident benefit test that a business is required to meet in order to be eligible for certain tax incentives, such as increased Section 179 expensing for small businesses. To meet that test, 35 percent of the business' workforce must be RC residents. The same test applies to the rural EZ located in Mississippi (Mid-Delta EZ). In the case of the rural EZ, for an EZ business to be eligible for tax-exempt bond financing, it must also meet the 35 percent resident test. The GO Zone tax incentives proposed by the Administration include bonus depreciation and increased Section 179 expensing. These tax incentives track similar RC tax provisions in empowering local residents with control of the rebuilding incentive.

Federal wage and tax incentives are essential to helping the economic recovery of distressed areas. The GO Zone proposals will provide businesses in the affected region with the tools needed to help attract private capital by offering financial benefits to companies that commit to locate in areas where they otherwise might not,

and to target these populations when seeking new employees. By putting tax relief into the hands of local businesses, the GO Zone proposals will ensure that local citizens are directly involved in the decision as to whether, how and where to rebuild.

Areas that experience economic rebirths as a result of business creation often experience new housing development and an influx of new residents with varied socio-economic backgrounds who are attracted to upcoming areas that offer affordable housing opportunities within close proximity to jobs, cultural amenities, transit and other aspects of urban life. Accordingly, by encouraging business development, the tax incentives will foster sustainable growth that will not disappear once the rebuilding process is complete.

11. Did poverty play a role in this disaster?

Answer:

- The “deep, persistent poverty,” of which the President has spoken, was very much in evidence in the destruction wrought by the flood in New Orleans. We have learned that the poor bore the brunt of the devastation because they were most likely to live in the lower-lying, more flood-prone sections of the city, such as Mid-City or the Lower Ninth Ward. In addition, people in these areas were less likely than others to have access to a car: about one in five people who lived in parts of the flooded area had no access to a car, versus one in ten elsewhere – a fact that became critical during the evacuation period.
- As the President has stated, “Within the Gulf region are some of the most beautiful and historic places in America. . . . There's also some deep, persistent poverty in this region, as well. That poverty has roots in a history of racial discrimination, which cut off generations from the opportunity of America. . . . We have a duty to confront this poverty with bold action.”

12. Some local officials have complained to us that a “Housing Command” has been set up, consisting of a few large, “military” reconstruction companies that have no real expertise in building residential houses and who advocate the “trailer park” approach to housing evacuees. Have local housing officials in the affected states been integrated into the Administration’s “Housing Command?” What has the Command proposed for permanent, long-term housing and have they called upon local home builders and community housing advocates to assist?

Answer:

There is a unit of FEMA called the Housing Management Group, formerly called the Housing Area Command (HAC). The HMG’s mission is to provide temporary housing for the families displaced by Hurricane Katrina. The Robert T. Stafford Disaster Relief and Emergency Assistance Act prohibits FEMA controlled

emergency funds to be used for any permanent housing (except in insular areas in limited circumstances). FEMA is limited to providing temporary housing such as travel trailers and manufactured housing. The initial FEMA evaluation of the Katrina disaster determined that there were insufficient existing sites for travel trailers and manufactured housing. The military contractors were engaged to build additional temporary sites and to place travel trailers on the driveways of families whose home is uninhabitable but who plan to rebuild. The contractors also oversaw the use of cruise ships as temporary housing and provided displaced worker housing to critical industries. In addition to the FEMA temporary housing effort, other federal agencies are working to provide single family homes and apartments to displaced families. There are also federal housing programs outside of FEMA that are working with local communities and states to address the permanent housing needs and community planning necessary for a successful recovery effort.

The President created an interagency Hurricane Katrina Task Force on Housing and Relocation Policy to lead the housing efforts through all stages, from shelters to long-term housing, chaired by HUD Deputy Secretary Bernardi. This Task Force will focus on combining state, local, federal, and non-governmental resources to maximize the housing and re-development efforts in New Orleans and the rest of the Gulf Coast. HUD has also joined with FEMA to establish the Joint Housing Solutions Center, the central location for inter-agency housing coordination and planning. These two efforts are more fully described in the testimony of Deputy Secretary Bernardi before the House Appropriations Subcommittee on Transportation, Treasury, and Housing and Urban Development, the Judiciary, District of Columbia and Related Agencies, on September 27.

In the rebuilding process, there will be many important decisions and many details to resolve. The federal government is fully engaged in the mission, but the leaders of the states of Louisiana, Mississippi and Alabama, the city of New Orleans, and other Gulf Coast cities will have the primary role in planning for their own future, so they can rebuild in a sensible, well-planned way. Sensible rebuilding of housing would minimize the exposure of individuals to harm from future disasters; minimize the future exposure of all taxpayers and tap the resources, efficiency and innovation of the private sector.

13. Earlier this year, you said you expected to develop a tax reform plan by the end of 2005, based on the recommendations from the President's Tax Reform Advisory Panel. Those recommendations are now due to be issued November 1. Should Congress still expect your tax reform plan by the end of this year?

Answer:

As you know, the President's Advisory Panel on Federal Tax Reform reported its recommendations to me on November 1. Now that the Panel has delivered its final Report to me, we have begun our evaluation of both its specific and overall recommendations. We will focus much of our evaluation on important specific

issues raised by Congress, and the impact of the Panel's overall packages on specific groups of taxpayers and entities. Once that evaluation has been completed, I will make recommendations for tax reform to the President. My recommendation will go to the President as expeditiously as possible given the need for careful review and evaluation of the options developed by the Panel as well as the need to take account of the public discussion of those options.

14. Recently the New Orleans municipal government announced that it reluctantly has to lay off about 3,000 workers. This could be very detrimental to the economic and civic recovery of New Orleans. A critical goal for New Orleans is to restore economic activity. The salaries earned each week by these 3,000 workers would be recycled back into the New Orleans economy with a multiplier effect. These layoffs deny New Orleans that multiplier effect for its economy. Moreover, many of the workers who are laid off will probably not return to New Orleans at all, harming the city's long-run recovery. Tax credits for businesses won't help if there are no customers in New Orleans to buy their products.

Would the Administration support legislation providing grants or loans to the city of New Orleans to allow it to maintain city workers on its payroll rather than to lay them off?

Answer:

As noted in the answer to Question #9, on October 7, 2005 the President signed into law the "Community Disaster Loan Act of 2005" which provides funds for direct loans to be used to assist local governments in providing essential services.

From Senator Rockefeller:

- 1.) The New Markets Tax Credit is designed to stimulate increased private sector investment and economic growth in low-income urban and rural communities. It offers a seven-year, 39% federal tax credit for investments made in businesses and projects in low-income communities.

Senators Landrieu and Vitter have introduced S. 1765, which includes an increase in New Markets Tax Credit allocation authority directed to areas affected by Hurricane Katrina.

This legislation would increase the New Markets allocation authority in 2005 from \$2 billion to \$6 billion, with \$4 billion set aside for investment in areas affected by Hurricane Katrina, and New Markets authority in 2006 and 2007 would be increased from \$3.5 billion to \$6.5 billion, with the \$3 billion in additional credit allocation authority set aside for investment in areas affected by Hurricane Katrina.

What is the Administration's position on this legislation?

Answer:

The New Markets Tax Credit (NMTC) provides a tax credit to investors who make “qualified equity investments” in privately-managed investment vehicles called “community development entities” or “CDEs.” The CDEs must apply for and receive an allocation of tax credit authority from the Treasury Department and must use substantially all of the proceeds of the qualified equity investments to make investments in low-income communities. The amount of the credit is 39 percent of the equity investment, and is claimed over a seven-year period.

Under S. 1765, a designated Hurricane Katrina Disaster Zone would become a low-income community for purposes of the NMTC. Currently almost half of Louisiana and Mississippi, and over one-third of Alabama, already qualify as “low-income communities” for these purposes. The legislation also would increase from \$9 billion to \$19 billion the total nationwide NMTC authority available in 2005, 2006 and 2007. This additional \$10 billion of authority could be used only for investments in the Hurricane Katrina Disaster Zone.

Disaster relief should be provided in the most efficient manner possible. Any disaster relief using the NMTC should be coordinated with other relief (including the Administration’s GO Zone proposal) to avoid being duplicative. Any expansion of NMTC authority would be unwarranted to the extent it results in credits being awarded to projects that would have been undertaken even in the absence of the credit.

2.) A study by the nonpartisan Tax Policy Center last week found that almost one-third of children do not qualify for a full child tax credit because family earnings are too low. More than half of kids that qualified for no credit at all were in households where at least one parent worked. Almost half of black children and 46 percent of Hispanic children qualified for less than the full credit because household earnings are too low; by comparison, only 18% of white kids were in that situation.

The President said he wanted to address “deep, persistent poverty” and “legacies of inequality” in the Gulf region, but he has made no proposals to enhance the two anti-poverty tax programs: the EITC and refundable child tax credit.

Do these findings disturb you? Will you advise the President to improve these programs to address issues of poverty and inequality?

Answer:

The Administration has supported past efforts to expand the Earned Income Tax Credit (EITC) and refundable child tax credit. Specifically, we supported provisions to provide marriage penalty relief for EITC claimants as well as to simplify the EITC eligibility rules, contained in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). The Administration also supported

the expansions of the refundable child tax credit contained in EGTRRA and the Working Families Tax Relief Act of 2004.

The study by the Tax Policy Center contained policy conclusions that would fundamentally alter the nature of our current tax assistance programs for working families. As the study found, many of the families who are not eligible for the full child tax credit do not have any earned income. Expanding eligibility of the refundable child tax credit to include these individuals would change the fundamental nature of the current child tax credit, changing it from a work subsidy to an assistance program that could discourage – not encourage – work. The study notes that the IRS could not easily administer such a program. Moreover, many nonworking families currently do not file tax returns, but would be forced to do so solely to obtain the child tax credit if eligibility was expanded to families that do not have any earned income.

Further, the study omitted the role of the earned income tax credit in meeting the needs of very low-income working families. Indeed, the refundable child tax credit begins to phase in just as the earned income tax credit peaks. Thus, many low-income working families who are not receiving the full amount of the child tax credit are, in fact, entitled to a fairly large earned income tax credit.

Expanding eligibility of the child tax credit and earned income tax credit would be costly. We should be focusing our limited resources on providing assistance to individuals directly impacted by Hurricane Katrina.

3.) Existing federal tax credit programs (Qualified Zone Academy Bonds, QZABs) to assist with school facilities can be used to renovate and repair schools but cannot be used for new construction projects. Given the scope of the damage done to school buildings some schools may be beyond repair. Would it be helpful to you if the federal programs that help to underwrite the financing of school bonds through tax credits be changed so that communities in the states affected by Katrina and Rita can use these bonds for new construction purposes as well when necessary?

Answer:

State and local governments can issue qualified zone academy bonds (QZABs) to finance the rehabilitation or repair, but not new construction, of public school facilities. QZABs may also be issued to provide equipment, develop course materials, or train teachers at qualified academies. Current law establishes authority to issue \$400 million of QZABs for each year from 1998 through 2005. The annual cap is allocated among the States in proportion to their respective populations of individuals below the poverty line. For 2005, the total QZAB authority for Alabama, Louisiana, and Mississippi is approximately as follows: \$7 million for Alabama, \$7.9 million for Louisiana, and \$4.8 million for Mississippi. Since money is fungible, the funds made available by QZABs do facilitate the

construction of new schools to the extent that they free up money that would otherwise be allocated by the States for rehabilitation and repair.

4.) Given the huge need for school repairs and construction in the disaster areas, and throughout the country, shouldn't we expand the QZAB program, and consider S.1538 America's Better Classroom Act to invest in education, and simultaneously create jobs and boost local economies?

Answer:

The President's Budget for Fiscal Year 2006 proposes to extend the authority to issue \$400 million of QZABs per year for two years to 2006 and 2007.

S. 1538 would authorize the issuance in 2006 and 2007 of an aggregate of: (1) \$22 billion of tax credit bonds for construction or rehabilitation of school facilities; (2) \$2.8 billion of additional QZABs; and (3) \$400 million of tax credit bonds issued by Indian tribes for school purposes. The Administration has serious concerns regarding the cost, scope, and complexity of S. 1538. The \$22 billion of tax credit bonds proposed in S. 1538 for 2006 and 2007 would exceed by 28 times the \$800 million of QZABs proposed by the Administration for that period. S. 1538 also contains provisions that would result in undue complexity. For example, unlike the QZAB provision, S. 1538 would permit the credit and the bonds to be separated, or "stripped," and sold separately; would allow the tax credit bonds to be held by mutual funds; and would allow the credit to be transferred through sale and repurchase agreements.

5.) Secretary Snow, it has been suggested by some that the Trade Adjustment Assistance Health Coverage Tax Credit (HCTC) could be used as a model to help the victims of Hurricane Katrina secure health insurance. This suggestion has been made despite the inability of the TAA Health Coverage Tax Credit to provide significant numbers of trade displaced workers with access to health insurance. Congress made a promise to American workers in 2002 that the potential loss of jobs from trade-related activities would not equal the loss of health coverage. However, this promise has not been realized because most of the displaced workers potentially eligible for the HCTC have not been able to access the credit because of significant barriers to enrollment, including prohibitively high premiums.

Does the Administration support using the HCTC to administer health insurance to hurricane victims? If so, how would the Department of the Treasury administer such a program? How would potential enrollees be protected against prohibitively high premiums and medical underwriting in the individual market? What would happen to hurricane evacuees with pre-existing conditions?

Answer:

The Administration generally does not support using the HCTC to administer health insurance to hurricane victims. We are concerned about the amount of time it would take to adopt new eligibility, enrollment, and payment procedures necessary to get the credit to the right people. Moreover, it might be difficult to justify providing the credit to hurricane victims when there are so many individuals who do not have access to affordable health coverage, in addition to those whose coverage was adversely affected by the recent hurricanes.

We believe that the time and funds necessary for the development of eligibility, enrollment, and payment procedures would be better spent on providing assistance to those individuals and families nationwide who desperately need access to affordable health coverage. The Administration's 2006 budget includes an advanceable, refundable tax credit for health coverage for lower income individuals and families. It would be provided on a much larger scale than the HCTC and we believe it can be administered more efficiently on a per capita basis. Moreover, the Administration's proposal would more precisely target the assistance to those who really need the subsidy.

6.) Please give me a status report on the HCTC program. I am specifically interested in the most recent enrollment figures as well as the steps the Department of the Treasury is taking to improve enrollment.

Answer:

The enrollment figures you reference were largely (63%) Trade Adjustment Assistance (TAA) or Alternative Trade Adjustment Assistance (ATAA) related individuals. In fiscal year 2005, through September 2005, the Advance HCTC Program has received over \$38 million from participants and paid more than \$106 million to health plans, including almost \$68 million paid by the IRS.

As for end-of year HCTC claims, the IRS has paid \$24.6 million on 14,613 Tax Year 2004 returns.

The total use of the HCTC increased 40 percent in 2004. Approximately 28,000 taxpayers used the HCTC in 2004 (advanced payment and end-of year claims), as compared to approximately 20,000 in 2003.

The IRS is committed to supporting efforts to improve enrollment in the HCTC. To that end, the IRS conducts a number of different activities including:

- Sending marketing letters to states to promote state-qualified plans (e.g. California, New Jersey, Louisiana, Kentucky and Arizona)
- Specific outreach to large industry groups (e.g. US Airways, United Airlines)

- **Coordinated efforts with unions, company executives and states to increase communication about the HCTC program.**
- **Outreach to assist states as new state-qualified plan options are established**
- **Outreach to assist states in communicating the availability of the State's National Emergency Grants program to help cover the costs of health coverage to bridge the gap for taxpayers from separation to enrollment into the HCTC program.**

7.) The Low Income Housing Tax Credit is an example of a public private partnership, and the LIHTC Program has been recognized as the most successful affordable housing program. Using federal tax credits, the program brings private capital into an area that would not otherwise be marketable.

What role should public private partnerships such as the Low Income Housing Tax Credit should play in the rebuilding effort?

Answer:

The process of rebuilding the areas of the Gulf Coast devastated by Hurricane Katrina will require the combined efforts of Federal, State and local governments, along with private industry and charitable organizations. There are clear areas for government funding, such as the rebuilding of roads and bridges, while private investment and market forces will primarily lead to the redevelopment of homes and businesses in an efficient manner. Local governments can help rationalize the rebuilding through effective and responsible zoning laws and building codes. In some cases, combined public and private funding can help direct investment towards those in our society with the greatest need, such as providing affordable housing to low-income households.

The low-income housing tax credit (LIHTC) is an existing tax subsidy program that encourages the production of rental housing for low-income households. Taxpayers who invest in qualified low-income rental units are eligible for the LIHTC. The LIHTC may be claimed over a 10-year period for a portion of the cost of rental housing occupied by tenants having incomes below specified levels. State housing authorities are allocated first-year credit authority equal to the greater of \$2 million or \$1.75 per capita, indexed for inflation beginning in 2003. Qualifying projects receive credits over 10 years that may have a present value of up to 70 percent of qualifying costs for new construction and up to 30 percent for substantially rehabilitated housing that is federally subsidized or for existing buildings. Credits are recaptured if the required number of units are not rented to qualifying low-income tenants for a period of 15 years.

The Administration would like the current law allocation of the LIHTC to be used to the extent possible to provide affordable housing to residents of the affected region. The Administration would be in favor of expanding LIHTC authority only

to the extent that such expansion can be shown to be a cost-effective method of subsidizing affordable housing to residents of the affected region.

From Senator Kerry:

1) I want to thank the IRS for their response to a letter that I sent with Senators Snowe, Grassley, and Baucus. The letter requested that the IRS provide assistance to Small Business Development Centers (SBDCs) in their role of trying to help small businesses in the Gulf Region with loan applications. As of Wednesday, only 20 small business loans have been approved. The IRS and the SBDCs have worked out an expedited process to help businesses obtain tax information. Many small businesses affected by the hurricane have lost all their records. Yesterday, I received a letter from Commissioner Everson stating that there is an agreement on this. I am concerned that the letter does not specifically state the details of the agreement. It is my understanding that an expedited process has been set up in order for the SBDCs to get taxpayer information. Could you explain the process and the amount of time it will take for a small business to obtain the tax information it needs to complete an SBA loan? How easy will it be for the SBDCs to obtain the needed information?

Answer:

An agreement is in place with SBDC and written procedures were provided to the State Directors of the SBDCs conveying expedited procedures and processes IRS and SBDCs will utilize to ensure expedited transcript processing.

2) The tax breaks in the Gulf Opportunity Zone are focused on capital investment. Small business expensing could help small businesses with the purchase of replacement equipment, but I am concerned that this relief will come too late. Wouldn't it make more sense to provide grants and loans to small businesses before tax relief is provided? Senator Snowe and I have introduced legislation and offered an amendment that was included in CJS appropriations that would increase the authorization for the disaster loan program and authorize \$450 million in grants to the state governments of the affected states. Why shouldn't this legislation be acted on now?

Answer:

The Administration will continue to marshal resources to address the needs of those impacted by Hurricane Katrina. Congress acted swiftly to make sure that appropriate relief was provided to the victims, the first order of business in responding to the hurricane. The President requested and Congress appropriated \$62 billion in funding for the relief effort, which included funding for existing FEMA loan programs.

The next step is to focus on rebuilding. There are several principles that will help inform this stage of relief. Further relief should be proportional to the disaster. Since it is still relatively early in the rebuilding process, we need to continue to

evaluate the needs of the area before finalizing the scope of our commitments. In this regard, tax relief is just one component of a broader set of policies. We learned from our experience in New York after the terrorist attacks on September 11 that tax relief is not always the best policy instrument to deliver relief. Some aspects of the initial round of tax relief provided to New York were not well-suited to the pace of redevelopment and the State and the City of New York have since requested that the tax provisions be replaced with funding that provides them greater flexibility to disburse funds.

The Administration's approach adheres to these broad principles. The total amount of relief that will be needed is not yet known, so we need to proceed cautiously to ensure that federal government resources are put to the best possible use. The tax provisions in the GO Zone proposal provide a broad set of incentives that encourage reinvestment in the area. The provisions are broadly applied so that the heavy hand of government is not picking winners and losers. The Administration has also proposed Worker Recovery Accounts to help displaced workers with job training and other needs while they transition back into the workplace and an Urban Homesteading Initiative to help provide a new beginning for lower-income evacuees. In addition, National Emergency Grants totaling more than \$79 million (of an approved \$203 million) have been awarded to date to Louisiana, Mississippi, Alabama and Florida, as well as evacuee states of Arkansas, Georgia, North Carolina, and Texas, to fund disaster relief employment for victims of Hurricane Katrina. These grants also provide job training or retraining and other employment-related services to assist individuals impacted by Hurricane Katrina to find or qualify for new jobs.

3) I am concerned that the proposals that you have outlined in your testimony do not do any thing to help low income individuals. Earlier this week, I introduced legislation that would strengthen the Earned Income Tax Credit. Shouldn't we be trying to help struggling families who are trying to rebuild their lives and isn't the EITC a proven method of helping low-income families?

Answer:

I agree that the earned income tax credit (EITC) has been successful in meeting many of its policy objectives. A number of recent academic studies have found that the EITC encourages work, particularly among single mothers. The EITC also lifts millions of people out of poverty each year. These policy successes have contributed to the President's support of past efforts to expand the EITC and refundable child tax credit. Specifically, he supported provisions to provide marriage penalty relief for EITC claimants as well as to simplify the EITC eligibility rules, contained in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). The President also supported the expansions of the refundable child tax credit contained in EGTRRA and the Working Families Tax Relief Act of 2004.

Expanding the EITC further would be very costly. We should be focusing our limited resources on providing assistance to individuals directly impacted by Hurricane Katrina.

4) In its September 20th meeting, the Federal Reserve indicated that Hurricane Katrina would have short-term economic effects, and would not pose a large threat to economic growth. The Congressional Budget Office indicated in a report that the effects of Katrina could result in the growth of the GDP being reduced between one-half and one percentage point in the second half of 2005 and further states that “economic growth and employment are likely to rebound during the first half of 2006 as rebuilding accelerates.” Do you agree with these views? If so, why do we need to provide tax relief that would benefit investors and businesses that will likely benefit from the rebuilding of the Gulf Region?

Answer:

- **We agree – and hope – that the Gulf Region will quickly begin to rebuild and create a stronger, more vibrant economy.**
- **In its work, CBO has assumed that federal aid is one reason the Gulf economy recovers quickly.**
- **Another, more important, reason the CBO is optimistic is that the economy was strong going into these disasters. The strength in the economy outside the Gulf Region helps to support the ongoing rebuilding effort inside the region.**
- **One reason the economy outside the Gulf Region’s devastation is so strong is that we have lowered tax rates to help entrepreneurs create new businesses and jobs. We have kept those taxes low, and our commitment has allowed businesses and consumers to set their spending and expansion plans accordingly.**
- **So we’re mystified why some people would like to undo those tax cuts, when the effect would be to slow the economy outside the Gulf Region. That would only make it more difficult for the region to rebuild and recover.**

5) The President has indicated that he will work with Congress to find spending offsets to pay for spending related to Hurricane Katrina. Do you know what these offsets are? Are you concerned that certain programs such as Medicaid should not be cut at this time?

Answer:

The Administration does not favor increasing tax rates on other income sources to offset the cost of further tax relief related to Hurricane Katrina. The President has indicated that to the extent possible, hurricane relief should be paid for by reducing spending.

We will work with Congress to identify spending offsets that will free up money for the reconstruction efforts. I applaud the efforts by the Senate Republican Leadership and Budget Chairman Gregg who have requested Committee Chairmen to find additional savings to pay for the costs of Katrina. They asked Committee

Chairmen who received reconciliation instructions to go above and beyond their targets and also asked non-reconciled committees to review policies and programs to find savings.

From Senator Lincoln:

In your testimony you stressed your support for incentives for the private sector to grow and expand to assist in the economic development for the states devastated by the hurricane. One proposal that we should consider is providing relief from the double taxation of the built-in gains tax to enable affected businesses to use their assets in the most productive way – to grow the business and create jobs.

Currently, small businesses that changed their tax status (from C corp to S corp) cannot sell off assets for ten years without being double taxed (a regular tax plus a built-in gains tax). The double tax leads companies to hold unproductive assets much longer than they otherwise would just so they do not have this double tax. This directly affects their cash flow by locking up their assets.

Taking away this double tax is not just important for those small businesses in the Gulf Coast region that want to rebuild. Businesses across the country may be looking to site facilities in that area. Secretary Snow, what do you think about this proposal that will help small businesses sell off unproductive assets and use that cash to rebuild or newly build facilities and create jobs in the areas affected by Hurricane Katrina?

Answer:

While the Administration seeks to encourage private investment in the hurricane disaster areas, we believe that there would be drawbacks to a proposal to eliminate the built-in gains tax for S corporations on sales of assets, the proceeds of which are invested in the areas impacted by Hurricane Katrina.

As you know, the built-in gains tax prevents certain C corporations from becoming S corporations and avoiding the second level of tax on gains accrued while they were C corporations. As long as we have a double tax on corporate income, fair tax policy requires that it be applied evenly. The proposal would treat some corporations that elected S status in the past 10 years more favorably than corporations that continue to be taxed on their income under subchapter C. Moreover, an elimination of the built-in gains tax targeted on assets used for rebuilding after the hurricane would be complex and burdensome for taxpayers, and would be difficult for the IRS to administer.

Other provisions of the Internal Revenue Code already allow businesses to defer the taxes on appreciated property in some circumstances. For example, if a taxpayer receives insurance proceeds for business property destroyed by the hurricane, the taxpayer is often able to reinvest those proceeds in other business property without paying tax. In addition, if a taxpayer holds appreciated property for use in a trade

or business, the taxpayer may be able to exchange that property in a like-kind exchange for other business property without paying tax.

From Senator Kyl:

To encourage rebuilding of businesses, the President has proposed increasing the limits for section 179 small business expensing and new bonus depreciation for larger businesses. As a general matter, I believe businesses should be able to expense immediately all business investments. On this targeted basis, should such tax benefits be made available to entities, such as those in the gambling industry, that have profitable businesses around the country and would likely rebuild their operations without the federal tax incentive?

Answer:

The Administration's proposal for expanded section 179 expensing is targeted to small businesses and to property placed in service in the area affected by Hurricane Katrina. The proposal for bonus depreciation is similarly limited to property used in the active conduct of a trade or business in the impacted area, although it is not limited to small businesses. Excluding profitable businesses from these incentive programs would seriously limit their effectiveness in the rebuilding effort, be difficult to administer, and would create anomalies in their application. Profitable businesses are more likely to use these incentives for sustainable development in the affected area, whereas businesses that have no current Federal income tax liability would not be able to take advantage of the provisions and, in all events, may have more limited resources to contribute to the rebuilding effort.

The President's Gulf Opportunity Zone (GO Zone) proposals will provide immediate relief both to small and large businesses by substantially lowering the tax cost of replacing or rehabilitating property destroyed or damaged in the disaster zone. The widespread devastation in the GO Zone has increased the riskiness of reinvesting in the area. This may be a significant decision factor as firms weigh the costs and benefits of reinvesting in the area, and, indeed, may be a more important factor for the investment decisions of larger businesses, which tend to have more investment opportunities outside of the Gulf region. We believe a temporary, targeted stimulus, as proposed by the President, will lower the tax costs of new investments in the GO Zone, and these lower costs will tend to offset the additional re-investment risk. Bonus depreciation and small business expensing will therefore encourage businesses, both small and large, to undertake the necessary rebuilding projects. Indeed, as mentioned, it is the large business with ample investment opportunities elsewhere that may need the greater tax incentives in order to induce it to remain in the Gulf region.

Statement of Senator Olympia Snowe
Senate Finance Committee
The Future of the Gulf Coast: Using Tax Policy to Help Rebuild Businesses and
Communities and Support Families after Disasters
October 6, 2005

Thank you, Mr. Chairman, for bringing us back together to discuss how we can aid the victims and businesses devastated by Hurricane Katrina. Last week, we heard valuable testimony from Governors Barbour, Blanco, and Riley on how to implement a post-Katrina tax policy that will help rebuild and revitalize the Gulf region. Also at that hearing, it was instructive to understand the effectiveness of past incentives, including those enacted following the September 11th terrorist attacks and the floods in the Midwest. Congress must ensure that we are utilizing those dollars as effectively and efficiently as possible.

The Governors described their daunting challenges in stark detail. Governor Blanco noted that 375,000 Louisiana citizens are out of work, and 71,000 firms have been shuttered or displaced, which is a stunning 40 percent of Louisiana's businesses. Some economists project that Hurricane Katrina could reduce economic growth by as much as a half a percentage point for the remainder of the calendar year. That is why Congress must continually assess the damage and destruction wrought by Katrina and Rita.

I was especially encouraged to see the Governors' strong support for President Bush's proposal for a Gulf Opportunity Zone that would offer a variety of tax incentives for small businesses, including enhanced expensing. This proposal is modeled after the Liberty Zone that the President proposed and Congress enacted for lower Manhattan following the events surrounding September 11th. I look forward to Secretary Snow elaborating on the President's proposals.

Mr. Chairman, without tax and other incentives, small businesses will not have the ability to rebuild their infrastructures and reclaim their competitiveness. As we consider proposals, we cannot ignore or downplay the fact that America's 25 million small businesses create three quarters of all new jobs, and grow at twice the rate of all firms. According to the Office of Advocacy at the Small Business Administration, small businesses provide half of the nonfarm private gross domestic profit. As the President said, it is the small business entrepreneurial spirit that will lead the way in rebuilding the devastated economies of the hurricane affected areas.

I was pleased to hear Governor Barbour and Joint Committee on Taxation Chief of Staff George Yin testify to the value of expensing for small businesses as part of a tax package for the region. I have long championed the ability of small businesses to expense investments in business assets and last year was successful in securing a two-year extension of the \$100,000 expensing limit under section 179. Expensing allows small business owners to have the resources they need to purchase the items necessary to recover their operations and markets. With plant and equipment in place, small businesses can once again begin to deliver goods and services, and new workers can be hired as the Gulf economy gains traction.

President Bush included in his Gulf Opportunity Zone proposal a doubling of the \$100,000 cap. Governor Barbour endorsed this provision and further testified that the cap should be eliminated for a two-year period. Mr. Chairman, I think all options should be on the table and explored by this committee as it looks to formulate its final tax package for the Gulf states.

Mr. Chairman, I believe accelerated cost recovery deductions and bonus depreciation are viable options for a tax package given how they can be tailored to a particular region. Last year Congress passed a 15-year depreciation of leasehold and restaurant improvements. But we need to go further than that in the Hurricane Zone, so small businesses have the cash flow they need to invest in their facilities. We should consider reducing the depreciation period to five years. This incentive is a true job creator on two fronts: it will both help spur the construction industry and allow employees to return to work at rebuilt businesses.

Mr. Chairman, when I visited the Gulf area two weeks ago with the Coast Guard, many of the victims voiced their deep concern for affordable housing. We must keep in mind that when businesses begin operating again and workers return to the area, they will need a place to live. I would like us to consider tax credits to rebuild the housing stock and provide housing for families and individuals. Not only would this incentive help to meet the immediate need of putting roofs over people's heads, but it would also put people back to work. This incentive could work in conjunction with the existing Low-Income Housing Tax Credit, for example.

This Committee should also give strong consideration to a proposal that would exempt from taxation disaster relief payments to a small business. Small businesses should not have to pay a tax on amounts they receive to repair or rehabilitate their facilities or the

contents of those facilities as long as those expenses were not insured. Under current law, such payments accrue tax free to individuals and they should do so for small businesses.

Finally, I could not agree more with Governor Riley when he testified that the Small Business Administration (SBA) is a critical component to the rebuilding effort. I am committed to making sure that the SBA has the resources it needs, is on the ground, and moving as swiftly as possible to assist small businesses in the affected areas get back on their feet. To that end, I introduced last week the Small Business Hurricane Relief and Reconstruction Act of 2005 that builds on my previous proposal to provide immediate and meaningful relief to hurricane victims. Additionally, I've asked the Internal Revenue Service to locate personnel alongside small business personnel in the Gulf region so tax documents required for approval can be expedited to SBA loan-processing departments. Secretary Snow, I would like to thank you and the Commissioner for the positive response that I have received in agreeing to this request.

Mr. Chairman, I look forward to hearing the testimony of our distinguished panel and to working with you and the Ranking Member in creating a comprehensive tax relief package to help rebuild the hurricane-ravaged region. The people of Louisiana, Mississippi and Alabama struggle every day in their quest to return to their pre-Katrina lives. We must do everything possible to help them achieve that goal. Thank you.



Rep. Frank Wolf
Testimony for the Senate Finance Committee
*Using Tax Policy to Help Rebuild Businesses and Communities
and Support Families after Disasters*
Thursday, October 6, 2005

Mr. Chairman, thank you for the opportunity to submit this testimony for the record. My heart goes out to the people of Louisiana, Mississippi and the entire Gulf Coast who have lost so much through the devastation of two hurricanes. New Orleans is working hard to rebuild the infrastructure necessary to once again have a thriving economy. Yet this progress is almost certainly going to be slowed as the city is facing reducing its staff by half.

As we consider how to provide federal assistance to victims of Katrina, it is critical that we make sure that resources are focused on helping these areas rebuild, rather than subsidizing certain self-sustaining industries like the gambling industry.

As you may know, the gambling conglomerates there have already vowed to rebuild "bigger and better" than before. Gambling conglomerates have also been named to the FORTUNE List of 100 fastest-growing companies for fifth consecutive year. Others are looking forward to a banner year in 2005. These were statements from the gambling conglomerates that own casinos in the Gulf region. The vast majority of the casinos in the area are owned and operated by entertainment companies that have been, and are likely to continue, reporting record profits.

With budget deficits growing to historic levels, we need to make sure tax dollars are going to those who truly need the government's help. As Congress struggles to rein in the growth of mandatory spending programs, it doesn't make sense to give expensive special interest tax breaks to gambling conglomerates.

This morning brought news that the two New Orleans public hospitals are destroyed. These hospitals treated more than 500,000 patients a year and will cost hundreds of millions to rebuild. Shouldn't our tax dollars be used to help rebuild critical infrastructure like these hospitals? Resources ought not be squandered on subsidizing the gambling conglomerates with casinos in the Gulf region who have already vowed to rebuild "bigger and better" than before.

A recent *Washington Post* article reported on the administration's plan to provide the gambling industry in the Gulf region with special tax breaks as part of its economic recovery package in the wake of the devastation left by Hurricane Katrina. It was reported that the benefit to just one casino enterprise could reach \$50 million. Tax breaks for the gambling industry, which are reporting billion dollar profits, do not make sense.

I trust you will do the right thing and make sure federal resources go to the poor, the needy and the vulnerable and not the gambling interests who already have insurance to cover catastrophic events like hurricanes. Thank you.

COMMUNICATIONS

STATEMENT FOR THE RECORD

**“THE FUTURE OF THE GULF COAST: USING TAX POLICY TO HELP
REBUILD BUSINESSES AND COMMUNITIES
AND SUPPORT FAMILIES AFTER DISASTERS”**

SENATE COMMITTEE ON FINANCE
OCTOBER 6, 2005

SUBMITTED BY THE AMERICAN CHEMISTRY COUNCIL*

The American Chemistry Council (“ACC”) is an association representing the leading companies in the U.S. engaged in manufacture of chemical products and in research to create products that make life better, healthier, and safer. The chemical industry is essential to all other manufacturing industries. The chemical industry has annual sales of \$516 billion, employees almost a million Americans, and is the largest U.S. exporter.

(1) Hurricanes Katrina and Rita adversely affected the chemical industry, its customers and employees disproportionately:

A large percentage of U.S. chemical manufacturing and research facilities are located in the States devastated by the hurricanes. To this effect, approximately 50-percent of U.S. chemical output occurs in areas declared disaster zones.

Approximately \$35 billion of chemical production takes place in Louisiana alone, in which the chemical industry employs approximately 24,500 people, or over 16-percent of the state’s manufacturing workforce. Other industries in Louisiana and the three adjoining states are major customers for chemical products, to include manufacturing, construction, transportation, trade, and business services.

(2) Scope of hurricane damage:

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Katrina and Rita shut down approximately 70-percent of the chemical facilities in Louisiana, Alabama, Mississippi and Texas. Although half of the facilities in the states are now operating, some are operating at far less than capacity, some are shut down for an indefinite period for repair and rebuilding, and some are damaged so extensively that assessment and engineering studies continue. Significant amounts of production capacity remains unutilized because of breakdown of infrastructure that supplies natural gas to manufacturing facilities, or because the dramatic increases in the cost of natural gas have meant operating losses.

Because of voluntary, self-regulating safety procedures long adopted by ACC member companies, damages and emergency shut-down of member facilities because of Katrina and Rita appear to have caused no environmental damage or threats to safety and health.

(3) Insurance coverage –

Generalizations with respect to property and casualty insurance coverage for an entire industry are difficult. In the chemical industry, each company assesses and responds to risk according to its unique circumstances of vulnerability and financial capacity. Damage from the hurricanes was other than uniform among companies, and companies continue to complete damage assessments and estimates of insurance coverage of damages sustained.

Regardless, it is manifest that the hurricanes have resulted in very significant property losses to the chemical industry, very substantial portions of which are self-insured. Self insurance arises through large “deductibles” or through coverage from a captive insurance company, in both cases with no proceeds forthcoming from third-party insurers. Although insurance coverage from captive companies may include third-party reinsurance, such reinsurance coverage typically occurs only after dramatic levels of loss. (Unfortunately, property damage among certain companies is so great that “catastrophic” third-party coverage may actually be called upon, this in itself a highly unusual situation indicating the enormity of loss arising from the hurricanes.)

Again, at the risk of generalization with respect to an entire industry, it appears that business interruption insurance will provide relatively little to stem operating losses to chemical manufacturers arising because of the hurricanes.

(4) Factors necessary to economic recovery –

Recovery by the chemical industry from the effects of Katrina present two fundamental challenges: (1) Rebuilding infrastructure and the human resources capacity; and, (2) dealing with shortages of and extremely high prices for key materials, in particular natural gas, as both power for manufacturing processes and feedstock for basic chemicals.

(a) Infrastructure –

In the case of the chemical industry, rehabilitation to transportation, power and communications infrastructure must take the following into account:

- Damage to rails, waterways, ports, terminals, highways, bridges and warehouses;
- Lack of power or unpredictable power;
- Interruptions in communications services;
- Dislocation of employees, contractors, and the workforce generally;
- Transportation difficulties for employees and other interruptions in re-establishing employee routine and schedules.

(b) Key material shortages –

The chemical industry depends upon abundant and affordable supplies of natural gas, to power manufacturing facilities and as the basic building block for thousands of industrial and consumer end products. The dramatic loss of natural gas production from Katrina and Rita has the following consequences:

- Shortages and price spikes for consumers and manufacturers;
- Manufacturing production far below capacity for chemical manufacturers, with reduced employment in the four states affected;
- Operating losses for U.S. chemical producers, inability to compete with foreign suppliers of basic chemicals, and, as with the two dot points immediately above, consequent negative effects on employees, customers, and the economy.

(5) Tax initiatives to speed recovery:

In addressing proposals for rebuilding communities that suffered greatly from the hurricane disasters, the Committee places appropriate emphasis on a pragmatic and measured approach, with reference to “effectiveness of past tax proposals.” The ACC endorses Committee adoption of tax measures carefully focused so as to accomplish rebuilding goals quickly and efficiently.

As among business sectors most immediately affected by Katrina and Rita, the chemical industry has examined (1) tax incentives and temporary tax relief measures; (2)

technical issues under the Internal Revenue Code and regulations and rules of the Treasury Department to clarify the law in certain areas and avoid disputes; and, (3) tax policy that addresses the critical need for a natural gas supply that is greater, more diversified and more affordable, a need the hurricanes have so clearly revealed.

(a) Tax incentives and temporary relief measures –

- First-year expensing of capital improvements to renovate, rebuild, or expand manufacturing, administrative and research facilities located within the Katrina and Rita disaster zones. Long experience has confirmed the effectiveness of programs for accelerated cost recovery, with first-year expensing of capital assets providing most beneficial effect.
- Other tax incentives narrowly designed and specifically targeted to assure continuation and speed reconstruction of infrastructure in the disaster areas. Such incentives would include measures to aid in financing infrastructure replacement, refinancing existing debt as necessary, and spreading such costs over an extended period of years.

(b) Clarification –

- Clarification that expenses from site and plant clean-up and disposal of debris and waste in the disaster area do not constitute capital expenditures for environmental remediation or improvements for the betterment of property. Code §§ 162, 167, 263. Also, clarification that clean-up and removal of damaged plant and equipment do not constitute capital expenditures for “demolition of structures” under Code §280B.
- Clarification that physical assistance received by taxpayers from federal, state, or local agencies so as to gain access or as necessary to resume operation of facilities does not constitute income from receipt of services. Further, clarification that government assistance in facilitating business operations does not constitute “contributions in aid of construction.” In absence of such clarification it might be contended that corporate taxpayers realized income from clean-up activities, infrastructure rehabilitation or other disaster remediation work performed by government authorities. For example, removal of debris from a taxpayer’s business facilities, repair of rights of way, or reopening of water channels might be deemed income from receipt of services or capital improvements. Code §§61, 118.
- Clarification that employers may provide grants to individuals, whether or not employees and their families, for assistance from hardship or dislocation from Katrina and Rita, through funds of a private foundation, without action by a formal selection committee of the foundation as to individual grants, and with simplified procedures for exercise of expenditure responsibility. Code §4945.

(c) Natural gas –

As noted above, the shortage of and high prices for natural gas exacerbated by Katrina and Rita have resulted in chemical production below capacity levels. Moreover, price spikes are creating operating losses. Unless such shortages and prices are addressed, delays will occur in economic recovery for the chemical industry and its employees, for customers of the industry dependent on chemical products, and for consumers faced with shortages of chemical-based products necessary to rebuilding in the wake of the disasters. Accordingly, we urge the Committee to address the precarious state of natural gas supply and distribution.

(6) A Separate Tax Policy Issue with respect to Superfund

In its consideration of appropriate tax policy responses to the effects of Hurricanes Katrina and Rita, we urge the Committee to avoid overlap between relief and rebuilding efforts in the Gulf and clean-up activities under the Superfund program. In this regard, emergency borrowing from the Superfund Trust Fund immediately following the attack upon the World Trade Center in September 2001 occurred under circumstances very different than those arising from Katrina and Rita. The matters under consideration by the Committee at the present time are fundamentally different as well. To this effect, the assets of the Superfund Trust Fund should be used solely for addressing Superfund sites currently under remediation and those listed on the National Priorities List in the future.



AMERICAN FOREST & PAPER ASSOCIATION

GROWING WITH AMERICA SINCE 1861

The Future of the Gulf Coast: Using Tax Policy to Help Rebuild Businesses and Communities and Support Families after Disasters

Before the U.S. Senate Committee on Finance

October 6, 2005

**American Forest & Paper Association
Comments for the Record**

The American Forest & Paper Association (AF&PA) is the national trade association for the forest products industry. We represent more than 200 companies and related associations that engage in or represent the manufacturers of pulp, paper, paperboard, and wood products. America's forest and paper industry ranges from state-of-the-art paper mills to small, family owned sawmills and some 10 million individual woodlot owners, including those with operations in the hurricane stricken areas of East Texas, Louisiana, Mississippi, and Alabama. Forestry and forest products manufacturing, along with the numerous suppliers to the industry, drive much of the local economy for many rural communities in these states and across America. In these states, alone, our direct industry payroll accounts for more than \$6 billion of the industry's approximately \$50 billion national payroll.

The forest and paper industry suffered major losses as a result of Hurricanes Katrina and Rita. Private landowners have lost significant value in their timberland, and manufacturing facilities have been affected by power shortages, dislocated employees and, in a few cases, actual structural damage. Nonetheless, the industry is focused on recovery and helping our employees and communities get back on their feet.

Estimates from forest inventories indicate potential timber losses from Hurricane Katrina amount to roughly 4.2 billion cubic feet of timber (15-19 billion board feet); spread over 5 million acres of light to heavily damaged forest land in Alabama, Louisiana, and Mississippi. Additionally, estimates from Hurricane Rita suggest an additional 7.3 billion board feet have been damaged spanning some 1.4 million acres between Eastern Texas and West Louisiana. According to the USDA Forest Service, the downed and damaged wood from Hurricane Katrina is sufficient to produce 800,000 single family homes and 25 million tons of paper and paperboard. Unfortunately, much of that timber is permanently lost and will not be recoverable.

As landowners begin the long process of recovery, they will be faced with high costs for removal of the damaged timber and higher than normal costs for replanting. Typically, the cost of replanting after a normal harvest is in the range of \$150 per acre, but the Mississippi Forestry Association estimates that, in the aftermath of Hurricane Katrina the figure is likely to be closer to \$300 per acre, or twice the

historic average. These reinvestment costs will place significant, increased burdens on individuals and an industry already distressed by the hurricane disasters.

The vast majority of the timber losses occurred on privately-owned land. The tragedy affects timber growers both large and small, from individual tree farmers to small and large businesses. The majority of these timber growers are families and individuals.

Many of these timber growers used these long-term investments in timber as their “nest egg” for financing educational expenses of their children and grandchildren, and their retirement. This tragedy has taken away this nest egg, leaving these timber growers with large economic losses, in many cases representing the totality of their investment, which has been held for many years, sometimes through generations of a family. Additionally, these timber growers face high clean up and reforestation costs, and a pressing need to remove damaged timber, replant the timber stands, and start their investments all over again. The tax law does not recognize these economic losses suffered by timber growers, since the current law casualty loss deduction rules limit tax losses to basis. Historically, timber growers of mature or nearly mature timber stands have a very low tax basis in the timber due to the unique, long term growing periods of the trees. Therefore, many timber growers who have lost most or all of their long term timber investments in these hurricane disasters will not receive any benefit from current law tax provisions designed to provide relief in casualty situations.

Furthermore, these timber growers will only be able to sell a small percentage of their damaged timber and will realize far less than the pre-disaster expectations of the timber growers. Damaged timber quickly deteriorates and loses value due to disease and decay. Experts on the ground suggest that less than 25% of the downed wood will be recoverable. For example, a tree stand intended to be sold as high value saw timber may only be partially useable, and then potentially only for lower value uses such as chips for papermaking, chipped board products or to fuel biomass energy production. Timber that was intended to be used for saw logs is already losing its value due to “blue stain” that has already begun. In a few weeks time, there will be little or no ability to use the downed timber to make solid wood products, unless they have been removed and put into “wet storage” where they can be used a year or 18 months later. Depending on the conditions on the ground, other recoverable timber may retain its usefulness for pulpwood or chipped wood products such as oriented strand board or particle board for a few months, while wood for biomass energy production will have value for potentially as much as two or three years.

This enormous amount of downed timber resulting from the Katrina and Rita disasters poses a serious threat to remaining healthy trees, especially in times of drought. The Department of Agriculture states that in a matter of weeks, a forest health crisis exists in a disaster of this nature. Action needs to be taken as expeditiously as possible in order to reduce the risk of further damage to the timber industry and the regional economy through additional disasters such as wild fires, and the onset of disease and insects which could spread to adjacent undamaged forest lands.

Since this tragedy affected a significant number of individual, small business, and large business timber growers, there is no single legislative tax solution to provide relief for the large number of timber growers who have suffered losses. It is possible, however, to develop and implement a series of tax changes that will be responsive to the severe loss suffered by affected individuals and businesses, while at the same time remaining targeted and effective. We believe the goal of any such legislation should be to provide an encouragement for landowners to keep their land forested rather than chose some alternative use for the land. The availability of long-term term timber supply is essential to the many

forest products manufacturing facilities that exist in the region. With this in mind, we suggest that the following four legislative approaches be taken:

1. Provide an incentive to replace damaged timber stands. Consideration should be given to allow full expensing of reforestation costs (including site preparation) in the disaster area. This proposal would sunset after five years. This proposal would provide an effective incentive to quickly replant the areas damaged by the hurricanes and return this property to productive use. This proposal should be combined with at least a 5-year loss carryback and preferably a 10-year loss carryback.
2. Allow casualty loss deduction for timber economic losses suffered from the hurricanes. Consideration should be given to modifying the casualty loss deduction rules for economic losses suffered from timber damaged by Hurricanes Katrina and Rita. The current law casualty loss rules do not take into account the unique nature of timber, which involves lengthy growing cycles [20 to 60 years depending on the type of tree], risks and hazards that are not insurable, and income realized only when the timber is harvested for productive use. Because the timber tax basis (without regard to the cost of the land) is typically low, the current law basis limitation on casualty losses prevents most timber growers from taking a deduction for their real economic losses. This proposal should be combined with at least a 5-year loss carryback and preferably a 10-year loss carryback.
3. Provide an incentive to remove damaged timber expeditiously. To encourage removal of damaged timber as quickly as possible, consideration should be given to excluding from gross income any gain from timber damaged by Hurricanes Katrina and Rita. This proposal would sunset after five years. The commercial value of damaged timber quickly declines with the passage of time and the cost/benefit of removal of the timber similarly declines. Excluding any gain from gross income would provide an incentive to continue the removal process and alleviate the threat posed from significant amounts of damaged timber to remaining forests.
4. Provide an incentive to expedite the processing of timber. To encourage expedited processing of timber damaged by Hurricanes Katrina and Rita, consideration should be given to easing the restrictions of the section 45 credit for electricity produced from biomass resources. This proposal would suspend the unrelated party sale rules for the incremental additional amount of electricity produced from biomass resources (over prior years) generated by timber processing facilities (such as pulping facilities and saw mills) that are located in Alabama, Louisiana, Mississippi, Texas, and contiguous states. Since it is not economical to transport timber long distances for processing (more than 100 or 150 miles), this proposal would encourage the additional use of biomass for energy production, particularly within the existing infrastructure. The policy benefit of such a proposal is two-fold. First, it will expand the ability of landowners to recover some of the value of their downed timber. This is primarily because the downed timber will have value for the longest time period as a fuel source rather than a raw material for other manufactured products. Second, it will encourage companies to utilize additional biomass for fuel as a replacement of other fossil fuels, including natural gas which is currently at a premium.

We understand that the Committee will be deliberating on a wide number of temporary tax relief provisions aimed at assisting the rebuilding of businesses and communities in the hurricane region. We respectfully submit that the options outlined in this testimony would provide effective relief to all

segments of the timber industry, a major industry and employer in the affected region that has suffered significant losses and disruption. The recommended options would additionally provide effective incentives for expeditious utilization of wasting damaged timber located in the region in order to accelerate essential rebuilding efforts.



October 6, 2005

The Honorable Chuck Grassley
Chairman
Committee On Finance
219 Dirksen Senate Office Building
Washington, DC 20510-6200

The Honorable Max Baucus
Ranking Member
Committee On Finance
219 Dirksen Senate Office Building
Washington, DC 20510-6200

Dear Chairman Grassley and Ranking Member Baucus:

The Mortgage Bankers Association (MBA)¹ commends you for holding today's hearing on using tax policy to help rebuild businesses and communities in the areas battered by recent hurricanes and respectfully request this letter be included in today's hearing record regarding the future of the Gulf Coast.

Since Katrina struck the Gulf Coast last month, MBA has been highly engaged with our members and nonprofit partners in helping to respond to the needs of those households and businesses affected by the storms and flooding. In turn, our members have been focused on their customers and how to provide the financial services they need while easing their burden as much as is possible.

But the mortgage industry will face its own challenges, especially those companies heavily invested in the affected communities. Those challenges include, among others, maintaining liquidity to provide temporary and long-term forbearance to borrowers, dealing with conflicts among insurance companies over coverage, managing properties

¹ The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 500,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,900 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

Chairman Grassley and Ranking Member Baucus
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that have been or will be abandoned, gaining access to properties to perform inspections and emergency repairs and the resulting costs and losses associated with all of these activities.

Above all, the industry wants to see the Gulf Coast region prosper again, and we need to support the infusion of capital to these areas and encourage rebuilding of homes and communities. To that end, MBA respectfully urges the Senate Finance Committee to consider the following tax policy responses.

REMIC Amendments

Congress should include in any tax-related hurricane relief the Real Estate Mortgage Investment Conduit (REMIC) Modernization Act (S. 580 and H.R. 1010). These bills reform the REMIC loan modification requirements, which would benefit real estate owners and tenants, as well as suppliers of real estate design, construction and renovation services. Under these bills, property owners who have suffered damage to their commercial or multifamily structures that are financed through a REMIC would be permitted to rebuild, improve or increase space to suit new or returning tenants without causing the REMIC trust to be engaged as an active business, which alters the tax treatment of the REMIC vehicle. As examples, the changes MBA supports would allow:

- **Preparing Space for Tenants:** Currently, property owners cannot demolish space in order to construct new improvements when such space comprises more than 10% of the total collateral. Violating this requirement could alter the tax treatment of the REMIC. The bills would remove this restriction, while protecting bondholders by ensuring that any modifications will enhance the value of the property.
- **Sales of Outparcels or Pad Parcels:** Under the current REMIC structure, sales of outparcels (sales of excess land) or pad parcels (sales of excess land for retail facilities) may be prohibited if the value of the outparcels or pad parcels are believed to materially alter the collateral. The bills would allow beneficial sales to be made, at the lender's option, to accommodate development of potential small business sites as part of rebuilding efforts in hurricane-affected areas without altering the REMIC tax structure.

Low Income Housing Tax Credits and Mortgage Revenue Bonds

Many of the displaced families are lower income and will need assistance in rebuilding their homes or relocating to affordable housing. The Low Income Housing Tax Credit program could be an effective rebuilding resource and a means of providing new housing for those relocating after the storms. However, an additional allocation of credits will be needed in the affected States over the

Chairman Grassley and Ranking Member Baucus
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next several years, as well as some relief from restrictions against combining the 9% credit program with other federal funds.

In addition the Mortgage Revenue Bond (MRB) allocation in the affected areas should be increased for the next three years to facilitate rebuilding efforts and existing waivers under program regulations for disaster areas should be extended from two to three years. Certain specific restrictions should additionally be waived or relaxed in using MRBs to fund rebuilding efforts. These would include, but are not necessarily limited to the following: the first-time homebuyer requirement, restrictions in using funds for refinancing existing mortgages, and resale price controls on homeowners.

Economic Depreciation

Current IRS Code authorizes 39 years for depreciation of non-residential structures. MBA supports permitting property owners of the Katrina and Rita-affected areas to depreciate their buildings based on the true economic life – just slightly over 20 years on average. Allowing property owners to depreciate their buildings over the true economic life of the asset would encourage economic development and reflect the realities of the asset's utility.

Accelerated Depreciation for Leasehold Improvements

MBA supports allowing a five-year depreciation for leasehold improvements in the hurricane-affected areas, which is analogous to the treatment in the New York City Liberty Zone (for property that was placed in service after September 10, 2001 and before January 1, 2007). Current law, which expires this year, allows for 15-year leasehold improvement depreciation.

Restoration of Contaminated Properties

The situation in New Orleans especially will have sweeping environmental implications. There will be many newly contaminated properties that will fit the Environmental Protection Agency (EPA) definition of brownfields properties. Brownfields are real property, the expansion, redevelopment, or reuse of which may be complicated by the presence of a hazardous substance, pollutant or contaminant. Cleaning up and reinvesting in these properties will take development pressures off undeveloped land and both improves and protects the environment. MBA encourages Congress to provide funding for and permanent extension of the brownfields provisions in current law.

Additionally, MBA supports H.R. 877 and S. 398 that provide for expanded expensing of environmental remediation and clean up costs and broadens the definition of "hazardous substances" to include "toxic substances" (notably, petroleum) contamination. In New Orleans alone, there are currently 66 known

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contaminated petroleum sites and that number is expected to climb into the hundreds. The total number of brownfields sites in post-flood New Orleans will be in the thousands.

Again, we appreciate you holding today's hearing and are grateful for your attention to these recommendations. As we continue to work with our members on the challenges presented in the Gulf Coast region, we might come back to you with additional suggestions. In the meantime, please let me know if we can provide any additional information or be of assistance in any way as the Committee considers the appropriate response for the hurricane victims and their communities.

Sincerely,

A handwritten signature in cursive script that reads "Kurt Pfotenhauer".

Kurt Pfotenhauer
Senior Vice President, Government Affairs

TRAVEL BUSINESS
ROUNDTABLE



A Strategic Partner to 



*Travel Industry Association
of America*

STATEMENT SUBMITTED FOR THE RECORD
BY
THE TRAVEL BUSINESS ROUNDTABLE
AND
THE TRAVEL INDUSTRY ASSOCIATION OF AMERICA

1100 NEW YORK AVENUE, NW
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WASHINGTON, DC 20005

SENATE FINANCE COMMITTEE

HEARING ON

**THE FUTURE OF THE GULF COAST: USING TAX POLICY TO HELP REBUILD BUSINESSES AND
COMMUNITIES AND SUPPORT FAMILIES AFTER DISASTERS**

THURSDAY, OCTOBER 6, 2005

INTRODUCTION

The Travel Business Roundtable (TBR) and Travel Industry Association of America (TIA), on behalf of the entire travel and tourism industry, would like to thank Chairman Grassley and Ranking Member Baucus for convening today's hearing to focus on ways in which tax policy can assist those affected by the destruction of Hurricane Katrina. Our industry strongly supports the relief efforts being made throughout the country and in our nation's capital as the U.S. recovers from one of the greatest natural disasters in its history. We also thank Congress and the Administration for their unwavering commitment to helping the individuals and businesses victimized by Katrina to rebuild. As the Finance Committee continues to formulate immediate and long-term solutions, we as an industry stand ready to assist those affected by the hurricane.

KATRINA'S IMPACT ON TRAVEL AND TOURISM

Overall, in the affected areas of Louisiana, Mississippi and Alabama, the travel and tourism industry accounts for 260,000 jobs and a payroll income of \$3.7 billion. In 2004, the industry generated \$18.3 billion in travel-related sales for the region. The gaming industry in Gulfport and Biloxi generates about \$911.5 million in annual revenues. Last year in New Orleans, more than 10 million visitors spent nearly \$5 billion, representing 44 percent of Louisiana's total tourism revenue and accounting for more than 80,000 jobs.

Travel and tourism was the largest industry impacted by the hurricane, and thus we assume a grave responsibility to our employees, employers and owners recovering from this disaster. Approximately one out of every five jobs in Louisiana, Mississippi and Alabama are travel and tourism specific, and has been impacted by Hurricane Katrina.

In the restaurant industry alone, the 6,800 restaurants and food-service establishments in the areas most heavily impacted by Katrina employed some 90,000 individuals. The gaming industry faced loss of or damage to 18 casinos in the region. Immediately following the hurricane, some 30,000 to 40,000 lodging rooms were unable to be occupied because of damage or because of their location in the evacuated areas. In New Orleans, approximately 200 business conventions have been canceled through December 1.

While the devastation to travel and tourism has been overwhelming, the outpouring of assistance from our industry has been great as well. In addition to donations of money and assistance by the companies and associations making up our industry, TBR and TLA, with industry support and endorsement from the American Red Cross, have launched an online job bank, www.katrinajobs.org, to provide thousands of job opportunities to displaced workers, especially those in the travel and tourism industry.

TAX POLICY RECOMMENDATIONS

While various administrative and legislative initiatives have already been implemented, there will be additional need for tax measures as recovery efforts move forward. The following requests are from our specific industry and are intended to be time-limited and targeted to the FEMA-designated disaster area only. We ask you to keep these in mind as you work through the next round of relief packages during the days ahead.

I. Katrina Disaster Employee Retention Credit

Although the Katrina Emergency Tax Relief Act of 2005 begins to address this area, we encourage the Committee to continue to expand the tax credits for wages paid by loyal employers located in the disaster zone who have continued to pay employees' wages and health benefits while their businesses are non-operational, or in many cases, nonexistent.

II. Housing

- Provide an employer deduction for costs associated with housing relocated employees
- Provide housing credit/allowance/vouchers for employees from the disaster zone
- Provide a tax deduction/credit for costs associated with housing an evacuee/family in your home or business
- Temporary housing provided to Katrina-affected employees by their employers not treated as a taxable benefit

III. Private Activity Bonds

Tax-exempt bond financing for rehabilitation/reconstruction/refinancing of business properties in the disaster zone, combining elements of the Liberty Bond and Enterprise Zone Bond programs to assist all businesses within the targeted zone

- IV. Work Opportunity Tax Credits**
The Katrina Emergency Tax Relief Act of 2005 addresses Worker Opportunity Tax Credits and we encourage the Committee to expand the time-frame of these tax credits to employers within and outside the designated area, due to immediate employment needs and the uncertain timeframe for their return to the affected region.
- V. Leasehold Improvements/Restaurant Depreciation**
Shorten depreciation timeframe to five years for disaster affected-region
- VI. Bonus Depreciation**
Allow 50% deduction for new investment in equipment, buildings and structures
- VII. Small Business Expensing**
Increase small business expensing from \$100,000 to \$200,000 for investment in new equipment
- VIII. Historic Preservation/Rehabilitation**
Allow a 30% tax credit for qualified rehabilitation expenditures to encourage the retention of the unique character of the disaster zone properties
- IX. Tourism Promotion to the Restored Disaster Zone**
To overcome extensive negative images associated with the area, due to extensive international media coverage of destruction, contamination and violence, we suggest:
- Increasing Business Meal Deduction to 100% for expenditures in the disaster zone
 - Restoring the Spousal Travel Deduction for business travel to the disaster zone
 - Creating a tax credit for advertising expenses associated with promoting travel to the disaster areas
- X. Provide Parity in Redevelopment Assistance to Non-Profit Entities**
A growing and substantial amount of the equity investment in the affected region has been funded by nonprofits such as community development corporations, pension funds, and other community-oriented investment trusts.

CONCLUSION

The travel and tourism industry is truly a sum of its many parts, and therefore we have a unique voice during this time of great hardship. We are the locus of economic development in the affected region, and will continue to work with the Administration and Congress to ensure that the people, who have played such vital roles within the Gulf Coast community, and more specifically in our industry, are protected and supported during this time of recovery.

Again, TBR and TIA thank the Committee, other congressional stakeholders and members of the Administration for their consideration of our recommendations and for their commitment to developing sound tax policies that aid the affected region and our industry. For the economic and social benefits to not only this region, but our entire nation, it is essential that the Gulf Coast rebuild and reopen for business as soon as possible.

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Jonathan M. Tisch
Chairman, *Travel Business Roundtable*
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Hyatt Hotels Corporation	USA Today
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International Association for Exhibition Management	Washington D.C. Convention and Tourism Corporation
International Council of Shopping Centers	Waterford Group, LLC
International Franchise Association	World Travel & Tourism Council
	Wyndham International
	Zagat Survey, LLC

The Travel Business Roundtable (TBR), a strategic partner to the Travel Industry Association of America (TIA), is a CEO-based organization representing all sectors of the travel and tourism industry. The mission of TBR is to educate elected officials and policymakers about the importance of the travel and tourism industry to the nation's economy.



**Travel Industry Association
of America**

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TIA is the national, non-profit organization representing all components of the \$600 billion travel industry. With over 2,100 members, TIA's mission is to represent the whole of the U.S. travel industry to promote and facilitate increased travel to and within the United States.